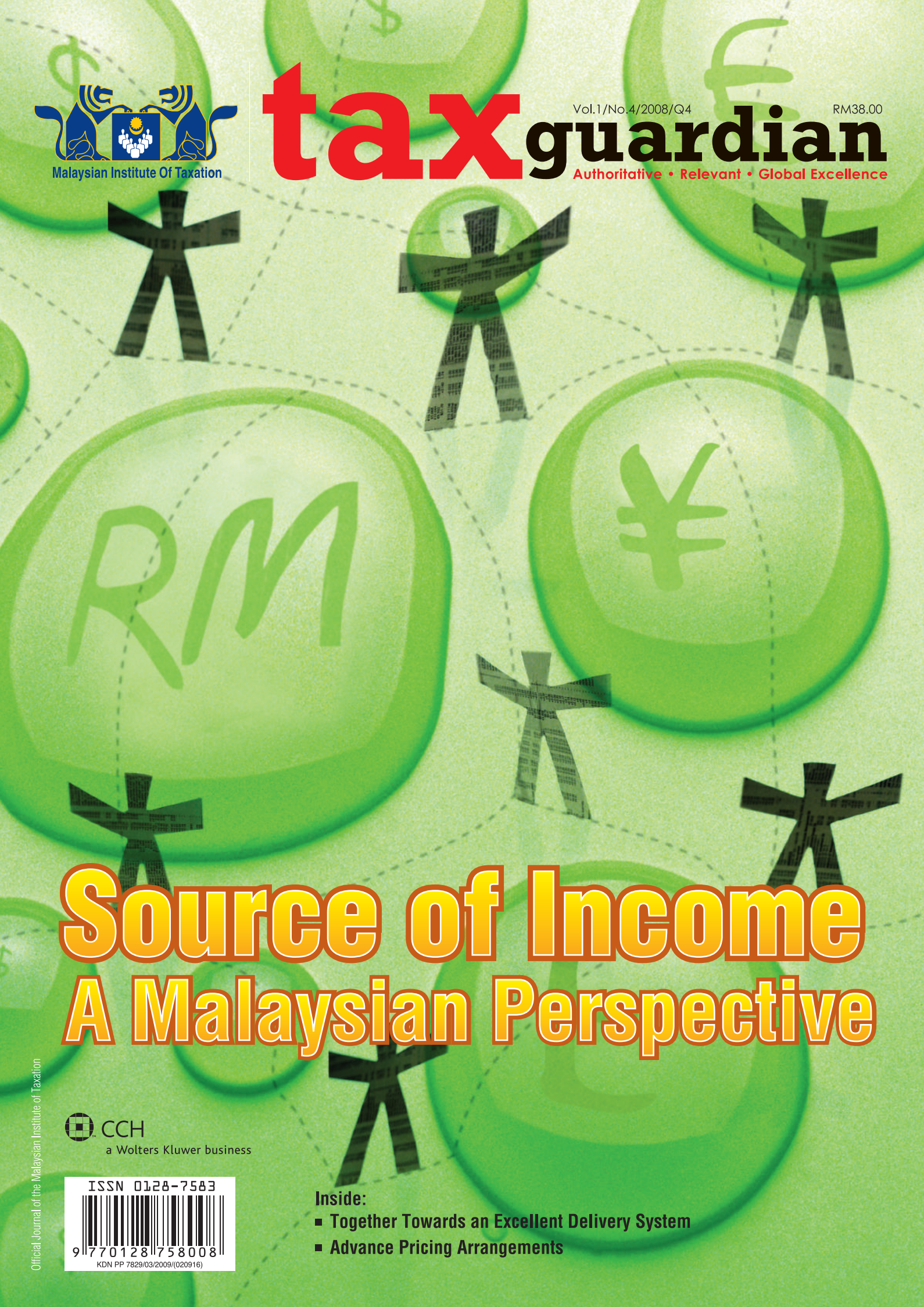
Malaysian Institute Of Taxation

tax guardian

Vol.1/No.4/2008/Q4 RM38.00

Authoritative • Relevant • Global Excellence



Source of Income
A Malaysian Perspective

CCH
a Wolters Kluwer business

ISSN 0128-7583

KDN PP 7829/03/2009/(020916)

Official Journal of the Malaysian Institute of Taxation

Inside:

Continuing Professional Development (CPD)

CALENDAR OF EVENTS 1ST QUARTER 2009

january

Date	Training Programme	CPD Points	Venue	Fee (RM)			Speaker
				Member	Member's Firm Staff	Non-member	
6 Jan 2009 9.00am - 5.00pm	Workshop: Income Reconstruction	8	Ipoh	315	365	415	Abdul Rahim
8 Jan 2009 9.00am - 5.00pm	Workshop: Income Reconstruction	8	Malacca	315	365	415	Abdul Rahim
12 Jan 2009 9.00am - 5.00pm	Workshop: Withholding Tax and Cross-Border Transactions	8	Kuala Lumpur	330	380	440	Chow Chee Yen
13 Jan 2009 9.00am - 5.00pm	Workshop: Income Reconstruction	8	Johor Bahru	315	365	415	Abdul Rahim
15 Jan 2009 9.00am - 5.00pm	Workshop: Income Reconstruction	8	Penang	315	365	415	Abdul Rahim
19 Jan 2009 9.00am - 5.00pm	Workshop: Income Reconstruction	8	Kota Kinabalu	315	365	415	Abdul Rahim
20 Jan 2009 9.00am - 5.00pm	Workshop: Income Reconstruction	8	Kuching	315	365	415	Abdul Rahim

february

5 Feb 2009 9.00am - 5.00pm	Workshop: Corporate Restructuring and Tax Management	8	Kuala Lumpur	330	380	440	Harvindar Singh
13-14 Feb 2009 9.00am - 5.00pm	Workshop: Introduction to Corporate Taxation & Self-Assessment System	16	Kuala Lumpur	630	730	830	Chow Chee Yen
16 Feb 2009 9.00am - 5.00pm	Workshop: Corporate Restructuring and Tax Management	8	Ipoh	315	365	415	Harvindar Singh
17 Feb 2009 9.00am - 5.00pm	Seminar: Tax Cases & Latest Updates	8	Kuala Lumpur	Early bird 375 Normal 425	Early bird 425 Early bird 495	Early bird 495 Early bird 545	Various Speakers
19 Feb 2009 9.00am - 5.00pm	Workshop: Corporate Restructuring and Tax Management	8	Malacca	315	365	415	Harvindar Singh
20 Feb 2009 9.00am - 5.00pm	Workshop: Understanding Deferred Tax for Tax Practitioners (rescheduled)	8	Johor Bahru	315	345	415	Danny Tan
27-28 Feb 2009 9.00am - 5.00pm	Workshop: Introduction to Corporate Taxation & Self-Assessment System (rescheduled)	16	Kota Kinabalu	630	730	830	Chow Chee Yen

march

5 Mar 2009 9.00am - 5.00pm	Workshop: Corporate Restructuring and Tax Management	8	Johor Bahru	315	365	415	Harvindar Singh
10 Mar 2009 9.00am - 5.00pm	Workshop: Latest developments on Transfer Pricing in Malaysia	8	Kuala Lumpur	330	380	440	Chow Chee Yen
16 Mar 2009 9.00am - 5.00pm	Workshop: Latest developments on Transfer Pricing in Malaysia	8	Johor Bahru	315	365	415	Chow Chee Yen
18 Mar 2009 9.00am - 5.00pm	Workshop: Corporate Restructuring and Tax Management	8	Kota Kinabalu	315	365	415	Harvindar Singh
19 Mar 2009 9.00am - 5.00pm	Workshop: Corporate Restructuring and Tax Management	8	Kuching	315	365	415	Harvindar Singh
23 Mar 2009 9.00am - 5.00pm	Workshop: Latest Developments on Transfer Pricing in Malaysia	8	Penang	315	365	415	Chow Chee Yen
26 Mar 2009 9.00am - 5.00pm	Workshop: Corporate Restructuring and Tax Management	8	Penang	315	365	415	Harvindar Singh
27 - 28 Mar 2009 9.00am - 5.00pm	Workshop: Introduction to Corporate Taxation & Self-Assessment System (rescheduled)	16	Johor Bahru	630	730	830	Chow Chee Yen
31 Mar 2009 9.00am - 5.00pm	Workshop: Latest Developments on Transfer Pricing in Malaysia	8	Ipoh	315	365	415	Chow Chee Yen

DISCLAIMER: MIT reserves the right to change the speaker(s)/date(s), venue and/or cancel the events without notice at their discretion.
ENQUIRIES: Please call Ms Latha, Ms Ally or Ms Nur at 03-2162 8989 ext 108, 113 and 106 respectively or refer to MIT's website www.mit.org.my for more information on the CPD programmes.

Be seen in the country's most authoritative Tax journal!

Tax Guardian is the official journal of the Malaysian Institute of Taxation. It provides tax practitioners and professionals in the industry with the latest tax regulatory updates, tax news in Malaysia and around the region as well as analysis of tax issues confronting taxpayers.

Thousands of professionals involved in tax, accounting and industry refer to ***Tax Guardian*** as an important reference point on tax matters on a regular basis.

The ***Tax Guardian*** is an excellent vehicle to showcase your products and services to this segment of successful professionals.

Contact us today to find out how you can advertise on ***Tax Guardian***.

Sean Liew • 012-3963510
• 03-2052 4600 • seanliew@cch.com.my

Consultancy

- Strengthen your brand among the tax professionals in the corporate segment
- Advertise job vacancy
- Relocation announcement
- Seeking strategic alliance announcement

Corporations

- IT solutions
- Health care
- Meeting packages
- Professional courses
- Corporate premiums
- Recruitment services
- Marketing services
- Banking products
- Publications
- Printing services
- Freight and shipping
- Migration services
- Office equipments and furniture
- Events organising and management
- Telecommunication
- Website designing services
- Club membership and facilities
- Car rental and transport services

and many more!

The Malaysian Institute of Taxation ("MIT") is a company limited by guarantee incorporated on October 1, 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 interests 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 effective secretariat.

Institute Address :

The Secretariat,
Unit B-13-2, Block B, 13th Floor
Megan Avenue II, No. 12 Jalan Yap Kwan Seng, 50450 Kuala Lumpur, Malaysia.
Institute Telephone: 603.2162.8989
Institute Facsimile: 603.2162.8990
Institute E-mail: secretariat@mit.org.my

Editorial Note

Seasons of change – that certainly seems to be the phenomenon sweeping the world in an unprecedented fashion in all arenas, be it economically, politically, socially, environmentally – and the thing one cannot afford to do is to ignore it. It is at times like these that it would serve us well, individually and collectively, to contribute in such a manner as to drive the change in a positive, substantial, and far-reaching direction.

The MIT continues its efforts in achieving just that in the area of taxation, and no better time than the present to foster collaborative effort; promote clarity, consistency and sound policies; and promote the convergence of interests between taxpayer and government towards enhancing economic resilience.

We trust you'll find this issue of *Tax Guardian* filled with relevant, authoritative articles that would also prove interesting reading. Our cover article, "Source of Income – A Malaysian Perspective" highlights an issue that has been at the heart of many a debate. Tax cases across comparative tax regimes are discussed; and approaches to the determination of source of business income, dividend, interest, royalty and other income are set out.

A discussion on Advance Pricing Arrangements is included on page 26, which now provides taxpayers an opportunity to carry on their related party transactions across borders with certainty. This will relieve both the tax payers and the Inland Revenue Board from utilising their limited resources to deal with lengthy transfer pricing audits and provide the Inland Revenue Board with a steady stream of tax revenues.

As well, presented as a feature article, are the current trends and issues in Malaysian tax incentives for Islamic finance, an area of increasing importance and interest globally. The laudable objectives and efforts of *PEMUDAH* are highlighted in the article "Together Towards an Excellent Delivery System".

Get to know your council members in the second and final part of our compilation of individual profiles and members' contributions to the Institute. Our quarterly segments of technical updates and case updates bring you the latest developments in tax law, including statutory orders gazetted to give effect to the 2009 budget proposals.

On a lighter note, it has been said that the art of taxation consists in so plucking the goose as to obtain the largest amount of feathers with the least amount of hissing *(Jean-Baptiste Colbert)* – perhaps our efforts will go some way in making this symbiotic relationship one of reciprocal harmony.

SM Thanneermalai
Chairman
Editorial Committee

Table of Contents

Note : The views expressed in the articles contained in this journal are the personal views of the authors. Nothing herein contained should be construed as legal advice on the applicability of any provision of law to a given set of facts.

INVITATION TO WRITE

The Institute welcomes original contributions which are of interest to tax professionals, lawyers and academicians. They may cover local or international tax developments. Article contributions should be written in UK English. All articles should be between 2,500 to 5,000 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.

Contributions may be sent to:

The Chairman, Editorial Committee
Malaysian Institute of Taxation
Unit B-13-2 Block B, 13th Floor
No.12 Jalan Yap Kwan Seng
50450 Kuala Lumpur
Malaysia.
E-mail: publications@mit.org.my

tax
Authoritative • Relevant • Global Excellence

Tax Guardian is the official journal of the Malaysian Institute of Taxation and is distributed to members and students of the MIT as well as subscribers, both corporate and individual. The contents of Tax Guardian do not necessarily reflect the views or opinions of the MIT and no liability is accepted in relation thereto. MIT does not accept liability for any views or opinions published herein. Advertisements appearing within this journal should not be taken to imply any direct support for or sympathy with the views and aims of MIT.

Publishing Consultant

CCH
a Wolters Kluwer business

For the past 20 years, CCH has been The Professional's First Choice for information, tools and solutions that help professionals make their most critical decisions. The CCH brand has been a market leader since 1913 and five generations of professionals have considered CCH products among the essentials in any office and critical to keeping up with day-to-day changes in the law and practice. It is one of the most respected names among tax professionals, accountants, attorneys and compliance professionals. Over these years, CCH has provided a wide range of high quality contents be it online, in print, software and training for professionals in Asia focusing in the following areas:

Tax & Accounting • Human Resource • Legal • Business

CCH Office : Commerce Clearing House (M) Sdn Bhd
Suite 9.3, 9th Floor, Menara Weld,
76, Jalan Raja Chulan, 50200 Kuala Lumpur,
Malaysia.
☎ : 603.2052.4688
: 603.2026.7003
✉ : support@cch.com.my
: www.cch.com.my
Advertising Enquiry : Commerce Clearing House (M) Sdn Bhd
Designer : DNA Red Services
Printer : Line & Tone Sdn Bhd

Know Your Council Members

Mr Khoo Chin Guan
Vice President

Khoo Chin Guan is the Executive Director – Head of Tax of KPMG Tax Services Sdn Bhd with over 26 years of tax experience. He advises clients in a wide range of industries on tax planning, tax audits, mergers and acquisitions, tax structuring and in-bound and out-bound investments.

Khoo is a Fellow Member of the Malaysian Institute of Taxation and the Chairman of its Technical and Public Practice Committee. In addition, he is an approved tax agent licensed by the Ministry of Finance.

Khoo is also a Fellow Member of the Association of Chartered Certified Accountants, United Kingdom. He also holds membership of the Malaysian Institute of Accountants and the Malaysian Institute of Certified Public Accountants.

Khoo is currently the External Examiner of the Malaysian Tax papers of the Advanced Diploma in Commerce courses offered at the Tunku Abdul Rahman College in which he is an alumnus.

As a Council Member, Khoo aspires to enhance the status of the Malaysian Institute of Taxation as the premier body in the field of taxation in Malaysia through his involvement as the Chairman of the Technical and Public Practice Committee.

Mr Adrian Yeo Eng Hui
Council Member

Raised in Kuching with a humble family background, Adrian Yeo established his first accounting career and obtained an MBA in London after obtaining his ACCA qualification. Upon his return to Kuala Lumpur, he worked with KPMG.

Today, Adrian runs an accounting firm in Petaling Jaya.

Adrian is active socially. He is the Secretary General for TAR College Alumni and Chairman of the ACCA Public Practice Committee. He speaks regularly on topics of simple finance and taxes to Small Medium Enterprises (SMEs).

A simple man at heart, Mr Adrian Yeo always wears a smile with his trademark orange attire. He is a keen reader and writes for a Chinese magazine on Entrepreneurship. Recently, his firm Adrian Yeo & Co won the Enterprise 50 award.

As the Chairman for MIT's Membership Committee, Adrian's priority is to work with its Public Relations Committee to uplift the image of the MIT and status of its members.

Dr Ahmad Faisal Zakaria
Council Member

Dr Ahmad Faisal Zakaria obtained his Doctorate of Philosophy (PhD) from the University of Hull, England and Master of Business Administration (MBA) from Southern New Hampshire University, New Hampshire, USA.

He is currently a Fellow member of the Malaysian Institute of Taxation, Malaysian Society of Accountants and the Association of International Accountants, UK. He is also a Licensed Accountant registered with the Malaysian Institute of Accountants.

Dr Faisal started his career as an Accountants Examiner with the Audit Division of the Cooperative Department of Malaysia. He then worked as an Assessment Officer with the Inland Revenue Board of Malaysia (IRB) and was assigned to the National Tax Academy as a Research Officer upon his completion of a doctorate degree in the UK. Dr Faizal was also attached to Perwira Affin Bank as a Tax Manager.

Currently, Dr Faisal runs his own consultancy firm known as AHMADFAISAL, which specialises in taxation and cooperative auditing. He was also appointed as a Director and audit committee member of a public listed company. Currently, Dr Faisal sits on the Board of the Advising Committee of Politeknik Sultan Azlan Shah, Behrang, Perak.

As a Council Member, Dr Faisal hopes to contribute to the Institute by improving the education section of the Institute and increasing student numbers in MIT's Examinations.

Part 2

Mr Aruljothi Kanagaretnam
Council Member

Mr Aruljothi Kanagaretnam holds a Masters in Business Management from Trinity University, UK. He has extensive experience in taxation having served the Inland Revenue Department/Inland Revenue Board (IRB) for 39 years. During this period, he served in various branches including the Investigation Unit.

When the Self-Assessment System (SAS) was introduced, Aruljothi played an important role in the formation of the Processing Centre, where he served as the Deputy Director. After his retirement in 2005, he continued to serve the IRB for another three years up to March 2008 to help see the smooth implementation of the SAS.

Aruljothi has been actively involved in organising international tax conferences such as the Commonwealth Association of Tax Administrators' Conference (CATA) and the Study Group on Asian Tax Administration and Research (SGATAR). He has spoken at various National Budget Tax Seminars organised jointly by the IRB and the Inland Revenue Officers' Union. He has also participated as a Malaysian Delegate at international tax conferences. He is currently a Consultant at VPI International.

As a Council Member of the Malaysian Institute of Taxation, he hopes to use his past experience to forge better relations and understanding between MIT and the relevant authorities.

Mr Chow Kee Kan
Council Member

Mr Chow Kee Kan, or better known as K K CHOW, is an approved auditor and chartered accountant. He started his own practice in 1984 after 10 years of working experience. In total, he has more than 30 years of practical experience in accounting, taxation and corporate management consultancy.

Chow is a MII certified trainer, and lectures widely (both in English and Mandarin since 1980) in courses conducted by colleges and universities.

Chow is also a Fellow Member of the Association of Chartered Certified Accountants, United Kingdom. He also holds membership of the Malaysian Institute of Accountants.

He was one of the pioneer council members of the Malaysian Institute of Accountants (MIA).

At present, he is a Trustee of the Malaysian Accountancy Research and Education Foundation (MAREF).

He is also an Independent Director of two main board public listed companies.

As a Council Member, his priority is to promote MIT to the Chinese community while maintaining its status in the tax industry.

Mr Neoh Chin Wah
Council Member

Mr Neoh Chin Wah is the managing partner of AljeffriDean, a member firm of MGI International and the president of AljeffriDean Affiliated Accounting Firms in Malaysia.

He was one of the pioneer council members of the Malaysian Institute of Accountants (MIA) in the reactivation years initiated in 1987 and has served in the MIA Council for 14 years. He is an approved trainer for the Directors' Training programme of the Malaysian Companies' Commission and speaks at seminars frequently. Currently, he is on the Board of Trustees of the Malaysian Accountancy Research & Education Foundation as well as the Audit Committee Chairman of APP Industries Berhad.

Neoh is a Fellow Member of the Chartered Association of Certified Accountants, an Associate Member of the Institute of Chartered Secretaries and Administrators and is a Certified Financial Planner.

Neoh hopes to contribute to MIT by sharing his working experience of over 30 years both in the Inland Revenue and private practice. Practising as auditor, liquidator and tax consultant at the same time, he hopes to bridge the gap in the different disciplines when deliberating tax issues. He helped to draft the amendments to the Institute bye-laws which was passed in the recent AGM.

As a Council Member, his priority is to assist in focusing on the Institutes activities to help build the Institute into "a body that members can be proud of."

Mr Peter Lim Thiam Kee
Council Member

Mr Peter Lim Thiam Kee is the Managing Partner of T K Lim & Associates, Chartered Accountants. He has an accounting degree, associateship in commerce and associateship in accounting from Curtin University, Western Australia. He is a fellow member of The Institute of Chartered Accountants in Australia, Institute of Chartered Secretaries and Administrators (London), Certified Practising Accountants (Australia) and a member of the Malaysian Institute of Certified Public Accountants.

He is the Chairman of The Chartered Accountants in Australia, Malaysia Chapter and is also a member of the International Federation of Accountants (IFAC), Small Medium Practices Committee. In addition, he is also a Council Member of the Malaysian Institute of Chartered Secretaries and Administrators, the Malaysian Institute of Accountants and Malaysian Institute of Certified Public Accountants.

Peter has over 30 years' experience as a general tax practitioner, audit assurance and management consultant. He also served as an examiner and chief examiner for certain papers for 20 years for the Malaysian Institute of Certified Public Accountants.

As a Council Member, he hopes to work closely with fellow council members to:

- meet the objectives of the Institute and the professional needs of its members;
- improve the Institute's working relationship with all the regulators and other professional bodies to achieve common interests.

Tuan Haji Ab Rahim b Abdullah
Council Member

Tuan Haji Ab Rahim b Abdullah holds a Bachelor degree in Economics from the University of Malaya and Master Degree in Taxation from the Golden Gate University, USA. During his 31-year tenure as a government officer in the Income Tax Department (IRD), he held several key positions which included as the Director of several branch offices including Sabah and Sarawak, the Director of the Investigation Branch (Northern Region), the Director of National Tax Academy (now known as Malaysian Tax Academy) and the Director of Corporate Services Department. His last held position before his retirement was the Director of IRB Sarawak.

Tuan Haji Ab Rahim has contributed significantly to the development of the IRD (Inland Revenue Board as it is today), including the development of the current Self-Assessment System. He has also contributed tax articles and prepared seminar papers for both national and international levels.

He is currently the Managing Director of ARA Tax Consultant Sdn Bhd and a tax adviser cum Director of Procellence Management Sdn. Bhd. His areas of specialisation are in Tax Investigation, Tax Audit and Tax Planning.

Tuan Haji Ab Rahim is an appointed Council Member of Malaysian Institute of Taxation. He is also a council member of Malaysian Association of Company Secretaries (MACS) and Institute of Corporative and Management Accountant (ICMA). He conducts tax seminars and workshops on a regular basis nationwide for MACS and ICMA and has published selected articles for MACS.

Mr Francis Tan Leh Kiah
Council Member

Mr Francis Tan graduated with LL.B from the University of London and was called to the Malaysian Bar in 1986. He is a Solicitor of the Supreme Court of England & Wales, an Associate Member of the Institute of Chartered Secretaries and Administrators and the Malaysian Institute of Taxation.

Francis who is an appointed Council Member of the Malaysian Institute of Taxation, is currently the Managing Partner of Azman, Davidson & Co, Advocates and Solicitors. He has over 20 years of working experience with the Government and the private sector. He served as an Assistant Registrar of Companies in the Registry of Companies of the then Ministry of Trade and Industry from 1972 to 1976. After leaving the government service, he became the Group Company Secretary of a large group of companies from 1977 to 1985. In 1986, he joined Azman, Davidson & Co as its Managing Partner.

He has been a member of the Securities Commission of Malaysia since May 1999. Prior to his appointment as a member of the Securities Commission, he also served as a director of several public listed companies.

Mr Mokhtar Mahmud
Council Member

Mr Mokhtar Mahmud graduated with a Bachelor of Social Science degree from Universiti Sains Malaysia. He also holds an MBA from New Hampshire College, as well as the ITP from Harvard University.

Mokhtar joined the Customs Department in 1973 and has served at state level in various divisions of the Department in Johor Bahru and Singapore, as well as served as a lecturer at the Customs Training College. He also served in the Internal Tax Division at the Customs Headquarters and has wide exposure in both operational and policy-making functions. He was an examiner for the compulsory departmental examination for customs officers. After having served 23 years, Mr Mokhtar went on optional retirement in 1996 to take up employment as a Managing Consultant in the Indirect Tax Advisory Group, PricewaterhouseCoopers. He then left PwC to set up Top Tier Services Sdn Bhd in 1998 and is now involved in rendering consultancy services in indirect tax matters.

As an appointed Council Member of the Malaysian Institute of Taxation, he hopes to contribute his vast experience and knowledge to the Institute in order that it continues to be the premier tax body in Malaysia.

News on Branches

MELAKA BRANCH

Majlis Berbuka Puasa with Yang Di Pertua Negeri Melaka

The MIT Melaka Branch Committee members were invited to a Majlis Berbuka Puasa Dinner by His Excellency Yang Di Pertua Negeri Melaka Tun Datuk Seri Utama Mohd Khalil b Yaakob at Istana Melaka on 19 September 2008.

Melaka Branch Committee members and Tun Datuk Seri Utama Mohd Khalil.

SARAWAK BRANCH

Members' Dialogue

A Members' Dialogue for the Sarawak branch was held on 14 September 2008. MIT Council Member Mr Lew Nee Fook met with members to discuss various issues of interest.

On 15 September 2008, the Branch Committee members and Mr Lew visited IRB Sarawak Branch to foster a closer working relationship.

Sarawak members with Mr Lew Nee Fook.

PERAK BRANCH

Members' Dialogue

The MIT Perak Branch held a dialogue with members in the Greentown Business Centre on 5 November 2008. During the dialogue, various operational issues were discussed by members. These issues will form the basis for a future dialogue with the IRB Perak Branch.

Ipoh members with Mr Lam Weng Keat.

EAST COAST BRANCH

Members' Dialogue

MIT's East Cost Branch members had a dialogue with the President of the Institute, Dr Veerinderjeet Singh on 1 November 2008 at M.S. Garden Hotel. About 54 members and tax practitioners from Kelantan, Terengganu and Pahang attended the dialogue. There was a good exchange of views and ideas. Various suggestions were also presented to the President on practice matters.

Participants paying full attention at the MIT Dialogue.

MIT East Coast Branch Annual Dinner

MIT East Coast Branch Annual Dinner.

Sitting L to R: Mr Chakngari @ Yusof bin Daud, Director of IRB, Temerloh Branch; Mr Ammar bin Johari, Director of IRB, Kuala Terengganu Branch; Mr Mat Lazim bin Salleh, State Director for Pahang, Terengganu and Kelantan; Dr Veerinderjeet Singh, President of MIT; YB Chang Hong Seong, Representative of Guest of Honour; Mr Wong Seng Chong, Chairman, MIT East Coast Branch; Mr Marzelan bin Kamaruddin, Director of IRB, Kota Bahru Branch; Mr Termizi bin Embong, Director of IRB, Kuantan Branch, Investigation & Intelligence Centre and Ms Wan Fauziah bt Wan Daud, Director of IRB, Raub Branch.

Standing L to R: Mr Chan Liang Chuang, Mr Ooi Boon Seng, Mr Yau Hun Ling, Mr Eddie Eries, Dr Yap Kim Fay, Mr Mohd Ali Abas, Mr Yeo Chin Meng and Mr Wang Fook Fok

L to R: Director of Federation of Malaysian Manufacturers, Eastern Region, Datuk Hj Mas'ut B A Samah, Organising Chairman, Mr Wong Seng Chong, Director of IRB Kota Bahru Branch, Mr Marzelan B Kamaruddin, Director of IRB Temerloh Branch and Mr Chakngari @ Yusof B Daub.

The MIT East Coast Branch held its Annual Dinner in Kuantan on 1 November, 2008 at M.S. Garden Hotel. The Guest of Honour was YB Chang Hong Seong, The Assemblyman for Teruntum who represented the Deputy Minister of Finance, YB Datuk Kong Cho Ha.

The dinner was attended by the State Director of the Inland Revenue Board (IRB) for Pahang, Terengganu and Kelantan, Mr Mat Lazim Bin Salleh as well as the Directors of the Kelantan, Terengganu, Kuantan, Temerloh and Raub IRB Branches. In addition, various other officials from the Companies Commission of Malaysia (CCM), Malaysian Industrial Development Authority (MIDA), Ministry of International Trade and Industry (MITI), National Audit Department, Accountant General's Department, Chamber of Commerce, the Pahang Bar, bankers and prominent local industrialists were in attendance.

The President of MIT, Dr Veerinderjeet Singh presented certificates of appreciation to various sponsors and donors. Guests received door gifts and were entertained with songs. 10 winners walked away with prizes during the lucky draw session.

The President of MIT, Dr Veerindeerjeet Singh and MIT East Coast Branch Chairman, Mr Wong Seng Chong at the MIT Members' and Practitioners' Dialogue.

L to R: Dr Veerindeerjeet Singh, Mr Wong Seng Chong, Mr Chan Liang Chuang.

State Director of East Coast, IRB, Mr Mat Lazim giving away a hamper to a lucky draw winner.

CPD Event News

Seminar on Tax Planning

Datuk Naban, one of the key speakers.

Ms Wong Yok Chin, one of the invited speakers.

Mr Mokhtar Mahmud spoke on Indirect Tax Planning.

On 23 October 2008, the Institute conducted a seminar on Tax Planning at Putra World Trade Centre, Kuala Lumpur which was chaired by Dr Ahmad Faisal, Council Member of MIT. The speakers for the morning session included Datuk D.P. Naban who spoke on "Is tax avoidance permitted in Malaysia?", followed by Ms Wong Yok Chin on "Corporate tax implications on mergers & acquisitions". The session continued with Mr Amarjeet Singh who spoke on "Issues to consider in structuring offshore investments".

The sessions continued into the afternoon with Mr Saravana Kumar on relief from stamp duty on mergers and acquisitions and Mr Mokhtar Mahmud speaking on indirect tax planning.

During the question and answer session, many interesting and challenging questions were raised and addressed.

Dr Ahmad Faisal, Council Member of the MIT chaired the seminar.

Participants of the seminar.

Speaker, Mr Amarjeet Singh and MIT's technical manager, Mr KS Lim.

Speakers, Ms Wong and Mr Mokhtar.

Visit by the Kenya Delegation

Delegates from the Kenyan Accountants and Secretaries National Examinations Board (KASNEB) visited the Malaysian Institute of Taxation on 14 October 2008. The purpose of the visit was to gather information relevant to the review of the Kenyan examination syllabuses and the administration of their examinations. The delegation was headed by Mr Joe M. Mbuthia, Mr Erasto N. Mukuria and Mr Bernard M. Njiru. The MIT Council members who were present during the visitation were Dr Veerinderjet Singh, Mr Aruljothi and Dr Ahmad Faisal.

The members of the Kenyan delegation listening to the briefing.

Mr Aruljothi Kanagaretnam, Ms Nancy Kaaur, Dr Ahmad Faisal, Ms Ann Vong, Mr Erasto N.Mukuria, Dr Veerinderjeet Singh, Mr Joe M.Mbuthia and Mr Bernard M. Njiru.

Dr Ahmad Faisal, Mr Joe M. Mbuthia and Dr Veerinderjeet Singh.

Source of Income - A Malaysian Perspective

By SM Thanneermalai, Lim Phaik Hoon and Dr Nakha Ratnam Somasundaram

With globalisation, businesses are now borderless and hence the determination of the source of income has become more complex. The article discusses the various approaches to determine the source of income.

The issue of source has been a subject matter of discussion since the introduction of the *Income Tax Act in 1967* and despite legislation being introduced from time to time attempting to contain the area of ambiguity, this still remains an area for interpretation. This is because the determination of source of income is an issue which is dependent on the facts surrounding each case and guidance has to be sought from the vast body of case law found locally and overseas.

Over the years, numerous judgements have created new tests, which have led us further away from certainty. However these judgements have acknowledged that the ascertainment of the actual source of income is a "practical hard matter of fact" and there is no simple legal test to guide us. The phrase "practical hard matter of fact" does not help reach a simple solution without delving into the facts surrounding each case and the legal precedents on this subject matter.

An example where this issue comes to life and reminds us of the level of complexity involved is in the world of e-commerce. With e-commerce paving the path of today's businesses and cross-border transactions rising with globalisation, the ascertainment of taxable source of income within any jurisdiction is an ever present challenge to tax authorities all over the world. The Malaysian tax authorities have not been spared such a challenge. Similar to other tax jurisdictions faced with this challenge, tax in Malaysia is charged on a territorial basis in that only income accruing in or derived from Malaysia is liable to tax (local sourced), while income remitted to but earned outside Malaysia (foreign sourced) by a resident Malaysian corporation (other than a resident company carrying on the business of banking, insurance or sea or air transport) is exempt from income tax: s 3 read in conjunction with para 28 of Sch 6 of the *Income Tax Act 1967*, (ITA).

The question then arises: what is local sourced income (which is subject to Malaysian tax) and what is foreign sourced income (which is exempt from tax in Malaysia)? This then leads to another question: how is the source of an income stream determined in Malaysia for taxability purposes?

The Malaysian income tax legislation prescribes an extensive list of the types of income subject to tax in Malaysia under s 4 ITA. Some of these income streams have specific derivation rules prescribed to assist in the determination of its taxability. The type of income streams and its corresponding derivation sections under the ITA are listed as follows:-

Section	Sources of Income	Derivation Section
4(a)	Gains or profits from a business	12
4(b)	Gains or profits from an employment	13
4(c)	Dividends Interest Discounts	14 15 -
4(d)	Royalties Rents, Premiums	15 -
4(e)	Pensions Annuities and other periodical payments	17 -
4(f)	Gains or profits not falling under any of the foregoing paragraphs ("Other Income")	15B, Finance Bill 2008
4A	Special Classes of Income	15A

In this article, the types of income that will be discussed, in relation to the determination of its source, will be restricted to the following types of income:-

(a) Business gains or profits;
(b) Dividend income;
(c) Interest income;
(d) Royalties;
(e) Other income

In addition, the article only covers the domestic legislation and excludes Double Taxation Agreements (DTA) matters.

Business gains or profits (business income)

As a general rule, the taxability of all income including business income is prescribed by s 3 of the ITA which specifies that income is taxable in Malaysia only if the income is derived from or accrued in Malaysia. With particular regard to business income, s 12 of the ITA articulates the specific derivation rules.

S 12 ITA is a deeming provision - it deems whatever 'gross income that is not attributable to operation of business carried on outside Malaysia' to be derived from Malaysia. The wording of s 12(1)(a) ITA therefore maximises the scope of charge for business income and serves as a catch - all residual section.

Hence, in relation to the taxability of business income, the distinction that needs to be made is not merely one of foreign business income versus local business income but a further distinction as between foreign business income attributable to a particular jurisdiction and foreign business income deemed to be derived from Malaysia.

In today's e-commerce businesses where trade is conducted online and activities within a single business are conducted in several countries, how does one identify where the business profit is actually being sourced? And how does one make the distinctions?

Generally, businesses and tax practitioners tend to use certain guiding factors from case law and acceptable conventional business practice to determine where a business profit is sourced. These factors among others include:

(i) where a contract is entered into
(ii) where services are rendered
(iii) where the control and management of a business is exercised, and
(iv) where the product is produced.

> … the guiding principles, namely to look at what the taxpayer had done to earn the relevant profits and where it had been done in order to determine where the source of business profits have been derived.

As for the first two points above, reference is made to the case of *Aneka Jasaramai Express Sdn Bhd*. This case involved a bus company that operated in both Malaysia and Singapore and the source of the income from sale of tickets in Singapore was in question. The High Court held that there was ample evidence to show that the contract of sale of tickets took place in Singapore and where payments were also received, and therefore the income from the sale of those tickets sold in Singapore did not accrue in or derive from Malaysia.

In *R.O. Drilling Co. Ltd*, a Malaysian case in relation to the issue of control and management as a determining factor of source of business profits, the Special Commissioners of Income Tax (SC) decided that the charter fees earned by a Hong Kong resident from a Malaysian incorporated company for offshore drilling in Malaysian waters was attributable to business carried on outside Malaysia as the central management and control of the company was exercised outside Malaysia. The area where the business substance — ie business acumen, business judgement, business intuition, business knowledge and business experience — are exercised and employed is where the central management and control actually abides, and this factor is more important than the physical manifestations of business activities in terms of time and space.

The issue of where the product is produced is corroborated by s 12 (1)(b) of the ITA which specifically prescribes that income from certain businesses such as manufacturing, agriculture and mining will be deemed to be derived from Malaysia regardless of where the sale of the article is ultimately made. Under s 12(1)(b) ITA therefore, business income will be seen to be locally sourced if the product traded is wholly or partly produced in Malaysia.

The interpretations to be given to s 12 ITA then leads to a host of uncomfortable questions: Does this mean that we can conclude that the profits of a business that is based in Malaysia but contracted in Hong Kong for example, is sourced from Hong Kong, and therefore not taxable in Malaysia? Where then is the source of profits of a business which concludes its sales and purchase contracts online? How about a business that renders services in two different

countries — can the profits be equally attributable to both countries? Is documentary evidence sufficient to determine the business profits source?

Operations test

The questions posed above are the types of questions that have made it impossible for the courts to prescribe definitive legal tests to address the issue of the source of business profits. As there is only limited precedence in Malaysia in relation to source of profits determination, direction is further sought from Hong Kong which has very similar source of profits rules as Malaysia. The operative s in Hong Kong is s 14 of the Hong Kong Inland Revenue Ordinance (as at 2007), which provides as follows:-

> "(1) Subject to the provisions of this Ordinance, profits tax shall be charged for each year of assessment at the standard rate on every person carrying on a trade, profession or business in Hong Kong in respect of his assessable profits **arising in or derived from** Hong Kong for that year from such trade, profession or business (excluding profits arising from the sale of capital assets) as ascertained in accordance with this Part."

The leading cases on the source of profits are *Hang Seng Bank Ltd* and *Orion Caribbean Ltd* which laid down the guiding principles, namely to look at what the taxpayer had done to earn the relevant profits and where it had been done in order to determine the source from which business profits were derived. This test is also known as the 'operations test'.

In the *Hang Seng Bank* case the Privy Council held that the income generated from trading in certificates of deposits on the Singapore and London markets were not profits arising or derived from Hong Kong, and therefore not liable to tax in Hong Kong. It was held that:

> *"Their Lordships were referred in the course of the argument to many authorities on different taxing statutes in different common law jurisdictions raising a variety of questions as to the geographical source to which income or profits should be ascribed. But the question whether the gross profit resulting from a particular transaction arose in or derived from one place or another is always in the last analysis a question of fact depending on the nature of the transaction. It is impossible to lay down precise rules of law by which the answer to that question is to be determined. The broad guiding principle, attested by many authorities, is that one looks to see what the taxpayer has done to earn the profit in question. If he has rendered a service or engaged in an activity such as the manufacture of goods, the profit will have arisen or derived from the place where the service was rendered or the profit making activity carried on.* ***But if the profit was earned by the exploitation of property assets as by letting property, lending money or dealing in commodities or securities by buying and reselling at a profit, the profit will have arisen in or derived from the place where the property was let, the money was lent or the contracts of purchase and sale were effected***" [the emphasis is ours].

In *Orion Caribbean Ltd*, a Cayman Island company's business had been ascertained as a matter of fact to be borrowing and

on-lending with a view to profit. Such profits of the taxpayer was found to arise from business transacted in Hong Kong since the taxpayer was used as a conduit to channel loans and funds raised or provided by its parent company, Orion Royal Pacific Ltd (ORPL) in Hong Kong which passed through the taxpayer to the ultimate borrowers under loan agreements negotiated, approved and serviced by ORPL. The Privy Council held that the test to determine source of profits should not only be based solely on the place of lending, to the exclusion of the place of borrowing. The ascertainment of an actual source of income is a "practical hard matter of fact". There is no simple, single legal test that can be employed to determine source of profits. The crux of the matter is the taxpayer was used as a channel for loans of funds raised or provided by ORPL in Hong Kong and passed through the taxpayer to the ultimate borrowers under loan agreements negotiated, approved and serviced by ORPL. As such, the profits of the taxpayer arose from business transacted in Hong Kong by ORPL on the taxpayer's behalf.

Totality of facts approach

As pointed out above the operations test is difficult to apply in circumstance where the taxpayer is engaged in several activities in several places to earn profits. In such circumstances the High Court in *Consco Trading Co Ltd* **reiterates the significance of the "totality of facts" principle in determining the source of trading profits**. *Consco Trading* was engaged in the business of trading polysilicon. Polysilicon was either purchased for resale directly or for processing into finished products for sale. The taxpayer did not have any overseas office or any other form of permanent establishment outside Hong Kong. In this case, the taxpayer argued that the 'profit-producing activities' were all undertaken outside Hong Kong while only 'non-profit producing activities were undertaken in Hong Kong, rendering the profits earned not taxable in Hong Kong. The activities undertaken outside Hong Kong included the sourcing of suppliers, negotiation, conclusion of contract, signing of the processing agreement through agents as well as the processing activities which were carried out by a subcontractor in China. The activities undertaken in Hong Kong included the placing of purchase order, invoicing, issuance of letters of credit as well as collections and making of payments.

In this case, the Board of Review carried out a weighing exercise and concluded that the preponderance of the relevant activities was done in Hong Kong and hence the profits in question were derived in Hong Kong. The Board rejected the taxpayers travel itinerary and went on to say that while the activities done in Hong Kong were formalities, they were essential activities and credit facilities such as letters of credit form an indispensable element in an overseas sale and purchase transaction without which no profits can be derived. The High Court held that:-

> *"… the Board had directed its mind to the relevant authorities and adopted the proper and correct approach. The authorities have clearly established that ascertainment of the actual source of income is a practical hard matter of fact and no simple, single legal test is determinative. To determine the source of profits, one must look broadly and consider all the circumstances and activities which generated the profits… while the place where the contract of sale and purchase was made is one important factor to be considered, it is not the only or the determinative factor. There is no rule of law that the place where the contract of sale and purchase is conclusive of the source of profits, though it is an important factor to be considered… the Board was aware of and considered the relevant facts. It took a global view of the evidence and carried out a weighing exercise and then concluded that the preponderance of the activities which earned the profits was performed in Hong Kong. The Board's finding that the profits were derived from Hong Kong is a finding of fact which the Court may not interfere."*

Operations test vs. totality of facts approach

As a result of these cases, uncertainties have arisen as to which approach to emphasise given the applicability of both approaches. The recent Hong Kong Court of Final Appeal (CFA) decision in *ING Baring Securities (Hong Kong) Ltd* clarified this uncertainty and re-affirmed that the guiding principle in determining the source of profits should be the operations test. In this case, ING Baring carried on the business of agency brokerage in Hong Kong as a member of a

multinational group of companies. It traded on the Hong Kong stock exchange or elsewhere. The income in dispute was commission, placement income and marketing income in respect of securities traded on stock exchanges outside Hong Kong ie whether such income made by the taxpayer which were derived directly or indirectly from transactions in securities traded on stock exchanges outside Hong Kong — were arising or derived from Hong Kong. It was decided in the CFA that all 3 income items were not derived from Hong Kong. The test laid down in the *Hang Seng Bank* case was adopted: what a taxpayer did to earn the profits and where the act took place. In each case, the income only arose when the securities were successfully traded on the foreign stock exchange. Therefore the actions that earned the profit were the trading of the securities or the allotment of the shares and these happened or were executed outside Hong Kong. Therefore, the income arose from outside Hong Kong.

The CFA concluded that when determining the source of commission income from the trading of listed securities, the important factor to consider is the place where the sale and purchase transactions were executed. The CFA stated that "while other steps taken in relation to the trading are relevant, the crucial step is usually the execution of the transaction for sale and purchase." The CFA decided that the taxpayer's income was derived offshore as the commission income was derived from trading of securities on an overseas stock exchange for which orders were forwarded to a licensed dealer for execution in the place where the stock exchange was located.

Lord Millett NPJ summarised as follows:

1. The place where the taxpayer's profits arise is not necessarily the place where he carries on business.
2. Where a taxpayer earns a commission for rendering a service to a client, his profit is earned in the place where the service is rendered, not where the contract for commission is entered into.
3. Transactions must be looked at separately and the profits of each transaction considered on their own.
4. Where the taxpayer employs others to act for him in carrying out a transaction for a client, his profit is earned in the place where they carry out his instructions, whether they do so as agents or principals.

Agency concept

What about business income earned by an agent of the taxpayer? In relation to the taxpayer's commission income in *ING Baring Securities*, Lord Millet of the CFA laid down the agency rule which states that where the taxpayer employs others to act for him in carrying out a transaction for a client, his profit is earned in the place where they carry out his instructions whether they do so as agents or principals.

Lord Millett also opined as follows:

> *"In considering the source of profits, however, it is not necessary for the taxpayer to establish that the transaction which produced the profit was carried out by him or his agent in the full legal sense. It is sufficient that it was carried out on his behalf and for his account by a person acting on his instructions. Nor does it matter whether the taxpayer was acting on his own account with a view to profit or for the account of a client in return for a commission".*

Lord Millett here appears to apply the maxim of *qui facit per alium facit per se* (he who acts through another, acts himself) in determining the source of profits derived through an agent. Based on the maxim, a third-party contractor would be considered an agent if the subcontractor acts on behalf of the taxpayer and according to the taxpayer's instructions.

This is contrasted with *Consco* where it was held in the High Court that the processing activities that were carried out by an independent contractor in China were irrelevant in determining the source of profits as the activities were not performed by the taxpayer.

The Malaysian case

While the cases and the decisions laid out above are not binding on taxpayers in Malaysia, they serve as persuasive support in addressing the issue of the source of profits in Malaysia. The Inland Revenue Board of Malaysia has not indicated an inclination for any preferred approach and in this regard, all the principles laid out above could therefore be considered equally important guidelines in determining the source of business profits in Malaysia.

The determination of the source of business profits questions is entirely dependant on the facts and circumstances of each case and there must be documentary evidence to support the claims and assertions made. While a particular element may be a crucial determining factor in one particular case (eg: the source of the letters of credits substantially determined the source of profits in *Conso*), the same element may not be a determining factor in another case in deciding the source of profits. Each case has therefore to be determined on its own particular facts.

Dividend income

The source of dividend income fortunately is a lot more straight-forward. In addition to the general charging section, s 14 of the ITA clearly prescribes that the source of dividend income is dependent on the resident status of the company. Under the derivation rules, the dividend is deemed to be derived from Malaysia if at the time of the paying, crediting or distributing the dividend, the paying company is a resident of Malaysia.

S 14(2) ITA goes on to specify that where a company was not resident in the previous year of assessment, only dividends paid, credited or distributed by the company on or after the day on which the management or control of any business of the company were first exercised in Malaysia is deemed to be derived from Malaysia.

In this regard, the source of dividend income unlike the business source discussed above can be identified with little or no room for dispute.

Interest income

Aside from s 3 ITA, the only express provision contained in the ITA as to derivation of interest is a deeming provision contained in s 15 which deems interest income to be derived from Malaysia under the following circumstances:

S 15(a), (b)(i)	if responsibility of payment lies with the government, state government or with a person who is resident (in Malaysia) for that basis year; and
S 15(b)(ii)	the interest is payable in respect of monies borrowed and employed in or laid out on assets used in or held for the production of gross income derived from Malaysia or the debt in respect of which the interest is paid is secured by any property or asset situated in Malaysia.

As such, in order to determine where interest income is sourced, there is a need to consider the reason for such borrowings as well as where the collateral for the debt is situated.

S 15(c) ITA further deems interest that is charged as an outgoing or expense against any income accruing in or derived from Malaysia as Malaysian sourced. This section aims to also subject to tax non-residents deriving Malaysian income in respect of loans granted to Malaysian companies.

Thus it would appear that the scope of charge for interest income is narrower than that of business income. However this is dependent on how the role of s 15 is viewed. Support is sometimes derived from the heading of s 15 ITA which reads, "Derivation of interest and royalty in certain cases" to state that s 15 ITA merely covers *certain circumstances* in which interest income is considered deemed to be derived in Malaysia, leaving the scope of charge in other circumstances subject to s 3 and open to debate.

> …it appears that the place where an obligation is created or where the contractual terms were executed, to which interest income is subsequently derived plays a crucial role in determining the source of interest income.

There is also the view that s 15 ITA is the sole test and that s 15 ITA and nothing else is tasked with determining the derivation of s 4(c) ITA interest as is the task of the other derivation provisions in the act. In other words s 15 ITA should be taken as a conclusive definition of derivation of interest with the result that if interest cannot be said to be derived from Malaysia under s 15 ITA than it is not derived from Malaysia altogether. Read in light of the entire legislation, s 15 ITA is the sole test has its merits. It is also argued that s 15 ITA is generally singularly quoted or tagged to s 4(c) ITA in guideline(s) issued by the Inland Revenue Board indicating its singular usage.

While a detailed analysis of the definition of source in relation to interest income is beyond the scope of this article, reference is made below to the decisions of several key cases that shed some light on the meaning of source as a starting point to the discussion of the source of interest. The varied approaches taken in case law that address the source of interest income approach is also presented below as a possible guide.

In the South African case of *Commissioner for Inland Revenue vs. Lever Bros and Unilever Ltd*, a case that is frequently quoted in other source of interest cases, it was held that "the source of receipts, received as income, is not the quarter whence they come, but the originating cause of their being received as

income and that this is the work the taxpayer does to earn them, the quid pro quo which he gives in return for which he receives them". Watermeyer CJ in this case went on to say that "it was the making and carrying out of the agreement relating to the £11,000,000 by the taxpayer, which earned the income for him, rather than the existence of the debt resulting from that agreement". A similar quote is obtained from a UK case, *Hart (inspector of taxes) v Sangster* which underscores the importance of the contract under which interest is paid. Here it was stated that "[t]he deposit of money would yield no income at all unless there was an agreement to pay interest, express or implied. The source of the income seems to be the deposit of money on certain terms".

From these cases, it appears that the place where an obligation is created or where the contractual terms were executed, to which interest income is subsequently derived plays a crucial role in determining the source of interest income. However, this approach may only be apt in situations of a straight forward debt/ loan structure. It is neither an appropriate approach nor determinative in situations where considerable activity has been undertaken to earn interest income. As such, this approach was expounded in the New Zealand case of *Commissioner of Inland Revenue (N.Z.) v N.V. Philips Gloeilampenfabrieken* (the *Philips Case*), where several principles were laid out.

In this case, a Dutch company (D Co) sold and exported products to a New Zealand company (NZ Co), and as a result the NZ Co owed D Co £80,000, which it was unable to pay. From negotiations, it was agreed that the liability be converted into a loan from D Co and that the loan should bear interest. A loan agreement was executed in the Netherlands under which D Co sent NZ Co a cheque drawn by D Co in London. Upon receipt of the cheque, NZ Co endorsed the cheque and sent it back to D Co as repayment of amounts owing for goods unpaid and also made appropriate entries into its books. Thereafter, NZ Co paid interest on the loan. The New Zealand tax authorities sought to assess NZ Co as agents for D Co in respect of interest received by D Co.

The judges in this case took slightly varying views. While both Greeson J and North emphasised the importance of looking at the "originating cause" of the payment of interest, interestingly enough, the judges had different views as to the source of the interest. The outcome of North's decision reiterates the stance already presented above in that **the place where the contract is executed is held to be the source of the interest (ie the Netherlands)**. Greeson J on the other hand, applied the **"provisions of credit test" and held that the title to the interest paid sprang from the loan and since the credit was provided in London from which sprang the obligation to pay interest, the loan originated from London**. Turner came to a similar decision as North but through the introduction of an interesting approach in which he explored 4 possible meanings of source as follows:

(a) "…the income of the NZ Co; the fund from which the interest actually came from…"
(b) "The capital fund or investment in respect of which the interest is payable - £80,000"
(c) "The debt or chose in action – D Co's legal right to recover the money: NZ"
(d) "The transaction or contract by virtue of which the chose in action arose."

Turner held that the first meaning could not be properly designated as the source of the interest paid for these are the income not of the lender but merely of the cause of the payment of interest (ie not sufficient to look at where the funds out of which the interest was paid).

On the second meaning, Turner held that the funds could not be "a source in New Zealand" for it "cannot be said that the money had any location at all". He then states that he is led to the "conclusion that the source must be found in either (c) or (d)" and that he was of the opinion "that the better view is that **the source is located where the transaction which the debt took its origin took place**, (d) rather than where the debt itself (c) was located". In other words Turner was of the view that **the execution loan agreement determined the source of the income** – He expressed the view that "upon the execution of the loan agreement the loan was granted by D Co to NZ Co by way of settlement of accounts: the loan setting off against the liability for the unpaid goods and nothing further was required to be done to perfect the loan".

In addition to the "originating cause" principles, all 3 judges in the *Philips Case* cited the test of what a practical man would regard as the real source as "a practical hard matter of fact". This approach is expounded using the Singapore case of *Chandos Pte Ltd v Comptroller of Income Tax* which reaffirms this position. This case serves as a noteworthy guide for the Malaysian dilemma as the reading of the charging section in the *Singapore Income Tax Act*, s 10, referred to in this case has the same effect as s 3 and s 4 of the Malaysian ITA.

Here, Delacom Investments Pty Ltd (Delacom), an Australian company obtained a loan from Chandos Pte Ltd (Chandos), a Singapore Company in order to pay Nazly Pura Jaya Pte Ltd (Nazly) for purchase of mineral rights in Australia. Chandos opened the account and obtained an overdraft facilty from a Singapore branch of a bank in which Delacom also had an account. On the loan agreement execution date, both parties travelled to Johor Bahru (JB) where the agreement was executed and cheques changed hands and payment was made to Nazly. The cheques drawn by Chandos and Delacom were credited to their respective bank accounts. At no time was interest payable by Delacom to Chandos ever paid or remitted to Chandos in Singapore. The Singapore tax authorities sought to tax the interest payable on the loan. Relying on the principles laid down in *Lever Bros and Unilever*, the taxpayer argued that the interest income on the loan was not derived in Singapore on the basis that the loan was executed in JB where the cheques also changed hands.

The judge in this case rejected the taxpayer's argument. The judge was of the view that the activities in JB were "too superficial and also artificial" and found that **the**

determination of source should be made on the basis of what a "practical man would regard as a real source of income". He went on to emphasise that "the ascertainment of actual source is a practical hard matter of fact".

An analysis of the facts of this case, and the transactions involved concluded that:

- the overdraft facility was made available in Singapore
- the cheque cleared in Singapore, and
- the loan disbursed in Singapore and credited into Delacom's account in Singapore (an act without which Chandos would have had no rights to payments of interest).

Based on the above facts, it was held that interest was **derived from Singapore** on the basis that "given all these facts, it just cannot possibly be argued that a practical man would regard the source of income in respect of the interest as not being in Singapore".

> Going back to the argument of whether s 15 ITA is the sole test in the determination of source of interest in Malaysia is relevant in identifying the significance of the approach adopted in the case laws above to the Malaysian taxpayer. For many years, the taxpayer, tax practitioners and the Inland Revenue Board (IRB) in Malaysia have commonly adopted the approach that s 15 is in fact the sole test for the determination of the source of interest.

The recent guidelines issued by the IRB[1] on determination of source of interest income makes reference to s 15 ITA as a deciding test. It appears that the tax authorities' view is to confine itself to the s 15 ITA being the key test in determining this matter.

Given the uncertainty of the source of interest issue in Malaysia, a sound guide to taxpayers is the operations test in *Hang Seng Bank* and *HK-TVB international Ltd* as there would always be a need to identify what has been done or needs to be done and where it has been done in order to earn the interest income, to ascertain the true source of income as a practical hard matter of fact. Commercial substance and documentary evidence would also serve to negate issues of superficiality of transactions.

Royalty income

Royalty income shares the same charging and derivation sections as interest income: s 3 and s 15 ITA of where s 15 (a), (b) (i) and (c) are also applicable to royalty.

As such, the arguments above in relation to s 15 ITA being the sole test would similarly be applicable here. Accepting s 15 ITA as the sole derivation section in relation to royalties, it would appear that royalty income is only deemed to be derived in Malaysia in circumstances where the payer of the royalties is a government, state government or resident of Malaysia and the royalty is charged as an outgoing or expense against any income accruing in or derived from Malaysia.

As regards the source of the royalty income a relevant case is *Chesebrough-Ponds International Ltd v DGIR 2 MLJ 25.* In this case, one of the principles established is that a patent or trade mark which has been registered in Malaysia and licensed to agents to use in return for royalty payments would constitute a property situated in Malaysia. On this basis, it may be contended that the royalty income derived from the licensing of the patent outside Malaysia would be regarded as derived from outside Malaysia. It should be noted that the general principle established in *Cheeseborough-Ponds* related to development tax and its applicability to business income as opposed to royalty income. However, the case could still be considered persuasive for purposes of determining the source of royalty income.

Other income

In the past, there was no provision to determine and collect tax on other income from non-residents under s 4(f). These types of income include, among others, commissions, guarantee fees and introducer's fees.

Pursuant to the recent budget announcement, a new s 15B ITA has been introduced that replicates the derivation s of royalty income: s 15(a), (b)(i) and (c) ITA which prescribes the derivation rules for 'other income'.

Effectively, this section also seeks to subject to tax 'other income' of non-residents previously not subject to tax. Since this is a new announcement, clarifications are being sought from the tax authorities on the scope of this new tax section and how wide the scope is meant to be.

Conclusion

With the exception of dividend income, the determination of source of income is an ongoing issue in the Malaysian arena, as it still is in all other tax jurisdictions adopting the territorial scope of taxation. This is due to the fact that the prescription of a universal test to identify the source of profits is impossible as the situations in which the source of a profit has to be ascertained are too many and varied. While several approaches and principles have been laid out and discussed as above, they are meant to serve as broad guiding principles to assist in the consideration of the source of profits issue. At the end of the day the question as to the derivation of a source of income is entirely dependant on the facts and circumstances of the case and the documentary evidence available to support the stance taken. TG

Both SM Thanneermalai and Lim Phaik Hoon are the Senior Executive Director and Executive Director of PricewaterhouseCoopers Taxation Services Sdn Bhd. Dr Nakha Ratnam is the Tax Specialist of Multimedia University. The content of this article represents the authors' personal views and not that of PricewaterhouseCoopers Taxation Services Sdn Bhd and Multimedia University. All authors can be contacted at thanneermalai.somasundaram@my.pwc.com; phaik.hoon.lim@my.pwc.com; and nakharatnam@yahoo.com.

1 The tax treatment for offshore company which make an elections under s 3A of the *Labuan Offshore Business Activity Tax Act 1990*, April 2008

Together Towards an Excellent Delivery System

By Chua Tia Guan

Tax reform in Malaysia

"In Sweden we pay taxes online. The corporate income tax, value added tax, labour contributions and property tax are filed on a single form. Doesn't everyone do it that way?" The World Bank Doing Business 2007 Report quoted a business owner, Mr Astrid in Sweden where the tax system is highly simplified.

Back home, in Malaysia, what kind of tax system do we want? Have we ever asked ourselves, why can't we do away with individual tax filing for employees who don't have other income other than salary since they are already under the Schedular Tax Deduction scheme? How much more tax revenue would be collected from such filings vis-a-vis the additional administrative cost incurred?

The establishment of *PEMUDAH*

Recognising the need for close collaboration, the Prime Minister, Datuk Seri Abdullah Ahmad Badawi has called for a public–private sector partnership to recommend and implement public service improvements, towards making Malaysia more business-friendly.

The Special Task Force to Facilitate Business, or *PEMUDAH (Pasukan Petugas Khas Pemudahcara Perniagaan)* was established on 7 February 2007. It reports directly to the Prime Minister. *PEMUDAH* comprises 13 heads of selected Government Ministries and Departments and 10 leaders of Malaysian business. *PEMUDAH* is co-chaired by Tan Sri Mohd Sidek Haji Hassan, Chief Secretary to the Government of Malaysia and Tan Sri Yong Poh Kon, President of the Federation of Malaysian Manufacturers.

The impetus

To support Malaysia's transition towards a knowledge-driven economy, the Prime Minister has placed special emphasis on addressing the softer aspects of competition such as the quality of the business environment. This is particularly urgent in the context of increasing global competition.

Malaysia's competitive position, as reflected in various international surveys such as the World Bank Doing Business Report, provided the impetus behind the formation of *PEMUDAH*. Malaysia ranked 25th out of 175 countries in the World Bank Doing Business 2007 Report.
The World Bank Doing Business Report is a series of annual reports investigating the regulations that enhance business activity and those constraints it. Doing Business Report presents quantitative indicators on business regulations and the protection of property rights that can be compared across 181 economies and over time. Regulations affecting 10 stages of a business's life are measured: from starting a business to closing a business. The indicators are used to analyse economic outcomes and identify what reforms have worked, where and why.

Using this report as a framework, *PEMUDAH* was tasked to address the areas related to the business environment. Malaysia's current international rankings in these areas are shown in Table 1: Doing Business Ranking. Through the reforms recommended by PEMUDAH, Malaysia has improved its overall ranking to 20th place for Doing Business 2009 Report from that of the 25th place in 2007. Effective tax reforms have improved our ranking significantly in the Paying Taxes indicator to 21th place compared to that of 60th place a year ago.

PEMUDAH is to provide the catalyst for change towards placing Malaysia in the top 10 of the World Bank Doing Business ranking.

Table 1: Doing Business Ranking

Malaysia's Performance	2009	2008	2007
Overall Ranking	20	25	25
Ease of doing business			
1. Starting a business	75	82	71
2. Dealing with Licenses / Construction Permits*	104	106	137
3. Employing workers	48	46	38
4. Registering property	81	73	66
5. Getting credit	1	1	3
6. Protecting investors	4	4	4
7. Paying taxes	21	60	49
8. Cross border trading	29	24	46
9. Enforcing contracts	59	60	81
10. Closing a business	54	57	51

** The Dealing with Licenses Indicator has been reworded as Dealing with Construction Permits in the Doing Business 2009 Report*

PEMUDAH structure

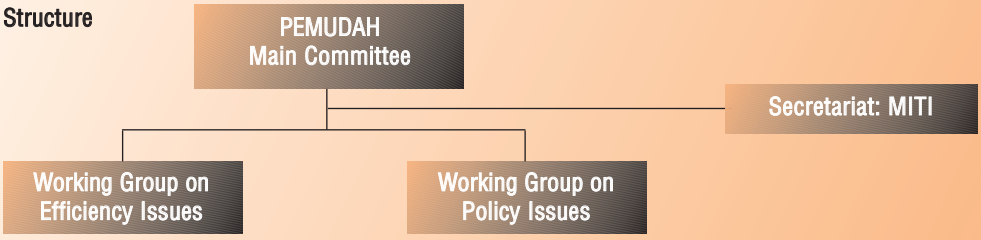
To effectively analyse and improve the prevailing public service delivery, *PEMUDAH* formed two working groups, namely, Working Group on Efficiency Issues, to focus on processes and procedures; and Working Group on Policy Issues, to focus on policies and regulations that impact national competitiveness. In addition, focus groups have also been established to help identify areas of improvements. The PEMUDAH structure is depicted in Diagram 1: *PEMUDAH* Structure.

Reengineering

"Taking cognizance of a rapidly changing and increasingly competitive world, the Government must be prepared to change laws, policies and regulations as "nothing was cast in stone". This is consistent with the Government's role as the facilitator and enabler of economic growth." This is the level of commitment of the Prime Minister in his effort to improve the public delivery system.

"Reengineering" is the way to go instead of just improving the existing systems. For example, we should ask ourselves why a licence is required? Is the licence for control or for revenue purpose? Can we live without the licensing requirement? Or is there any other better way to achieve the same objective?

Diagram 1: PEMUDAH Structure



Focus Groups:

- Paying Taxes
- Registration of Property
- Trading Across Borders
- Enforcing Contracts
- Closing Business
- E-payments
- Cost of Doing Business
- Government Procurement
- DBKL

Vision and values

The vision of *PEMUDAH* is to achieve a globally benchmarked, customer-centric, innovative and proactive public service in support of a vibrant, resilient and competitive economy and society. This vision is underpinned by the following values:

- a sense of urgency
- proactive public–private sector collaboration
- facilitation, not hampering
- no more regulation than necessary, and
- zero tolerance for corruption.

Clarity is power

Clear rules and regulations as well as procedures without ambiguities will increase compliance of laws by the citizenry. It facilitates business operations and provides certainty to investors. Further, rules and regulations must be made available and easily accessible by the general public. Publication of guidebooks for each application procedure is an effective means of disseminating information to the intended audience. To-date, *PEMUDAH* in collaboration with various government agencies and non-governmental organisations has published two guidebooks, namely, Guidebook on the Employment of Expatriates and Guidebook on Registering Property (Freehold) in Malaysia.

E-enabled

Making the public delivery system E-enabled enhances its accessibility to the general public. Electronic means would enable on-line tracking and monitoring of an application, thus enhancing transparency and accountability of the public delivery system. The result could also serve as a performance measure tool for each government officer/ agency/ department against the key performance indices (KPIs) set earlier.

In this connection, the Business Licensing Electronic Support System, BLESS (www.bless.gov.my), a portal which provides information and facilities for companies to apply online for licences or permits to start operating a business in Malaysia has been introduced.

The BLESS facility enables a company representative to select relevant licence, fill up the online application form, submit these online and track the progress of the applications throughout the process until notification of approval or otherwise. This would enable simultaneous processing of multiple licensing involving multiple agencies which would provide faster turnaround time. Further, BLESS provides an online communication platform for the licensing agencies to communicate directly with the applicant company for any clarification and justification for the licence applications which effectively saves time and resources for both parties. For the initial implementation, BLESS only covers the application of business licences for the manufacturing sector within the Klang Valley.

E-payment

In addition, E-Payment facilities have been further strengthened to provide convenience to the general public to make payments to the Government. At least 87 Government agencies offer 138 online payment services as at 4 September 2008. Payments can be made via the respective agency's portal, MyGovernment Portal or bank's online payment portal. In addition, payments can also be made via direct debit or credit card.

Public participation

The public's contribution of ideas and feedback is vital to the improvement of the public delivery system. Toward this end, *PEMUDAH* has set up a website (www.pemudah.gov.my) to receive suggestions and feedback from the general public. *PEMUDAH* is committed to respond to any suggestions and feedback within three working days on efficiency issues; for more complex or policy related issues, it may take a longer time, but the public will be kept posted on the progress.

Successful tax reforms

According to the World Bank, simple moderate taxes and fast, cheap administration mean less hassle for businesses– also more revenue collected and better public service. Since 2005, 90 reforms in 65 economies have pointed to the following 4 most successful tax reforms:

1. Introduce online filing

   "A quarter of the world's countries have electronic filing and payment of business taxes. That means no need for paper documents – and no need for personal interaction with tax officers. A third of the world's countries now use electronic payment methods such as bank transfers–and half use payment by cheque."

2. Combine taxes

   "Almost 50% of countries have more than one labour tax or contribution, 27% more than one tax on profits and 41% more than one tax on property. If the base is the same (salaries, profits or property value), why not just combine them? Having multiple taxes increases the bureaucratic burden for both the taxpayer and tax administration."

3. Simplify tax administration

   "Making the tax rules for business complex is unlikely to bring about more revenue – quite the opposite in fact. Countries that do not require special books (ie separate book keeping requirements for tax purposes only) have 10% more revenue (as a percentage of GDP) on average than countries that do. And having a clear tax law increases tax revenue by 6% on average."

4. Reduce tax rates and broaden the base

   "High tax rates can force companies into the informal sector (ie businesses have a strong incentive to evade taxes). Such countries can increase tax revenue by lowering rates and persuading more businesses to comply with the new tax system."

Focus group on paying taxes

Based on the above successful tax reforms in other countries, the Focus Group on Paying Taxes addresses the taxes and mandatory contributions that a medium-size company must pay or withhold in a given year, as well as measuring the administrative burden in paying taxes. These measures include the number of payments an entrepreneur must make; the number of hours spent preparing, filing and paying; and the percentage of their profits they must pay in taxes. Malaysia's ranking in Paying Taxes Indicator is tabulated in Table 2: Paying Taxes Indicator in Doing Business 2009.

Table 2 : Paying Taxes Indicator in Doing Business 2009

Country	Singapore	Hong Kong	Malaysia	
Year	2009	2009	2009	2008
Ranking	5	3	21	60*
Payments	5	4	12	35
Time (hours)	84	80	145	160
Profit tax (%)	7.9	18.6	16.8	17.5
Labour tax and contributions (%)	14.9	5.3	15.6	15.6
Other taxes	5.1	0.3	2.1	3
Total tax rate (% profit)	27.9	24.2	34.5	36
** Ranking revised from 56th placing to 60th placing*				

This Focus Group is working on 3 broad areas:

i. Income taxes, namely Corporate Tax, Individual Tax, and Stamp Duty;
ii. Customs taxes, namely Sales Tax, Service Tax, Excise Duty, and Goods and Services Tax;

iii. Other Taxes, namely Employees Provident Fund (EPF), Social Security Organisation (SOCSO), Human Resource Development Fund (HRDF), Road Tax, and Quit Rent.

To-date, the Focus Group on Paying Taxes has made numerous recommendations in relation to the public delivery system in taxation. The following are the recommendations and their implementation stage:

1 Income Taxes

- Introduce e-registration for companies and individuals to register their tax files (implemented by the IRB);
- Develop an online mode for submission of estimate and revision of corporate tax liability (in progress).
- Issue guidelines to stipulate the conditions, circumstances under which a set-off of overpayments can be allowed against tax instalments; specify when this can be allowed in the case of a group of companies; and the documentation required (implemented by the IRB).
- Issue a list of common employment benefits wherein the amount can be considered to be fully utilised in the carrying out of the employee's duties to avoid the need for an employee to make the necessary claims for deduction in their personal tax returns (announced in the 2009 National Budget).
- Issue guidelines to stipulate the circumstances in which lower tax estimates will be considered for companies (implemented by the IRB).
- Issue guidelines to stipulate circumstances in which penalties on late payment or under-estimation can be lowered or waived and a scale of penalties which would increase with the number of offences (implemented by the IRB).
- Review the existing Public Ruling on Entertainment Expenditure to make the position clear as to when would a full deduction or a partial deduction apply and to stipulate the relevant circumstances (implemented by the IRB).
- Allow taxpayers and tax agents to submit tax returns at any Assessment Branch as well as the Central Processing Centre and to provide proof of submission of the tax returns by manual means (implemented by the IRB).
- Make available the English translation of the tax return on the website for non-residents and foreigners as well as provide translations in other languages (the translations in English, Chinese and Tamil are now made available by the IRB).
- Revise client charter to stipulate timelines in handling appeals and objections from taxpayers and introduce mechanism to monitor adherence to the charter (implemented by the IRB).
- Allow bonus to be taxed in the year of receipt to avoid administrative costs as well as avoid any confusion to taxpayers (announced in the 2009 National Budget).

2. Customs Taxes

- Allow payments to be made at the nearest branch instead of controlled stations (implemented by the Customs).
- Enable forms to be downloaded from Customs' website (implemented by the Customs).
- Introduce new sales tax composite form – CJP 1 where taxpayers are only required to submit 3 copies (implemented by the Customs).
- Allow submission of Excise Forms 7 & 8 in the forms of CD/ disc/ diskette/ thumb drive (implemented by the Customs).
- Abolish the requirement to submit the Daily Sales Record (Lampiran A of Form CP3) for Service Tax purposes (implemented by the Customs).
- Abolish the requirement to submit the attachment to Sales Tax Form CJ10 but it shall be kept for post - audit purposes (implemented by the Customs).

3. Other Taxes

- Encourage electronic submission of EPF and SOCSO contributions by employers (in progress).

Initiatives by the IRB

The efforts by the IRB under the leadership of Datuk Hasmah Abdullah to proactively improve the delivery system in the areas of taxation must be commended. The following are the improvements made by the IRB:

- Reduce the period taken for refunding tax overpaid due to companies and individuals from one year to between 14 and 30 days in cases of submissions through e-filing.
- Refund tax overpaid for the current year of assessment without reference to the previous years of assessment.
- Years prior to 2006 assessment to be finalised later and further monies repayable/ tax payable to be dealt with separately.
- Refund tax overpaid directly to taxpayers without the need for formal application.
- Reduce the number of procedures and the processing time taken in the assessment of stamp duty.

Conclusion

For the last 22 months since the establishment of *PEMUDAH*, many improvements to the public delivery system as initiated by *PEMUDAH*, have been made by the respective government ministries and agencies. These improvements are in the areas of starting a business, business licences, dealing with construction permits, immigration matters, tax administration, trading across borders, registering property and e-payment facilities. Details can be found at the *PEMUDAH* website, www.pemudah.gov.my

These improvements would not have been achieved without the hard work of the government ministries and agencies as well as the suggestions and feedback from the general public. We strongly believe that together we can make Malaysia a good place to do business and a great place to live. TG

References:

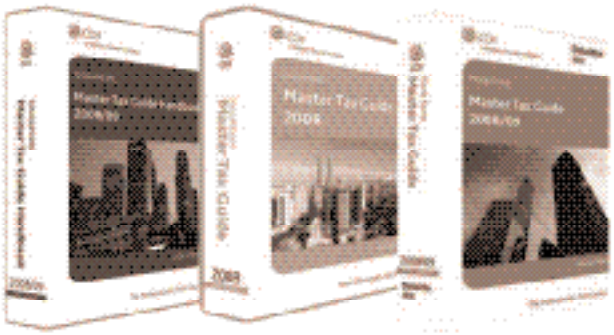
1. Doing Business 2008 Report
2. PEMUDAH 2007 Annual Report
3. http://www.doingbusiness.org/ExploreEconomies/?economyid=119
4. http://www.doingbusiness.org/ExploreTopics/PayingTaxes/
5. https://www.bless.gov.my/
6. http:www.pemudah.gov.my

Chua Tia Guan is a member of PEMUDAH cum the Chairman for Focus Group on Paying Taxes. He is also the Head of Tax & Financial Planning of Great Vision Advisory Group and can be contacted at tia.guan.chua@greatvision.com.my.

CCH
a Wolters Kluwer business

Be Vexed by Tax Issues No More!

Long regarded as the most practical, easy-to-use yet authoritative guides to tax law and practice in major Asian trading jurisdictions, CCH's annually updated Master Tax Guides have been relied upon by generations of tax lawyers and practitioners. Their astonishing simplicity and rich content put them way ahead of other tax services.



Master Tax Guides 2008/09

Malaysia • Singapore • Hong Kong • Japan • India • China • Macao

With an unbeatable combination of up-to-date and crystal-clear explanation of the overall tax system and planning strategy, CCH's Master Tax Guides help you ensure the most favourable and speedy tax outcomes.

Each Guide lays out the applicable law of taxation in a clear, non-academic language. Highlighting recent changes in revenue laws and practical implications of recent cases, each Guide leads you expertly through tax legislation, revised tax rates for existing and newly introduced tax categories and all relevant tax treaties. Understand the overall framework of each taxation regime and get insightful expert commentary on statutory and administrative tax law. Discover:

- Which tax applies to whom under what circumstances;
- How to calculate specific tax liabilities;
- How unsettled tax issues have been and are currently interpreted; and
- How to proceed with them and in what forum.

Some of the Guides' most valuable aspects include their user-friendliness, succinctness, time-saving features and layout.

You'll be amazed as you experience, time and time again, each Guide's thoughtful design. Let not tax matters vex you anymore!

And problems solved.

Apply your tax knowledge effectively with this comprehensive series comprising 7 major Asian regions

- Minimise tax liability
- Discover and use tax incentives effectively
- Plan long-term tax strategies
- Ensure full compliance with the latest changes

CCH's Master Tax Guides give you a wealth of highly practical features to save you time and money, including:

- updates on new and proposed tax changes
- completely up-to-date commentary of the latest laws and regulations
- explanatory citations to laws and regulations
- sample tax computations
- case tables
- subject locators
- checklists of common taxable, non-taxable, deductible and non-deductible items
- tax rate summaries
- tax filing obligations and their respective due dates
- superb index organised for quick answers
- easy-to-use tables, including up-to-date with holding tax tables
- commonly used tax forms with English translations (selected countries only)

Order form

Fax : 03.2026.7003

Order ref: MA 146

Title	Version	Code	Price (RM)	Qty	Amount
Malaysian Master Tax Guide 2008	Book	1748M	198.00		
Singapore Master Tax Guide 2008/09	Book	1753S	308.00		
Hong Kong Master Tax Guide 2008/09	Book	1740H	248.00		
Japan Master Tax Guide 2008/09	Book	1767S	473.00		
China Master Tax Guide 2008/09	Book	1742H	359.00		
Macao Master Tax Guide 2008/09	Book	1744H	414.00		
India Master Tax Guide 2008/09	Book	1799S	404.00		
India Master Service Tax Guide 2008/09	Book	1856S	314.00		
India Master Fringe Benefit Tax Guide 2008/09	Book	1857S	314.00		

☐ I would like to subscribe to eBiz Alert for free (please fill up your contact details below including email address) eBiz Alert is a free all-in-one monthly business e-newsletter that delivers concise current issues, trends and regulatory watch to the subscriber. It covers topic areas on Tax & Accounting, Corporate Law, Human Resource and overall business/ economy in the Asia Pacific region and globally. **FREE**

Total

Payment Options

☐ I enclose a cheque made payable to "Commerce Clearing House (M) Sdn Bhd"

Cheque No. _____ RM _____

☐ Please debit my ○ Visa ○ MasterCard RM_____

Card No.: ☐☐☐☐-☐☐☐☐-☐☐☐☐-☐☐☐☐ Expiry Date _____/_____

Card Holder's Name: _____ Card Holder's Signature: _____

Customer's Details

Mr/Ms Name: _____ Designation: _____

Company: _____
(As per business registration)

Business Registration No. : _____ Business Nature: _____

Company size: ☐1-4 ☐5-9 ☐10-19 ☐20-49 ☐50-99 ☐100-199 ☐200-499 ☐500-999 ☐1000+

Address:_____

_____ Postcode: _____ State: _____

Tel: _____Fax: _____ Email: _____
(Important to receive future special update/news)

_____ _____
Authorised Signature & Company Stamp Date

Contact Us

Toll Free Customer Service Hotline	1-800-181-151
Fax	(603) 2026 7003
Address	Suite 9.3, 9th Floor, Menara Weld, No. 76, Jalan Raja Chulan, 50200 Kuala Lumpur, Malaysia.
Web	www.cch.com.my
Email	mktg@cch.com.my

Terms & Conditions

1. Order is subject to acceptance by CCH.
2. Price(s) is valid in Malaysia and is subject to change without prior notice.
3. Book(s) will only be delivered upon receipt of payment.
4. Good(s) sold is not returnable. If the book is received in an unsatisfactory condition, it should be exchanged within a week of receipt.

Advance Pricing Arrangements

By Sockhalingam Murugesan

"To ensure that Malaysia remains an attractive investment destination in the region, particularly among multinational companies, the tax framework has to be transparent and business friendly. To enhance certainty on pricing issues for inter-company trades within a group, the Government proposes to introduce an ***Advanced Pricing Agreement*** *(APA) mechanism. This mechanism is widely practiced in developed countries and has succeeded in resolving issues relating to transfer pricing"*

Datuk Seri Abdullah Ahmad Badawi
Prime Minister and Minister of Finance
introducing the Supply Bill (2009) in the Dewan Rakyat on 29 August 2008.

Introduction

In presenting the 2009 Budget, the government has proposed the introduction of a new s 138C *Income Tax Act, 1967* (ITA) which provides for taxpayers to make an application to enter into an Advance Pricing Agreement (APA) with the Malaysian competent authority in relation to their cross–border related party transactions.

Applications under s 138C will have to be made using a prescribed form and shall contain particulars as may be required by the Director General. In this respect guidelines pertaining to the APA regime in Malaysia are expected to be issued soon.

The new section will become effective from 1 January 2009.

What is an APA?

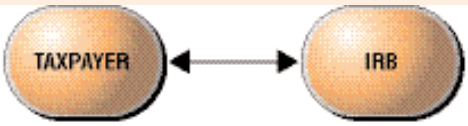
An APA is essentially an agreement entered into by a taxpayer and the tax authorities in relation to the future application of the arm's length principle of the taxpayer's cross–border related party transactions thereby reducing the possibility of any future disputes regarding the transfer prices.

In most countries, an APA generally carries an effective period of between 3 to 5 years.

Types of APA

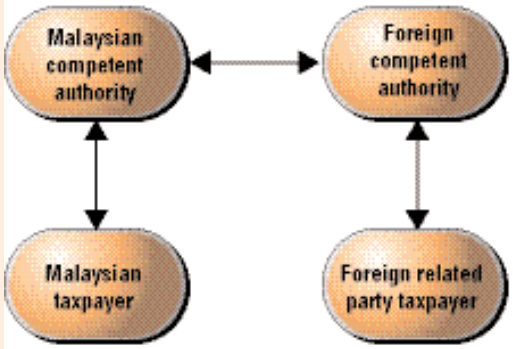
APAs can generally be categorised into the following types:-

Unilateral APA



As the name suggests, a unilateral APA is an agreement entered into between the IRB and a Malaysian entity in respect of transactions with related parties outside Malaysia. As the agreement only involves the IRB's confirmation of the taxpayer's transfer pricing position in Malaysia, it does not guarantee that related parties in other countries will avoid the risk of taxation by the foreign tax authorities on the same transaction.

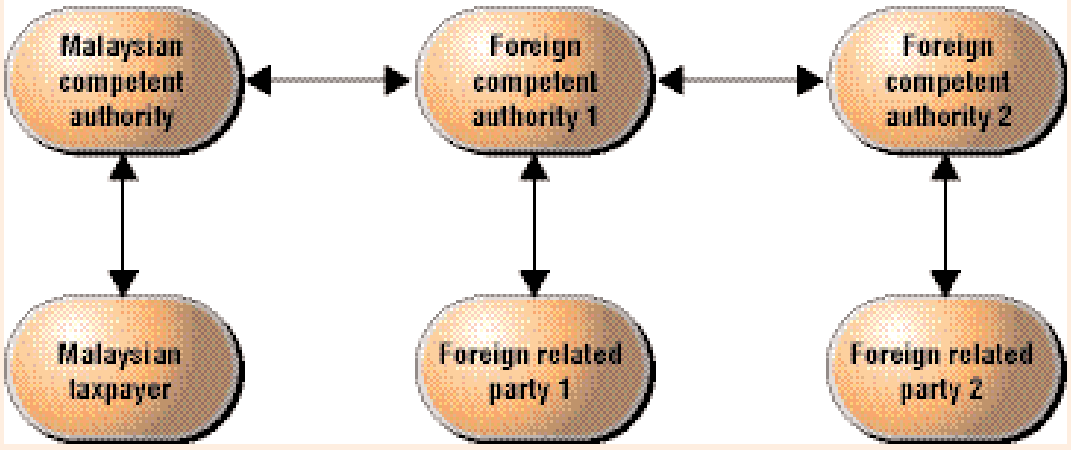
Bilateral APA



A bilateral APA is an agreement reached between the Malaysian taxpayer, the IRB, the foreign related party taxpayer and the foreign competent authority on the transfer pricing position of an inter–company transaction involving the Malaysian taxpayer and its foreign related party. Under a bilateral APA, the competent authorities will negotiate and agree on the transfer price that should applied by both the Malaysian taxpayer and its foreign related party for the said transaction.

Since an agreement is reached by both tax authorities, the Malaysian taxpayer and its foreign related party will be assured of the certainty of their respective transfer pricing positions.

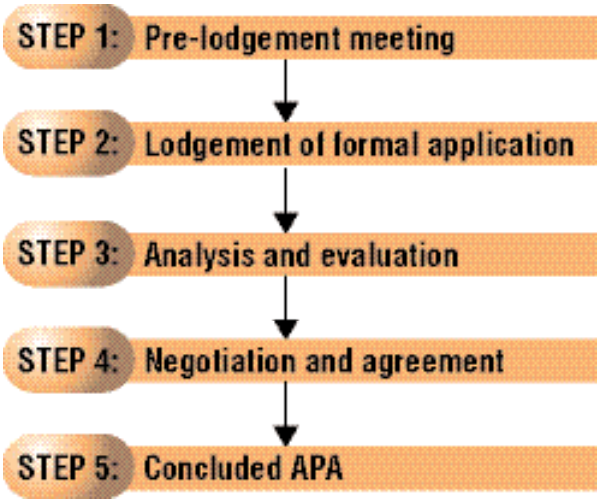
Multilateral APA



A multilateral APA is an arrangement between the Malaysian competent authority and two or more foreign competent authorities in relation to a series of related party transactions involving the countries concerned. A multilateral APA is entered into when the related party supply chain involves two or more countries.

Typical APA process

In most countries a typical APA process can be divided into 5 stages:-



APA Process	Key Aspects
Step 1: Pre-lodgement meeting	Matters covered include: • the suitability of an APA • provision of broad outline of proposed transfer pricing (TP) methodology • discussion of whether unilateral or bilateral APA to apply • discussion of required documentation and analysis • agreement on date for lodging formal application • agreement on APA timetable Pre-lodgement meetings do not bind either party.
Step 2: Lodgement and formal application	Application to include: • outline of transactions subject to the APA • details of the proposed TP methodology, supported by relevant information • terms and conditions governing the application of the TP methodology • data showing that the TP methodology will produce arm's length results • discussion and analysis of critical assumptions • a suggested period of time for which the APA will apply
Step 3: Analysis and evaluation	Evaluate the data submitted and seek additional information where necessary. Authorities may call for meetings to seek further information and clarification.
Step 4: Negotiation and agreement	For unilateral APA, formalisation of written agreement between the IRB and the taxpayer. For bilateral or multilateral APA, the relevant competent authorities exchange position papers outlining the acceptability of the proposed TP methodology. A written confirmation of the concluded agreement is provided to the taxpayer.

APA Process	Key Aspects
Step 5 : Concluded APA	A concluded APA contains: • the transactions, agreements or arrangements covered by the APA • the period and tax years covered by the APA • the agreed TP methodology and critical assumptions • arm's length range of results • obligations of taxpayer as a result of the APA • when a taxpayer files its tax return prepared in accordance with the APA, the confirmed transaction is treated as having been conducted at arm's length.

Going forward – What can we expect?

The rules pertaining to s 138C are expected to be issued before the end 2008. Until then one would not know exactly what the rules would entail.

However, one would be able to get some ideas of some of the provisions governing APAs in countries with APA rules. Some of these are highlighted below:

Roll back

In some jurisdictions, upon the conclusion of an APA, the authorities can apply, or provide an option to the taxpayer to apply, the agreed transfer price or margin on years prior to that covered under the APA. This is commonly known as a "roll back" provision.

We would have to wait for the detailed rules to determine if the roll back provision is covered and the corresponding penalties, if any.

Tax audits and investigations

Taxpayers must be aware that the mere fact that an application for an APA has been submitted or approved, does not remove the authorities' right to conduct a tax audit or investigation on the company. Therefore, taxpayers must ensure that notwithstanding an APA has been obtained, taxpayers should continue to maintain the required documentation, records and analyses as required under the ITA.

Separate teams

In countries with an APA regime, separate teams are established to conduct transfer pricing audits and to review APA applications. We hope the APA rules would incorporate this practice as it would certainly promote greater taxpayer confidence.

When should one seek an APA?

Before submitting an application for an APA, the taxpayer should first undertake a detailed analysis of the transaction to determine whether an APA is required. In making the analysis some of the points that the taxpayer should consider include:-

- a cost benefit analysis: Is it a significant transaction?
- should it be a unilateral or bilateral APA?
- is the future price or margin defendable?
- is the future price or margin expected to be maintained in near future?
- roll back: what was the historical price or margin earned? is that defendable?

APA for domestic transactions?

The proposed s 138C provides for applications of APA for cross–border related party transactions. We hope that the authorities may also consider the provision of a unilateral APA for domestic transactions as the provisions requiring arm's length pricing under both the existing s 140 of the ITA and the proposed s 140A ITA do not differentiate between domestic and cross–border transactions.

By allowing the provision of an unilateral APA for domestic transactions, taxpayers who undertake transactions with a related party who is subject to tax at a significantly different effective tax rate (eg due to incentives, tax losses etc), would be able to obtain a degree of certainty on the transfer prices applied on such transactions.

Although it has been proposed that a corresponding adjustment will be considered for domestic transfer pricing adjustments, the cost of any penalties on the transfer pricing adjustments may be significant enough to warrant a domestic APA for these companies.

Conclusion

As transfer pricing is a complex issue, difficult to resolve and often referred to as an art as opposed to a science, the introduction of an APA regime in Malaysia is certainly welcomed. As Malaysia continues to compete with other countries in the region for foreign investments, an APA regime will further boost Malaysia's position as a location of choice as multinationals who undertake a significant amount of cross–border related party transactions would have an avenue to obtain certainty on their transfer pricing position.

Nevertheless as APA applications can only be made on a going forward basis for future transactions, taxpayers should ensure that contemporaneous transfer pricing documentation continued to be maintained to substantiate the arm's length nature of their related party transactions. TG

Sockalingam Murugesan *is a Director with Ernst & Young Tax Consultants Sdn Bhd. The content of this article represents the author's personal views and not that of Ernst & Young Tax Consultants Sdn. Bhd The author can be contacted at Sockalingam.Murugesan@my.ey.com.*

Malaysian Tax Incentives for Islamic Finance – Trends and Issues

By Yeo Eng Ping

Tax neutrality has always been a key issue in Malaysia, when considering whether to use an Islamic structured finance product as compared to a conventional product. The growing importance of the Islamic *sukuk* is apparent - in year 2001, *sukuk* issuances accounted for 30% of the total number of bond issuances approved by the Securities Commission, and in 2007, this proportion grew to 53%.

The development of the Islamic debt capital market and the issuance of *sukuk* have been accelerated by the Malaysian Government's policy of implementing tax neutrality, and effort in establishing a tax framework that ensures the tax cost of using an Islamic product is no higher than its conventional counterpart. It is generally observed that Islamic financing products are more complex because they typically involve a greater number of transactions. That means that potentially, taxes and duties could be triggered at each leg of the transaction.

Some of the measures that are in place to promote tax neutrality include legislation which for income tax purposes, deems profit in lieu of interest to be treated as interest, and which disregards any disposals of assets or leases which are strictly required for the purpose of complying with *Syariah* principles and made pursuant to a scheme of financing approved by the Central Bank or the Securities Commission.

Most recently, legislation was also introduced to achieve tax transparency for the special purpose vehicle (SPV) established solely for the issuance of Islamic securities which adopt the principles of *mudharabah*, *musyarakah*, *ijarah* and *istisna* approved by the Securities Commission, and solely for the purpose of complying with the principles of *Syariah*, to counter inadvertent tax leakages related to use of such an SPV.

Similarly, in relation to stamp duty, there is also legislation to exempt any additional instrument executed pursuant to an Islamic financing scheme approved by the Central Bank or Securities Commission, where such instrument is strictly required for the purpose of complying with *Syariah* principles, and which will not be required for any other schemes of financing. In this way stamp duty is effectively imposed once, in the same manner as conventional financing.

Tax Incentives

In recent years, and particularly with the launch of the Malaysia International Islamic Finance Centre (MIFC) initiative in August 2006, there has been a trend to introduce tax incentives (over and above those enjoyed by conventional products), to intensify the competitiveness of Islamic finance products and enlarge the pool of players in the Islamic finance industry in Malaysia. Some of the added tax advantages for Islamic securities include:

- tax exemption on interest paid or credited to any person in respect of non-Ringgit Islamic securities originating from Malaysia, and approved by the Securities Commission.
- tax deduction given on the issuance costs for Islamic securities approved by the Securities Commission which adopt the principles of *mudharabah, musyarakah, ijarah* and *istisna,* or any other *Syariah* principle approved by the Minister of Finance, up to YA 2010.
- stamp duty remission of 20% on Islamic financing instruments approved by the Central Bank or Securities Commission, with the effect that stamp duty on these instruments would be 80% of the duty for conventional loans.
- tax exemption on income from the business of dealing in *sukuk*, for specified persons, up to YA 2011.

In addition, there are tax incentives provided to players in the Islamic finance industry in Malaysia, which include:

- Islamic banks and Islamic banking units are given an income tax exemption on Islamic banking business conducted in international currencies, up to YA 2016.
- *Takaful* companies and *takaful* units of insurance companies are also given an income tax exemption on *takaful* business conducted in international currencies, up to YA 2016.
- Tax deductions are to be given to any new Islamic stock broking company in Malaysia equal to the amount of the establishment expenditure incurred by the company, for applications made up to 31 December 2009.
- Tax exemption is given on income from the business of providing fund management services for approved Islamic funds, up to 2016.

- Income tax exemption is to be given for non-resident consultants with Islamic finance expertise.

Characterisation Issues

While these tax incentives will undoubtedly go a long way towards promoting Malaysia as a centre for origination for Islamic securities and financing, an interesting issue from a tax perspective is the characterisation of an Islamic financing transaction and the profit element of such a transaction. As highlighted above, any profits received and expenses incurred in lieu of interest in transactions conducted in accordance with the *Syariah* principles will be treated as interest for tax purposes. Hence, a tax deduction is accorded for the profit payments that meet such criteria, and various consequential tax implications and incentives may follow such conclusion. Any profit which is not in lieu of interest would not enjoy such tax treatment, and would be subject to different tax rules.

The question, therefore, is: what criteria should be applied to identify a true financing transaction from a normal business venture where both are structured to adopt *Syariah* principles? To illustrate, the essence of the principles of *musyarakah* and *mudharabah* is the sharing of profits in a business venture.

It appears that at the present time, the approach is to accept such arrangements as being Islamic financing arrangements so long as approvals have been obtained from the Central Bank or the Securities Commission as such. Conceivably however, there could be situations where it becomes difficult to ascertain whether a transaction is a *bona fide* financing transaction or simply a business venture.

In characterising an arrangement or a profit element for Malaysian tax purposes, should these attributes be scrutinised?

- the intention of the parties entering into the arrangement
- the level of risk taken by the investor
- the rate of return to the investor, and whether the effective return is "contained"
- pre-agreed disposition of the relevant assets by the SPV back to the user of the Islamic product at the maturity of investment
- pre-agreed time line for the Islamic venture as opposed to an open-ended investment.

International Aspects

The characterisation issue may be more complicated in the context of a cross-border Islamic financing. While an Islamic transaction may be approved by a Malaysian regulatory authority as a financing transaction, this characterisation may not be readily accepted in a foreign country, particularly one where Islamic transactions are less common. A mismatch in characterisation across jurisdictions may raise a variety of tax issues in foreign jurisdictions depending on their tax laws.

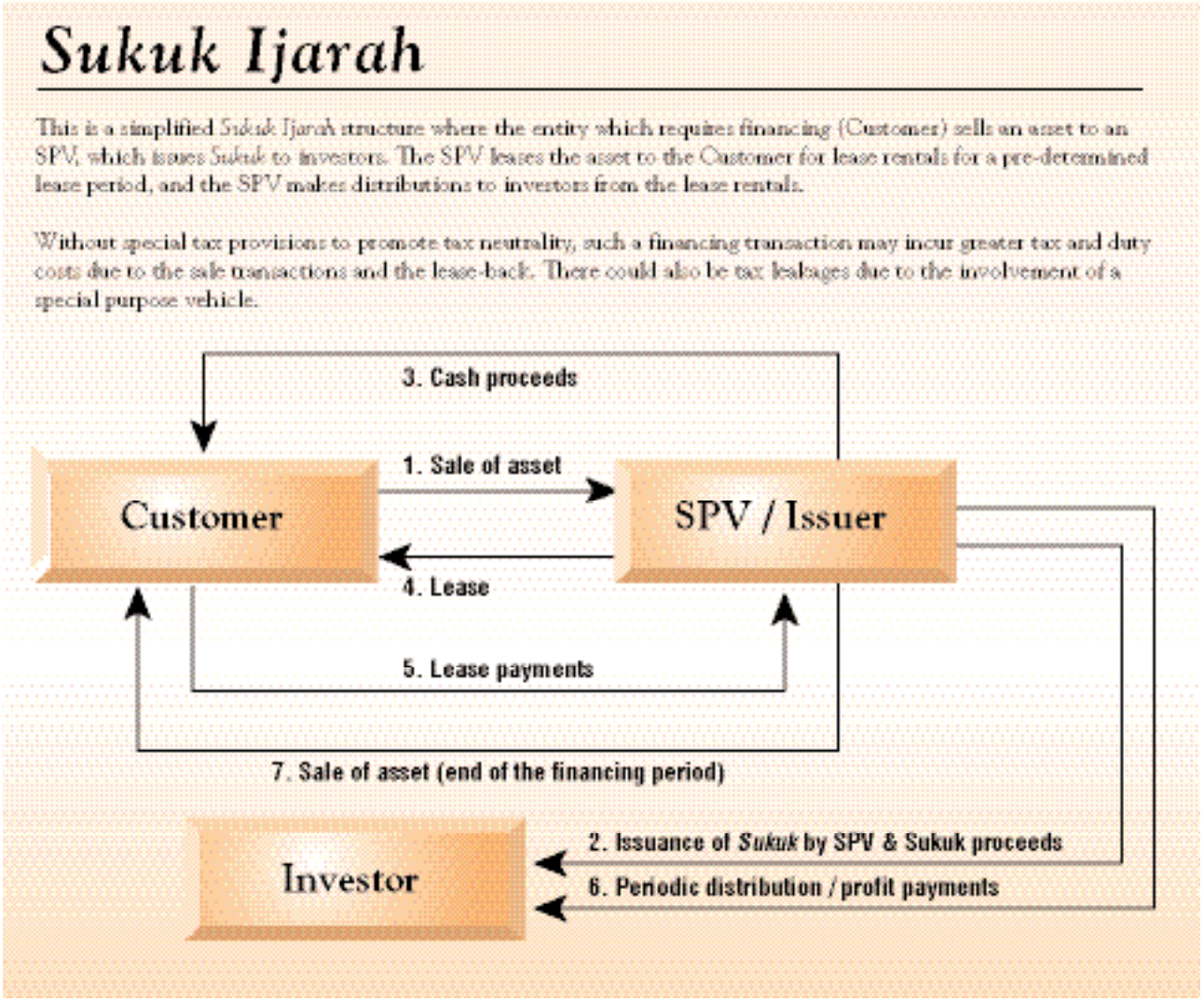
This issue is currently not dealt with in any Double Taxation Agreement (DTA). For example, in an *ijarah* transaction where the *sukuk* holder is outside Malaysia, would the home country of the *sukuk* holder regard the profits received as business profits, lease rental or interest income? This would be particularly relevant if the characterisation in the foreign country results in a significantly different tax exposure.

Further, if the *ijarah* assets are located outside Malaysia, would the foreign tax laws impose transaction taxes on the basis of a sale and leaseback (as is typical of *ijarah* transactions)?

As Islamic financing is becoming more common globally, perhaps the time is ripe for the introduction of special clauses to DTAs to take into account Islamic finance transactions, so that investors would have more certainty and receive the same protection as it would under conventional financing.

To continue its leadership in the area of Islamic financing and to anchor its position as an international Islamic financial centre, it would be in Malaysia's interest to play a prominent role in engaging stakeholders both locally and internationally, including prominent bodies such as the Organisation for Economic Co-operation and Development (OECD), to develop common solutions to these tax issues. TG

Yeo Eng Ping is an Executive Director of Ernst & Young Tax Consultants Sdn Bhd. The content of this article represents her personal views and not that of Ernst & Young. She can be contacted at Eng-Ping.Yeo@my.ey.com. *Parts of this article were previously published in International Finance News – February 08 Issue.*



TECHNICAL UPDATES

Technical Updates are summarised from the selected Government Gazettes published between 15 September 2008 and 11 November 2008.

INCOME TAX

Income Tax (Exemption) (No. 7) Order 2008 [P.U.(A) 351/2008]

Interest income received by individuals resident in Malaysia from money deposited in the following institutions will be exempted from income tax:

(a) a bank or a finance company licensed or deemed to be licensed under the *Banking and Financial Institutions Act 1989*
(b) a bank licensed under the *Islamic Banking Act 1983*
(c) a development financial institution prescribed under the *Development Financial Institutions Act 2002*
(d) the Lembaga Tabung Haji established under the *Tabung Haji Act 1995*
(e) the Malaysia Building Society Berhad incorporated under the *Companies Act 1965*, and
(f) the Borneo Housing Finance Berhad incorporated under the *Companies Act 1965*.

This Order revokes:

- Income Tax (Exemption) (No. 12) Order 1996 [P.U.(A) 64/1996]
- Income Tax (Exemption) (No. 13) Order 1996 [P.U.(A) 65/1996]
- Income Tax (Exemption) (No. 41) Order 1997 [P.U.(A) 383/1997], and
- Income Tax (Exemption) (No. 6) Order 1998 [P.U.(A) 155/1998].

The Order is deemed to have come into operation on 30 August 2008.

Income Tax (Accelerated Capital Allowance) (Bus) Rules 2008 [P.U.(A) No. 356/2008]

For 2009 till 2011, capital expenditure incurred on the purchase of a bus by a person (as the first registered owner) in the basis period for a year of assessment in respect of a business source in relation to commercial transportation qualifies for an initial allowance of 20% and an annual allowance of 80%. Where the bus is purchased under a hire-purchase arrangement, the capital expenditure incurred in the relevant basis period will qualify for the accelerated capital allowance (ACA).

The person must be a resident of Malaysia and a holder of a public service vehicle licence or a tourism vehicle licence. "Bus" means stage bus, charter bus, express bus, mini bus, employees' bus, feeder bus, school bus and excursion bus. The bus shall be locally assembled or constructed (not reconditioned) and used for commercial transportation of passengers or conveyance of tourists.

There will be a clawback of the ACA granted if the person sells, conveys, transfers, assigns or alienates the bus with or without consideration within two years from the date of acquisition. The clawback is computed in the basis period of a year of assessment in which the bus is sold, conveyed, transferred, assigned or alienated and is effective for the 2009 to 2013.

Income Tax (Accelerated Capital Allowance) (Plant and Machinery) Rules 2008 [P.U.(A) No. 357/2008]

For the 2009 and 2010, capital expenditure incurred on the purchase of plant and machinery in the basis period for a

year of assessment by a company in respect of a business source qualifies for an initial allowance of 20% and an annual allowance of 80%. Where the plant and machinery is purchased under a hire-purchase arrangement, the capital expenditure incurred in the relevant basis period will qualify for the ACA.

The company must be a Malaysian resident incorporated in Malaysia with an ordinary paid-up share capital of RM2.5 million or less at the beginning of the basis period for a year of assessment.

The following shall have effect for the years of assessment 2009 until 2012:

(i) The above Rules shall not apply to a company in the basis period for a year of assessment –
  (a) where more than 50% of its ordinary paid-up share capital is directly or indirectly owned by a related company or vice versa; or
  (b) which has been granted any incentive under the *Promotion of Investment Act 1986*; or reinvestment allowance under Sch 7A of *Income Tax Act 1967 (Act)*; or
  (c) where the company has made a claim on special allowances for small value assets under para 19A, Sch 3 of the Act.

(ii) Related company is a company whose ordinary paid-up share capital exceeds RM2.5 million at the beginning of the basis period for a year of assessment.

(iii) There will be a clawback of the ACA granted if the person sells, conveys, transfers, assigns or alienates the plant and machinery with or without consideration within two years from the date of acquisition. The clawback is computed in the basis period of a year of assessment in which the plant and machinery is sold, conveyed, transferred, assigned or alienated.

Income Tax (Accelerated Capital Allowance) (Information and Communication Technology Equipment) Rules 2008 [P.U.(A) No. 358/2008]

For the years of assessment 2009 till 2013, capital expenditure incurred on the purchase of information and communication technology (ICT) equipment as specified in the Order by a person resident in Malaysia in the basis period for a year of assessment for a business source qualifies for an initial allowance of 20% and an annual allowance of 80%. Where the ICT equipment is purchased under a hire purchase arrangement, the capital expenditure incurred in the basis period will qualify for ACA.

The ICT equipment specified are: access control system, banking system, barcode equipment, bursters/decollators, cables and connectors, computer assisted design (CAD), computer assisted manufacturing (CAM), computer assisted engineering (CAE), card readers, computers and components, central processing unit (CPU), storage, screen, printers, scanner/reader, accessories, communications and network, software system or software package.

The following shall have effect for the years of assessment 2009 until 2015:

(i) The above Rules shall not apply to a person if in the basis period for a year of assessment, the person has been granted –
  (a) any incentive under the *Promotion of Investments Act 1986*, or
  (b) reinvestment allowance under Sch 7A of the *Income Tax Act 1967*

(ii) There will be a clawback of the ACA granted if the person sells, conveys, transfers, assigns or alienates the ICT equipment with or without consideration within two years from the date of acquisition. The clawback is computed in the basis period of a year of assessment in which the ICT equipment is sold, conveyed, transferred, assigned or alienated.

Income Tax (Accelerated Capital Allowance) (Security Control Equipment and Monitor Equipment) Rules 2008 [P.U.(A) No. 359/2008]

For the years of assessment 2009 until 2012, capital expenditure incurred in the basis period for a year of assessment from a source consisting of a business in relation to the installation of:

(a) security control equipment as specified in the Schedule at any building of permanent structure used for the purpose of that business by an individual resident in Malaysia; or

(b) security control equipment as specified in the Order for a factory by a company approved under the *Industrial Co-ordination Act 1975*; or

(c) any Global Positioning System(GPS) for a container lorry bearing Carrier Licence A and for a cargo lorry bearing Carrier Licence A or C by a company and used for the business purposes of the company qualifies for an initial allowance of 20% and an annual allowance of 80%. Where the security control equipment and monitor equipment is purchased under a hire-purchase arrangement, the capital expenditure incurred in the basis period;

will qualify for the ACA.

The security control equipment specified in the Order are: anti-theft alarm system, infra-red motion detection system, siren, access control system, close circuit television, video surveillance system, security camera, wireless camera transmitter, time lapse recording and video motion detection equipment.

The following shall have effect for the years of assessment 2009 until 2014:

(i) The above Rules shall not apply to an individual or a company if in the basis period for a year of assessment, that individual or company has been granted –
  (a) any incentive under the *Promotion of Investments Act 1986*, or
  (b) reinvestment allowance under Sch 7A of the *Income Tax Act 1967*

(ii) There will be a clawback of the ACA granted if the person sells, conveys, transfers, assigns or alienates the security control equipment and monitor equipment with or without consideration within two years from the date of acquisition. The clawback is computed in the basis period of a year of assessment in which the security control equipment and monitor equipment is sold, conveyed, transferred, assigned or alienated.

Income Tax (Deduction of Pre-Commencement of Business Expenses Relating to Employee Recruitment) Rules 2008 [P.U.(A) No. 361/2008]

Expenses incurred on the recruitment of employees prior to the commencement of business are deemed to be incurred on the day of commencement and allowed a deduction in arriving at the adjusted income of a person resident in Malaysia from its business in the basis period for a year of assessment.

The expenses incurred shall be expenses on the recruitment of employees to enable the person to commence its business. The expenses are of the kind allowable under s 33 of the *Income Tax Act 1967* relating to the recruitment of employees and incurred within the period of one year prior to the commencement of its business.

These Rules are effective from the year of assessment 2009 onwards.

Income Tax (Exemption) (No. 8) Order 2008 [P.U.(A) No. 378/2008]

A Malaysian resident company incorporated under the *Companies Act 1965* is exempted from payment of income tax on net income received from the sale of certified emission reduction [ie gross income from the sale less expenditure (not being capital expenditure) incurred for the purposes of obtaining certified emission reduction].

"Certified emission reduction" is defined to mean a Kyoto Protocol (an international agreement relating to United Nations Framework Convention on Climate Change) unit equal to one metric tonne of carbon dioxide equivalent, calculated in accordance with Kyoto rules and is issued for gas emission reductions from an activity of clean development mechanism project approved by the Ministry of Natural Resources and Environment.

This Order is effective for the years of asssessment 2008 until 2010.

Income Tax (Exemption) (No. 9) Order 2008 [P.U.(A) 393/2008]

Statutory income derived from a business of dealing in non-ringgit *sukuk* that originates from Malaysia and issued or guaranteed by the Government of Malaysia or approved by the Securities Commission under the *Capital Markets and Services Act 2007* (Act) by a Malaysian resident who is:

(a) a holder of a Capital Markets Services License granted under s 61 of the Act;

(b) a registered person under s 76(1)(a) of the Act; or
(c) a registered person under s 76(2) of the Act;
is exempted from tax provided that such dealing is carried on through the proprietory account of such person.

Such dealing shall be treated as a separate and distinct source of business and activity and separate accounts are to be maintained by such person.

This Order is effective from the years of assessment 2009 until 2011.

Income Tax (Exemption) (No. 10) Order 2008 [P.U.(A) 394/2008]

Statutory income derived from the regulated activity of dealing in securities and advising on corporate finance relating to the arranging, underwriting and distributing of non-ringgit *sukuk* that originates from Malaysia and issued or guaranteed by the Government of Malaysia or approved by the Securities Commission under the *Capital Markets and Services Act 2007* (Act) by a Malaysian resident who is:

(a) a holder of a Capital Markets Services License granted under s 61 of the Act;
(b) a registered person under s 76(1)(a) of the Act;
(c) a registered person under s 76(2) of the Act; or
(d) a specified person under Sch 3 of the Act who carries on the regulated activity of advising on corporate finance solely incidental to the carrying on of its business or the practice of his profession;
is exempted from tax.

Such activity shall be treated as a separate and distinct source of business and activity and separate accounts are to be maintained by such person.

This Order is effective for the years of assessment 2009 until 2011.

Income Tax (Exemption) (No. 11) Order 2008 [P.U. (A) No. 410/2008]

Statutory income in relation to advisory fees received for the structuring and listing of a foreign corporation or the listing of a foreign investment product on a stock exchange that is a body corporate approved by the Minister of Finance to be a stock exchange under the *Capital Markets and Services Act 2007* (Act) of the following person is exempted from tax:

(a) a holder of a Capital Markets Services License granted under s 61 of the Act who carries on the regulated activity of advising on corporate finance;
(b) a registered person under s 76(1)(a) of the Act who carries on the regulated activity of "advising on corporate finance" as specified in Part I of Sch 4 of the Act; and
(c) a specified person under Sch 3 of the Act.

In addition, the person must be a member of the due diligence working group established under the "Guidelines on Due Diligence Conduct For Corporate Proposal" pursuant to s 337 of the Act .

This Order is effective for the years of assessments 2009 until 2013.

STAMP DUTY

- **Stamp Duty (Remission) (No. 2) Order 2008 [P.U.(A) 311/2008]**

50 per cent is remitted from the stamp duty chargeable on any loan agreement executed between a purchaser named in the sale and purchase agreement, who is a Malaysian citizen, and a bank, a financial institution, an insurance company, a co-operative society, or an employer under an employee housing loan scheme, to finance the purchase of only one unit of residential property costing not more than RM250,000 per unit. The sale and purchase agreement must be executed on or after 30 August 2008 but not later than 31 December 2010.

"Residential property" means a house, and a condominium unit, an apartment and a flat built as a dwelling house.

DOUBLE TAXATION AGREEMENTS (DTAS)

DTAs entering into force

- The DTAs signed by Malaysia with Myanmar (Order 1999 [PU (A) 302/1999]) and Chile (Order 1999 [PU (A) 84/2005]) respectively have entered into force. The DTAs are effective from the year of assessment beginning on or after 1 January 2009 for income tax and withholding tax; whilst in respect of petroleum tax, it will be effective from the year of assessment beginning on or after 1 January 2010.

- **Double Taxation Relief (The Government of the State of Qatar) Order 2008 [P.U. (A) 405/2008]**
  The double taxation agreement signed by Malaysia with the State of Qatar has been gazetted but not entered into force. The DTA shall have effect from the year of assessment beginning on or after 1 January in the calendar year following the year in which this agreement enters into force; except that in respect of petroleum tax, it will be effective from the year of assessment beginning on or after 1 January in the second calendar year following the year in which this agreement enters into force.

PUBLIC RULING

Public Ruling No. 3/2008 – Entertainment Expense

The IRB has issued the above Public Ruling on 22 October 2008. This Public Ruling explains:

(a) the tax treatment of entertainment expense as a deduction against gross income of a business; and
(b) steps to determine the amount of entertainment expense allowable as a deduction.

The Ruling supersedes Public Ruling No. 3/2004 (issued on 8 November 2004) and the Addendum to Public Ruling No. 3/2004 (issued on 23 August 2007) and is effective for year of assessment 2008 and subsequent years of assessment. TG

Case Summaries

Goh Eng Hwa v Ketua Pengarah Hasil Dalam Negeri

High Court (Malaya), Melaka
Originating Summons No. MT1-24-291-2006

Revenue Law – Income Tax Act – unpaid taxes- issuance of travel restriction by Revenue

Civil Procedure- application for declarations- preliminary objection-abuse of court process

Facts

The taxpayer applied for the following declarations by way of an originating summons:

a) that the taxpayer does not owe the sum of RM62,321.61, being unpaid taxes as assessed by the Revenue; and
b) that the s 104 certificate (travel restriction) issued by the Revenue was not sustainable and to be cancelled.

The counsel for the second respondent raised a preliminary objection to the taxpayer's application. She contended that the taxpayer's application was an abuse of court process. She argued that the appropriate process to challenge the Revenue's decision was by way of judicial review.

[Note: The High Court proceeded to determine the preliminary objection first before considering the substantive issues raised by the taxpayer in his application.]

Issue

Was the taxpayer's application for declarations by way of an originating summons an abuse of court process?

Decision

The High Court upheld the preliminary objection and dismissed the taxpayer's application. The court held that the appropriate process to challenge the Revenue's decision is by way of judicial review.

The court considered the following in arriving at its decision:

a) being a public authority, decisions made by Revenue officers should be challenged by way of judicial review;
b) the amendment to Order 53 of the Rules of High Court 1980 stipulates that from 22 September 2000, all applications to challenge the decisions of public authorities can only be made by way of judicial review;
c) cases decided since the amendment have consistently held that judicial review is the appropriate process to challenge the decisions of public authorities; and
d) the practice in the United Kingdom had also changed since 1977, where the House of Lords in *O'Reilly v Mackman* [1982] 3 All ER 1124 held that it was an abuse of court process to commence a writ action to challenge a public authority's decision instead of applying for judicial review.

The taxpayer's application was dismissed with costs in favour of the Revenue.

For the Taxpayer: WS Goh, Messrs WS Goh & Assoc

For the Director General of Inland Revenue: Suzana Atan, Senior Federal Counsel

Before: Mokhtarudin Baki, J.

Kanowit Timber Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri

High Court (Sabah & Sarawak), Kuching
Suit No. 14-03-2007

Revenue Law – Income Tax Act – s 22(2)(a)(i)- whether payment was trading income- whether payemnt represented a recovery

or recoupment of expenditure incurred- repairs and maintenance of logging roads and camp facilities

Facts

The taxpayer company appealed against the decision of the Special Commissioners of Income Tax (SCIT). The taxpayer was a logging contractor. Its business was to sell and extract timber. The taxpayer was the logging contractor for BS Company Berhad. Between 1990 and 1999, the taxpayer claimed RM11,465,267 as deductions under s 33(1) of the *Income Tax Act 1967* (ITA). The expenditure was incurred to maintain and repair the taxpayer's logging roads and camp facilities. The Revenue allowed the deduction of that expenditure under s 33(1).

On 30 June 1999, the taxpayer appointed AP Sdn Bhd as its subcontractor to fell and extract timber. The taxpayer also agreed to sell AP Sdn Bhd its logging equipment on an "as is where is" basis. Further, the taxpayer also sold logging roads and camp facilities for RM2,120,000. The amount represented:

a) the rentals that the taxpayer would have collected from AP Sdn Bhd for the use of the logging roads and camp facilities;
b) the expected tonnage which might be carried over the roads and was capped at 10 years; and
c) the expenditure incurred for the repairs and maintenance of the logging roads and camp facilities.

The RM2,120,000 was treated as sundry income in the taxpayer's audited accounts. The logging roads and camp facilities were not treated as assets in the accounts of the taxpayer. At the expiry of the contract between the taxpayer and AP Sdn Bhd, as well as the taxpayer's main contract with BS Contract Sdn Bhd, the logging roads and camp facilities remained with the latter. AP Sdn Bhd could not ask for any refund in respect of the RM2,120,000.

Before the SCIT, the taxpayer contended that the RM 2,120,000 was part of its trading receipt. The reasons were:

a) the payment in reality represented rental for AP Sdn Bhd for using the logging roads and camp facilities;
b) the amount was capped for a 10-year period; and
c) the amount was within the ambit of s 22(2)(a)(i) of the ITA as it was in reality a sum recouped, recovered from or reimbursement from the RM11,465,267 being the expenditure allowed for repairs and maintenance of the logging roads and camp facilities.

Meanwhile, the Revenue argued that the payment was a capital receipt. The payment amounted to the sale of the logging roads and camp facilities. The Revenue added that the taxpayer was a logging contractor and was not in the business of selling camp facilities and logging roads.

The SCIT applied the test laid down in *Californian Copper Syndicate (Ltd) v Harris* (1904) 5 TC 159 and held the RM2,120,000 received by the taxpayer was capital in nature. The SCIT held that the infrastructure sold by the taxpayer were disposal of its capital assets. It was also added that the taxpayer was a logging contractor and was never involved in the business of selling camp facilities and logging roads.

[Note: Before the High Court, both parties submitted a set of agreed facts. Among others, the parties stated that the Revenue had added back the sum of RM11,465,267 for the years of assessment 1992 and 1999. Subsequently, notices of additional assessment were issued on 2 November 2004. The taxpayer had appealed against the additional assessments and the appeal is still pending. The court took the decision to ignore the additional facts. As the appeal was by way of a case stated, the court's decision must be based on the same evidence before the SCIT. Hence, for the purposes of this appeal, the fact remained that the sum of RM11,465,267 was allowed as deductions under s 33(1) of the ITA.]

Issues

a) Was the RM2,120,000 received from AP Sdn Bhd was a capital receipt or revenue receipt?
b) Was the RM2,120,000 is within s 22(2)(a)(i) of the ITA?

Decision

Before considering the substantive issue, the High Court reiterated the following principles:

a) The burden of proof is on the person who is appealing against the decision of the SCIT.
b) The appellant must establish that the SCIT's decision was a decision "which no person properly instructed in the relevant law and acting judicially could have come to".
c) The party challenging the SCIT's finding of facts must request for the case stated to state a question whether a particular finding of fact is unjustified in view of the evidence adduced.
d) The findings of primary facts by the SCIT cannot be questioned by the appellate court unless item (b) above is satisfied.
e) The appellate court's role is to determine whether the SCIT's conclusion is consistent to the primary facts.

The court considered issue (2) first and applied the purposive approach to interpret s 22(2)(a)(i) of the ITA. The court observed that provision was an embodiment of the "tax benefit rule". Under this rule, when an amount deducted in prior years is recovered in a later year or an event occurs in a later year that is inconsistent with the deduction made, the taxpayer must include that amount in computing its income. The amount included must be to the extent of the deduction made by the taxpayer. Hence, the sums receivable under s 22(2)(a)(i) must be sums recoverable in respect of circulating assets in general, that is recoveries in respect of revenue expenditure. The court added that s 22(2)(a)(i) is to be read together with s 33(1).

For the first issue, the court held that the SCIT's conclusion was inconsistent with its finding of facts. In the facts found by the SCIT, it was stated that the RM2,120,000 was received by the taxpayer as a recovery or recoupment of the expenditure amounting to RM11,465,267 incurred on repairs and maintenance of the logging roads and camp facilities. According to the court, this means the original source of the payment stemmed from a revenue nature as the expenditure was held to be deductible under s 33(1) of the ITA. The court held the RM2,120,000 received by the taxpayer was revenue in nature and fell within s 22(2)(a)(i) of the ITA.

The taxpayer's appeal was allowed with costs.

For the Taxpayer: Dr Chew Peng Hui, Messrs Battenberg & Talma

For the Director General of Inland Revenue: Cik Noor Kamaliah Mohd Japeri, En Mohamad Harris Hanapi & Encik Wan Khairuddin Wan Montil, Revenue Counsel

Before: David Wong Dak Wah, J.

Kerajaan Malaysia v Neraca Untung Sdn Bhd
High Court (Malaya), Kuala Lumpur
Civil Suit No. S2-21-199-2001

Revenue Law – Income Tax Act – unpaid taxes- tax increased pursuant to s 103(4) and 103(5A)- whether the increased taxes amounted to penalty- whether the notices of assessment were served- presumption of service under s 145(2)

Civil Procedure- application for summary judgment- triable issue- whether the notices of assessment were served on the taxpayer

Facts
The taxpayer appealed against the Senior Assistant Registrar's decision to allow the Plaintiff's summary judgment application. According to the Plaintiff, the taxpayer was issued with notices of assessment and additional assessment for the year of assessment 1997. However, the taxpayer failed to settle the taxes raised.

The taxpayer, on the other hand:
a) denied receiving the notices;
b) argued that the Plaintiff failed to prove the service of the notices;
c) did not pay the taxes raised as they did not receive the notices;
d) denied owing the taxes; and
e) contended that the increases for late payment of tax amounted to a penalty and was without any basis.

The Plaintiff submitted that the notice of assessment was served on the taxpayer's tax agent. But, the Plaintiff failed to provide any evidence to support this. However, the Plaintiff argued that the taxpayer's tax agent had admitted receiving the notice of assessment.

Issue
Were the notices of assessment and additional assessment for the year of assessment 1997 were served on the taxpayer?

Decision
The High Court observed that s 145(2) of the ITA allows service via ordinary post or registered post. In the present appeal, the Plaintiff claimed that ordinary post was used to serve the notice of assessment.

The court held that the notice of assessment had been served on the taxpayer for the following reasons:

a) Section 145(2) of the ITA deems the notice to have been served on the taxpayer in the ordinary course of post; and

b) The taxpayer's tax agent had acknowledged the receipt of the notice of assessment in its correspondence with the Plaintiff. The Plaintiff tendered the correspondence to the court to support its contention.

However, the court held that the Plaintiff had failed to establish whether the notice of additional assessment was served on the taxpayer. The taxpayer's tax agent only acknowledged the receipt of the notice of assessment and not the notice of additional assessment. As such, there was a triable issue as to whether the taxpayer was served with the notice of additional assessment.

The taxpayer's appeal was allowed with costs.

For the Director General of Inland Revenue: Puan Shafibi Abdul Samad, Revenue Counsel

For the Taxpayer: Ms P.G. Loke, Messrs Cheah Teh & Su

Before: Dato' Azmel b. Hj. Maamor, J.

Sokoya v Revenue and Customs Commissioners
High Court, United Kingdom, [2008] EWHC 2132 (Ch)

Facts
The taxpayer filed his tax return for 2004–2005 showing £4,650 as income from his employment with a company. His return stated that he had no other income. The Revenue informed the taxpayer of its intention to enquire into the taxpayer's tax return and made an informal request for certain information. The taxpayer did not respond to the informal request. Subsequently, the Revenue issued a notice

requiring within 30 days, among others, the taxpayer's bank and building society statements for the relevant year, statements for all credit, debit or store cards held for the year, documents relating to sale of property and documents relating to mortgage.

The taxpayer decided to appeal against the notice to the Special Commissioner. He contended that the information and documents requested by the Revenue were superfluous. He added that the Revenue had no power to enquire into items where there was no entry in the tax return. According to the taxpayer, the Revenue did not reasonably require the information. The notice was an enquiry into his lifestyle, not into the tax return. The taxpayers also argued that the tax return was restricted to the information, which he had given in relation to his employment. Since, he did not include the other entries in the tax return, according to him, he had by implication, made a nil return.

Meanwhile, the Revenue argued that it had explained the reason for the notice in a letter to the taxpayer. However, the taxpayer did not respond to it. Hence, the notice was issued to request for further information to determine whether the tax return submitted by the taxpayer was correct.

The Special Commissioner held that the notice for further information issued by the Revenue was reasonably issued. According to the Special Commissioner, the notice allowed the Revenue to determine to which extent the tax return submitted by the taxpayer was incorrect or incomplete.

Issue

Did the Revenue reasonably require the notice to inquire into the tax return?

Decision

The High Court held that the Special Commissioner was correct to allow the notice issued by the Revenue. The court rejected the taxpayer's contention that the Revenue can only inquire into those aspects of tax return where he has made positive entries. The nil returns under the other aspects of the tax return were equally proper subject matter for the Revenue to investigate. The court arrived at this conclusion based on two reasons. Firstly, there was a specific provision under the income tax legislation which allows the Revenue to require documents to be produced to determine whether a return is incomplete or incorrect. According to the court, any construction of that provision to limit the power to require the production of documents would give no real meaning to the word "incomplete". Otherwise, it would be difficult for the Revenue to determine whether a taxpayer's entries in the tax return were correct. Secondly, the taxpayer had declared in the tax return that he had no other income. In such a case, the court held that it would be absurd to rule that such a declaration would shield the taxpayer from inquiries. The taxpayer also attempted to rely on Articles 6 and 8 of the European Convention on Human Rights, which was part of the United Kingdom law via the *Human Rights Act 1998*. However, the court dismissed it on the basis that the taxpayer's contention lacked substance.

The taxpayer's appeal was dismissed. TG

S. Saravana Kumar *is a tax lawyer with Lee Hishammuddin Allen & Gledhill. He appears regularly before the Special Commissioners of Income Tax and High Court for various tax and custom matters. He also advises business enterprises on tax advisory and tax planning matters. Saravana can be contacted at tax@lh-ag.com*

International News

By Rachel Saw

The column only covers selected developments from countries identified by the MIT and relates to the period September to 18 November 2008.

People's Republic of China

Tax treatment of services provided by parent company clarified

The State Administration of Taxation (SAT) issued a notice (Guo Shui Fa [2008] No.86) on 14 August 2008 clarifying the tax treatment of service fees charged by a parent company to its subsidiaries within China. The details of the Notice are summarised below.

- The expenses incurred by a parent company for providing various services to its subsidiaries must be charged at an arm's length and treated as normal service costs for the purposes of enterprise income tax, failing which the tax authorities are entitled to make adjustments.
- A parent company and its subsidiaries are required to enter into a service contract or agreement to determine the content and price of services and other related amounts. The service fees paid according to the contract or agreement mentioned above shall be included in the taxable income of the parent company and are deductible by the subsidiaries.
- In cases where a parent company provides the same kind of services to more than one subsidiary, the parent company may charge its subsidiaries, on a "cost plus" basis, by either entering into a separate service contract/agreement with each subsidiary, or a master "service sharing agreement" with all the subsidiaries receiving the services.
- Notwithstanding the above, management fees paid by the subsidiaries are not deductible in computing taxable income of the subsidiaries.
- Subsidiaries can only deduct the service fees paid to the parent company if they are able to submit the service contract/agreement or other related supporting documents.

The Notice makes no mention on the treatment of cross border transactions of a similar nature among *related parties*.

Debt-equity Ratios (thin capitalisation) Released

The Ministry of Finance (MOF) and SAT jointly issued a notice (Cai Shui [2008] No.121) on 19 September 2008 announcing the debt-equity ratios for the purposes of the thin capitalisation rule in Art. 46 of the new Enterprise Income Tax (EIT) Law as summarised below:

In determining taxable profits for the purposes of EIT, the interest on debts actually paid to an associated enterprise is

deductible only if the following debt-equity ratios are observed:

- 5:1 for financial services enterprises; and
- 2:1 for non-financial enterprises.

However, the ratios prescribed above do not apply if an enterprise can prove that the loan transactions are conducted at arm's length or the effective tax rate of the borrowing enterprise is not higher than that of the lending enterprise within China.

The Notice does not state its effective date.

Working guidelines for qualification of new high technology enterprises published

The Ministry of Science and Technology, the Ministry of Finance and the SAT jointly issued the guidelines for qualification of the New High Technology Enterprises (NHTE) on 8 July 2008 (*Guo Ke Fa Huo* [2008] No.362; henceforth "the Guidelines"), providing further clarification on the NHTE assessment criterion previously set out:

Ownership of core proprietary intellectual property
The exclusive license rights held by the applicant must be a license for sole use on a worldwide basis and not merely the rights to exploit the intellectual property (IP) in China. The IP must have been obtained within the 3 previous years, including IP obtained through exclusive licensing rights for a period of more than 5 years. The IP must support the key production techniques, or services, of the enterprise.

Requirements for research and development expenditure

- The Guidelines set out the definition of "R&D activities" and R&D projects. It also sets out the scope of qualifying R&D expenditure and the prescribed format to capture the relevant expenditure.
- It is required that at least 60% of the R&D expenditure must be incurred in China.
- Prescribed proportions of technical and research personnel directly involved in the R&D activities must be achieved and maintained.

Revenue arising from new high technology products / services
Revenue arising from these products and services must be more than 60% of the total annual turnover of the enterprise and the products/services generating the income should fall into the encouraged items of the Catalogue (which was previously published).

Factors governing innovativeness
Details are provided on the 100-point score-card system used to assess the innovativeness of enterprises using scientific technology, for which an applicant must score more than 70.

4 factors are used in the assessment:

- own proprietary IP rights;
- R&D outcome conversion capability;
- quality of R&D management:; and
- growth potential indicators.

Application process
The Guidelines provide a detailed description of the Application process.

The status of the NHTE is valid for 3 years and can be renewed.

Transitional measures for existing qualified NHTEs established in the High New Technology Industrial Zones (including Beijing New Technology Production Development Experimental Park) before 31 December 2007 are also prescribed.

Passive income of non-resident enterprises taxed on gross basis

The MOF and SAT jointly issued a notice (Cai Shui [2008] No. 130) on 28 September 2008 to state that the passive income derived by a non-resident enterprise referred in Para. 3 of Art. 3 of the EIT Law must be taxed on a gross basis. No taxes or fees can be deducted unless otherwise provided under Art. 19 of the EITL and Art. 103 of the Implementation Regulations of the EITL.

Draft of VAT reform approved

It has been reported that the State Council approved the proposal of the MOF and the SAT concerning the VAT reform on 8 November 2008. The new rules of VAT are likely to apply as from 1 January 2009.

The reform focuses on:

- the input VAT credit on purchases of fixed assets by the general taxpayer will apply to all industries subject to VAT nationwide. The full amount of the input VAT on the fixed assets will be deductible. However, fixed assets do not include personal cars, motorcycles, yachts and real estate for the VAT purposes;
- the abolition of VAT exemption on certain imported equipment;
- the abolition of the VAT refund on the domestically manufactured equipment purchased by foreign investment enterprises;
- the reduction of the VAT rates for small-scale taxpayers to 3%; and
- the increase of the VAT on mineral products to 17%.

It is expected that the new rules of VAT will be published shortly.

India

New companies law to be introduced

The government, on 29 August 2008, approved the introduction of a new Companies Act to replace the current Companies Act 1956 as the former is said to need comprehensive revision in light of the changing economic and commercial environment. The Companies Bill 2008 is to be introduced to Parliament and provides for, amongst others:

- the basic principles for all aspects of internal governance of corporate entities and a framework for their regulation thus harmonising the company law framework with the imperative of specialised sectoral regulation;
- the articulation of shareholders democracy with protection of the rights of minority stakeholders, responsible self-regulation with disclosures and accountability, substitution of government control over internal corporate processes and decisions by shareholder control. It also provides for shares with differential voting rights to be done away with, and valuation of non-cash considerations for allotment of shares through independent valuers;
- the smooth transition of companies operating under the Companies Act 1956 to the new law, including from one type of company to another;
- the introduction of a new entity in the form of One-Person Company while empowering the authorities to provide a simpler compliance regime for small companies. It also retains the concept of Producer Companies, while providing a more stringent regime for not-for–profit companies to check misuse and does not impose any restrictions on the number of subsidiaries that a company may have;
- speedy incorporation process, with detailed declarations/disclosures about the promoters, directors, etc. at the time of incorporation itself;
- the facilitation of joint ventures;
- the relaxation of restrictions limiting the number of partners in entities such as partnership firms, banking companies, etc. to a maximum 100 with no ceiling as to professions regulated by Special Acts;
- the duties and liabilities of the directors, and for every company to have at least one director resident in India. The Bill also provides for independent directors to be appointed on the boards of such companies as may be prescribed, along with attributes determining independence;
- the recognition of both accounting and auditing standards. The role, rights and duties of the auditors defined as to maintain integrity and independence of the audit process. Consolidation of financial statements of subsidiaries with those of holding companies is proposed to be made mandatory;
- a single forum for approval of mergers and acquisitions, along with concept of deemed approval in certain situations;
- a separate framework for enabling fair valuations in companies for various purposes;
- Shareholders Associations/Group of Shareholders to be enabled to take legal action in case of any fraudulent action on the part of company and to take part in investor protection activities and "Class Action Suits"; and
- a revised framework for regulation of insolvency, including rehabilitation, winding up and liquidation of companies, with the process to be completed within a time limit.

New category of contributors to Employees Provident Fund and Pension Scheme introduced

With effect from 1 October 2008, "international workers" will be required to contribute to India's Employees Provident Fund Scheme and Employees Pension Scheme.

Effectively:-

- Foreign nationals working in India are now brought under the ambit of the Provident Fund.
- International workers would be required to contribute a percentage of their salary to the Indian Social Security Scheme and employers will be required to make a matching contribution.

- Where no Social Security Agreement with India exists, the inbound/outbound employee will be required to contribute to the host country's social security scheme.
- Where a Social Security Agreement exists, the inbound/outbound employee may remain on the country of origin's social security scheme.

Treaty between India and Mauritius – Treaty shopping not factor in foreign direct investment proposals from Mauritius, according to India's Foreign Investment Promotion Board

India's Foreign Investment Promotion Board (FIPB), which had been rejecting foreign direct investment proposals from Mauritius for several months on the grounds of "treaty shopping" as advocated by the tax authorities, has now rejected the tax authorities' arguments on the basis that "treaty shopping" is a tax issue that is separate from the regulatory approvals governing investment into India. The FIPB maintains that it will base its decisions on the foreign investment policy, and that tax issues would not affect such decisions which should instead be left to the tax authorities.

Indonesia

Revised interpretation of "beneficial ownership" under Tax Treaties

The tax authorities issued circular SE-03/PJ.03/2008 on 22 August 2008 on their interpretation of the phrase "beneficial ownership" for tax treaty purposes, thus revoking circular SE-04/PJ.34/2005 on the same matter.

Both circulars provide that the "beneficial owner" is the real owner of income in the form of dividend, interest and/or royalty income, with full rights to directly enjoy the benefits of the income. In addition, a non-resident taxpayer who seeks treaty relief under an applicable tax treaty with Indonesia must have a valid certificate of domicile in order to qualify. Unless both these requirements are met, tax must be withheld at the domestic rate of 20%.

The new circular is silent on the status of special purpose vehicles as beneficial owners, which the old circular specifically excluded from the definition of a beneficial owner. Further guidance on the prevention of treaty abuse will be covered under a separate circular, which will be issued later.

Enactment of income tax bill

Indonesia's proposed income tax bill was enacted by the Indonesian parliament on 2 September 2008, which is effective 1 January 2009.

Clarification – Application of Tax Treaties in calculating BPT for trading representative offices

The tax authorities issued Circular Letter SE-2/PJ.03/2008 on 31 July 2008 to clarify the application of tax treaties in calculating the branch profits tax rate applicable to representative offices engaged in trading activities.

Trading representative offices are currently taxed on 1% of their gross export proceeds, at a final tax rate of 0.44% comprising corporate income tax and branch profits tax. The circular clarifies that if an applicable tax treaty stipulates a lower branch profits tax rate than the domestic rate of 20%, the treaty rate applies in arriving at the final tax rate.

Singapore

Supplementary administrative guidance on APAs

On 20 October, 2008, the Inland Revenue Authority of Singapore (IRAS) published a supplement to the provisions on advance pricing agreements (APAs) in the transfer

pricing guidelines previously issued on 23 February 2006. In summary, the supplement:

- sets out in detail the APA application procedure from the pre-filing meeting with the IRAS, through to the formal application, and review and negotiation stages. It also highlights certain factors that should be considered by the taxpayer before applying for an APA, such as potentially high time and monetary costs, and the level of co-operation required from the taxpayer;
- addresses the circumstances under which the IRAS may consider to allow an APA applicant's request for the APA to apply to "roll back" years; and
- sets out the circumstances which warrant the IRAS discontinuing with the APA process initiated for a taxpayer's case and the approach taken by the IRAS under such circumstances.

New R&D tax measures – details

The IRAS issued a circular dated 31 October 2008 on details of the 3 new R&D measures introduced in the 2008 Budget. Key details of the measures, which are effective the year of assessment (YA) 2009, are set out below. The Circular also contains guidance on the relevant administrative procedures for claiming the incentives, and examples of how they are to be computed.

Deduction of 150% of qualifying R&D (QRD) expenditure incurred from YA 2009 to YA 2013

- applies to expenditure incurred by a taxpayer on QRD activities undertaken in Singapore;
- applies to payments made by the taxpayer to an R&D organisation to undertake on his behalf, QRD activities in Singapore (limited to 130% where a breakdown of the payments made cannot be identified);
- capital allowances (CAs) can be claimed on plant and machinery used for undertaking the QRD activities even if unrelated to the taxpayer's business;
- the expenses and CAs are to be offset against income that is subject to the highest tax rate, with any balance to be offset against the next lower tax rate and so on; and
- gains or losses from the disposal of intellectual property rights (IPRs) will be subject to tax only if the taxpayer is engaged in acquiring IPRs, or develops IPRs for the purpose of resale.

R&D allowance claimable against chargeable income

- given at 50% of the first SGD 300,000 of the company's chargeable income or actual chargeable income, whichever is lower, derived during the basis periods YA 2009 to YA 2013, pursuant to a prescribed formula;
- the allowance is credited to an R&D account at the end of each basis period, subject to a maximum of SGD 450,000;
- the allowance can be claimed provided that (i) the company has a credit balance in its R&D account on the first day of the basis period of utilisation; and (ii) the company has incurred incremental qualifying R&D expenditure in the basis period;
- the allowance is first available for offset against the assessable income for the YA immediately following the YA in which the allowance is granted;
- the allowance is to be offset against income that is subject to highest tax rate, with any balance to be offset against the next lower tax rate and so on; and
- any unutilised R&D allowance in a YA cannot be carried back or transferred to related companies and the last YA in which the allowance can be utilised is YA 2016.

R&D Incentive for Start-up Enterprises (RISE)

- a qualifying start-up company can elect to convert its current year unutilised tax adjusted losses for a YA into a cash grant provided it meets certain conditions;
- the cash grant is computed according to a prescribed formula and is subject to a cap of SGD 20,250 for each YA; and
- the election is irrevocable for the YA in question and partial conversion of losses is not allowed.

Thailand

Revenue Department clarifies withholding tax on swap payments

It has been reported that the Revenue Department has issued two department instructions on 15 August 2008 (Paw. 136/2551) and 29 September 2008 (Paw. 114/2545) on the "variance payments" relating to interest swaps as follows:-

- if there is an interest rate swap contract in which no contracting party is a lender, the variance payment from the interest rate swap would be assessed under s 40(8) of the Revenue Code, which is not subject to withholding tax under s 70;
- however, if one of the contracting parties is a lender, then the variance payment from the interest rate swap will be treated as interest under s 40(4)(a) of the Revenue Code, which is subject to withholding tax; and
- where both parties intend to enter into a loan agreement, but separately conclude an interest swap agreement which essentially converts the loan interest to a variance from the interest swap, that variance will be considered income under s 40(4)(a) of the Revenue Code and will be subject to withholding tax.

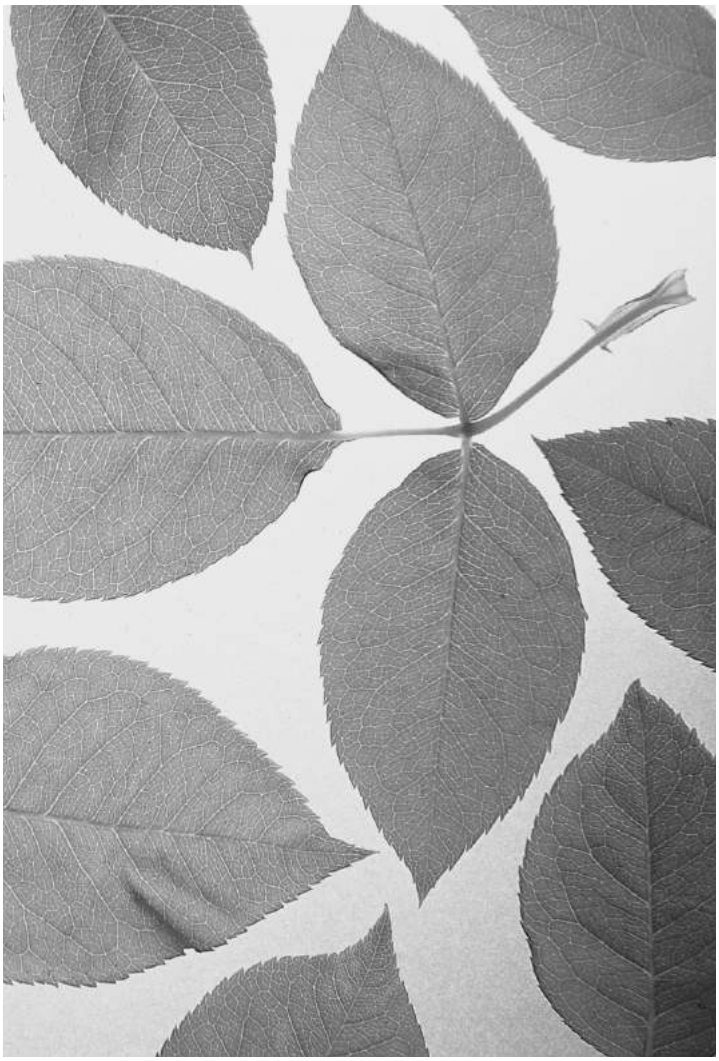
This follows a Supreme Court decision where it was held that the income from a swap payment was considered s 40(8) income, even though one of the contracting parties was a lender, since the swaps were concluded separately from the loan agreements.

Vietnam

Decree on personal income tax issued

In line with the scheduled implementation of Personal Income Tax Law (PIT Law) on 1 January 2009, to regulate taxpayers, taxable income, tax-exempt income, reduction of tax and the basis for calculating PIT, the Government issued Decree 100/2008/ND-CP (Decree 100) of 8 September 2008.

Decree 100 classifies taxable and tax-exempt income, and provides for a progressive tax regime in respect of income from businesses, wages and salaries, ranging from 5% to 35% with the highest band being a monthly income of over



VND 80 million. The minimum monthly taxable income will be VND 4 million for both Vietnamese and foreigners. Also noteworthy are the changes resulting in housing allowances, relocation, travel, and tuition payments, being taxable with effect from 1 January 2009.

Environmental tax measures introduced – Clean Development Mechanism Projects and Certified Emission Reductions

The Ministry of Finance and the Ministry of Natural Resources and Environment jointly issued the Inter-Ministerial Circular No.58/2008/TTLT-BTC-BTN&MT on 4 July 2008 to provide for the fiscal regime with respect to Clean Development Mechanism (CDM) project.

(a) Fee for sale of Certified Emission Reductions (CERs). Describes the process with regard to the registration and transfer of CERs, upon which a fee (based on a prescribed formula) is to be paid for the sale of the CERs. With regard to CDM projects, where a foreign party is involved and said party does not have an office in Vietnam, the domestic investor is responsible for the payment of the fee.

(b) CDM projects funded by Official Development Assistance. CERs generated from CDM projects funded by Official Development Assistance are owned by the State. Therefore, it is the investor who will be responsible for selling CERs and paying over the sales proceeds of the CERs (*less* any applicable selling expenses) to the EPF.

(c) Price subsidy. A project may be eligible for a price subsidy (based on a prescribed formula), which is funded by the EPF, if it meets certain conditions.

In addition to the above environmental tax measures, it was reported that the Vietnamese MOF intends to increase the taxes on the extraction of minerals, metals, natural gas, coal, and gemstones and that a special consumption tax would be imposed on vehicle owners as part of efforts to cut fuel consumption and reduce traffic congestion (this comes after a hike in car registration taxes from 5% to 15% and an increase in tariffs on imported cars by 13% earlier in 2008).

New enterprise income tax and VAT laws published

Further to their adoption by the National Assembly on 3 June 2008 (TNS:2008-06-27:VN-1), the Law on Enterprise Income Tax No. 14/2008/QH12 and Law on Value Added Tax No. 13/2008/QH12 were published on 5 November 2008. The Laws will come into effect on 1 January 2009.

Proposed unemployment insurance

Further to the Law on Social Insurance (LSI) which came into effect on 1 July 2007, Unemployment Insurance (UI) is to be introduced in Vietnam on 1 January 2009. It is reported that a draft decree will be issued shortly.

The UI is expected to be compulsory for employers with ten or more employees employed under (i) an indefinite-term labour contract, or (ii) a definite-term labour contract between 12 months and 36 months. A contributory rate of 1% of the monthly salary is expected to apply to both the employer and employee. TG

Rachel Saw *is a Senior Research Associate at the International Bureau of Fiscal Documentation (IBFD). The International News reports have been sourced from the IBFD's Tax New Service. For further details, kindly contact the IBFD at ibfdasia@ibfd.org.*

Constructive Dismissal

With the courts imposing greater responsibilities on employers towards their employees, it is imperative that employers equip themselves with the necessary knowledge to avoid and manage constructive dismissal cases in the workplace.

What is Constructive Dismissal?

Constructive dismissal is a term used when an employee terminates his employment contract and considers himself discharged from further performance of his work as a result of his employer's behaviour. For example, the employer has made the employee's position at work untenable leaving the employee with no alternative but to quit his employment under protest. Although there is no actual dismissal by the employer, the end result is the same as if the employee had been fired.

In *Quah Swee Khoon v Sime Darby Bhd* [2001] 1 CLJ 9, *Gopal Sri Ram* JCA defined "constructive dismissal" as:

> "… There is no magic in the phrase. It simply means this. "An employer does not like a workman. He does not want to dismiss him and face the consequences. He wants to ease the workman out of his organisation. He wants to make the process as painless as possible for himself. He usually employs the subtlest of means. He may, under the guise of exercising the management power of transfer, demote the workman. That is what happened in *Wong Chee Hong* [1988] 1 CLJ 298 (Rep), [1988] 1 CLJ 45. Alternatively, he may take steps to reduce the workman in rank by giving him fewer or less prestigious responsibilities than previously held. Generally speaking, he will make life so unbearable for the workman so as to drive the latter out of employment. In the normal case, the workman being unable to tolerate the acts of oppression and victimisation will tender his resignation and leave the employer's services. …"

Constructive Dismissal is the 3rd most common type of dismissal suit heard in the Industrial Court

(Statistic Year Book 2006, Industrial Relations Department)

In *Kelang Container Terminal Sdn Bhd v Tuan Syed Khadzail bin Syed Salim* [1993] 1 ILR 1 (Award No 1/1993), the learned Chairman of the Industrial Court held as follows:

> "Constructive dismissal denotes conduct by an employer, amounting to a breach of contract such as entitles the workman himself to terminate the contract summarily (Award No 119/1980). The issue before this court is whether the company was guilty of conduct which was a significant breach going to the root of the contract of employment. Similarly whether the company had evinced or shown an intention not to be bound by the contract any longer and had led the claimant to say, 'I cannot work here. I must go.' An employer can place his employee in a position in which the employee really has no option but to tender his resignation. Normally the test for constructive dismissal is contractual. It is the unjustified treatment by the employer. The changes in hours, place or kind of work and then subsequently changing the terms of employee's work in any of those respects can make working life sufficiently trying to prompt resignation."

Breach of contract by the employer

In a constructive dismissal, the employer has to have repudiated or fundamentally breached the employee's employment contract either in an express (written term), or in an implied term.

Not all acts of unfairness by the employer would amount to a fundamental breach of contract; only the most serious acts could amount to a "fundamental" breach. For example, if the employer was simply a little rude on one occasion with an employee, this would probably not amount to a fundamental breach. But if the employer consistently bullied the employee, this would certainly amount to a fundamental breach of contract.

Conduct amounting to a breach of contract
The following are some examples of breaches of contract entitling the employee to claim constructive dismissal:

- Reducing or attempting to reduce an employee's wages or salary or other contractual benefits that the employee is entitled to under his terms of service.
- Not supporting the employee in difficult work situations.
- Harassing or humiliating the employee, particularly in the presence of other staff.
- Victimising or targeting the employee for no reason.
- Unilateral variation of the employee's job content or job scope without consultation or reasons.
- Making a significant change in the employee's job location at short notice.
- Falsely accusing the employee of misconduct such as theft or of being incapable of carrying out his job.
- Excessive demotion or disciplining of the employee.

Compensation paid out per case could well amount to RM500,000.

Implied breach of contract
A fundamental breach of an implied term of the employment contract of employment also entitles an employee to claim constructive dismissal. Examples of implied terms of the employment contract that may be breached by the employer are:

- the duty of maintain mutual trust and confidence
- putting an employee in cold storage
- relegation of job duties, and
- not giving any work or duties.

Conduct of employer need not be a single act

Conduct complained may consist of a series of acts or incidents, some may be quite trivial but cumulatively can amount to a breach which is calculated to destroy or seriously damage the relationship of confidence and trust between the employer and employee.
A "last straw" act that lead to the employee terminating the employment contract as a result of the employer's conduct does not have to be of the same character of the earlier acts, nor does it have to constitute unreasonable or blameworthy conduct, although in most cases it will do so.

Conditions to Constructive Dismissal

The Industrial Court in *Secure Guards Sdn Bhd v Her Bhajan Kaur* [1996] 2 ILR 1342 set out the conditions to be met before an employee can successfully claim that they had been constructively dismissed. The conditions are:

1. There must be a breach of contract by the employer, which may be either an actual breach or an anticipatory breach.
2. The breach must be sufficiently important to justify the employee resigning, or else it must be the last in a series of incidents which justify his/her leaving. However, a genuine, interpretation of the contract by the employer does not constitute repudiation in law.
3. The employee must leave soon in response to the breach and not for some unconnected reason.
4. The employee must not delay in terminating the contract in response to the employer's breach. If there is a delay, he/she will be deemed to have accepted the employer's breach.

If the employee leaves in circumstances where the above conditions are not met, the employee will be held to have resigned and there will be no dismissal.

Apart from the conditions above, it would be advisable for the employee to inform the employer why they are pleading constructive dismissal before walking out on the employer.

Burden of proof is on the employee

In a claim of constructive dismissal, the employee is responsible for proving that they have been constructively dismissed.

Once constructive dismissal is proven by the employee, the burden of showing whether the dismissal is with just cause and excuse falls on the company.

Length of time

The length of time is a crucial factor. The law requires that the employee leave soon after the breach.

In *Konnas Jet Cargo System Sdn Bhd v Shaik Badarudin Shaik Kamarudin*

> Constructive Dismissal lawsuits have grown by 267% from 2002-2006.

[2002] 1 ILR 651, the claimant continued to work in the company for one month and 19 days after the breach had occurred.

The Industrial Court considered the length of time factor and held the following:

> "Once an employee discovers that there is substantial breach or breaches of employment that goes to the root of the contract of employment he must act immediately either by protesting or giving notice to the employer and walking out of the job, otherwise he might be said to have affirmed the new terms of the contract. Thereby accepting it with the terms added."

Employer's response

The employer must respond to the letter from the employee claiming constructive dismissal. All allegations raised must be addressed.

If the employer remains silent, an adverse inference may be drawn against the employer that they have no explanation to offer and that the employee was justified in the claim. Alternatively, delay in responding is could draw an inference that the response given at a later date was an after-thought.

An example of a response from the employer is as follows:

Dear *[name]*,

Re: Breach of terms and conditions

We refer to your letter dated *[date]*.

We are indeed surprised to note the contents therein, particularly your allegation that the Company has breached the terms and conditions of your employment by [details]. We strictly deny your contentions above and wish to put on record that *[company's stand or defence to allegations]*.

In the circumstances, you are hereby requested to immediately report back to work, failing which we can only assume that you have abandoned employment.

Yours faithfully,
[designation of company official]

If you haven't taken steps to minimise your exposure to this risk, then you should start now. TG

*Contributed by **CCH Asia Pte Limited**. For further details, email mktg@cch.com.my.*

How sure are you ...

... that your current employment practice meets the minimum **mandatory** employment standards?

Of course you have been abiding with the Malaysian employment law and practice but how much do you know about the recent amendments to the *Employees Provident Fund Act 1991* (EPF Act) and the *Employment Act 1955* (EA)?

The *Employment* Act covers the rights of workers and employers in the working relationship where it provides minimum benefits and rights of employees such as overtime rates, working hours, annual leave and public holidays, sick leave, maternity protection, etc. The Act also covers issues such as termination, retirement and retrenchment. The employment standards stipulated in the Act are mandatory for employers. Failure to comply with these standards could result in a fine not exceeding RM10,000 as well as compounds. A good and responsible employer always ensures that their current employment policies are compliant with the latest developments in Employment Law.

Employment Act 1955 • Employees Provident Fund Act 1991 with Regulations and Rules

CCH's latest book on **Employment Act 1955 • Employees Provident Fund Act 1991** ***with Regulations and Rules*** consolidates the latest amendments on the employment law as well as their related Regulations and Rules in full text.

Best of all, this book comes with CCH's much appreciated and well-loved feature — ***complete historical data of the amendments*** to the Acts. With these history notes, plus other useful features such as topical indexing, lists of amending legislation and quick reference subsection headings, you can be sure of getting your money's worth ... and a far superior employment law reference book.

NEW!

✓ Soft cover bound book
✓ 472 pages

- No more scouring through HR employment law references or the Internet to find out what the law was before the latest amendments. This book comes with complete history notes of all the amendments made to the Acts since 1981.
- Includes all the amendments in the Employees Provident Fund (Amendment) Act 2007 which are in operation as at 30 September 2008.

Most important of all, problem solved!

Order Form — Fax : 03.2026.7003 — Order Ref : MA 147

Title	Code	Retail Price (RM)	Qty	Amount (RM)
Employment Act 1955 • Employees Provident Fund Act 1991 with Regulations and Rules	**1765M**	**60**		
☐ I would like to subscribe to eBiz Alert *(please fill up your contact details below including email addresses)* About eBiz Alert - eBiz Alert is a free all-in-one monthly business e-newsletter that delivers concise current issues, trends and regulatory watch to the subscriber. It covers topic areas on Tax & Accounting, Corporate Law, Human Resource and overall business/ economy in the Asia Pacific region and globally.				***FREE***
			Total Amount	

Payment Option

☐ I enclose a cheque made payable to **"Commerce Clearing House (M) Sdn Bhd"**

Cheque No. _____ RM _____

☐ Please debit my ○ Visa ○ MasterCard RM _____

Card No.: ☐☐☐☐-☐☐☐☐-☐☐☐☐-☐☐☐☐ Expiry Date ____/____

Card Holder's Name: _____ Card Holder's Signature: _____

Contact Details

Mr/Ms Name: _____ Job Title: _____

Company: _____ Business Registration No.: _____ Business Nature: _____
(As per business registration)

Company Size ☐ 1-4 ☐ 5-9 ☐ 10-19 ☐ 20-49 ☐ 50-99 ☐ 100-199 ☐ 200-499 ☐ 500-999 ☐ 1000+

Address: _____

_____ Postcode: _____ State: _____

Tel: _____ Fax: _____ Email: _____
(Important to receive future special updates/news)

Authorised Signature & Company Stamp

Date

Terms & Conditions:

1. Order is subject to acceptance by CCH.
2. Price(s) is valid in Malaysia and is subject to change without prior notice.
3. Book(s) will only be delivered upon receipt of payment.
4. Good(s) sold is not returnable. If the book is received in an unsatisfactory condition, it should be exchanged within a week of receipt.

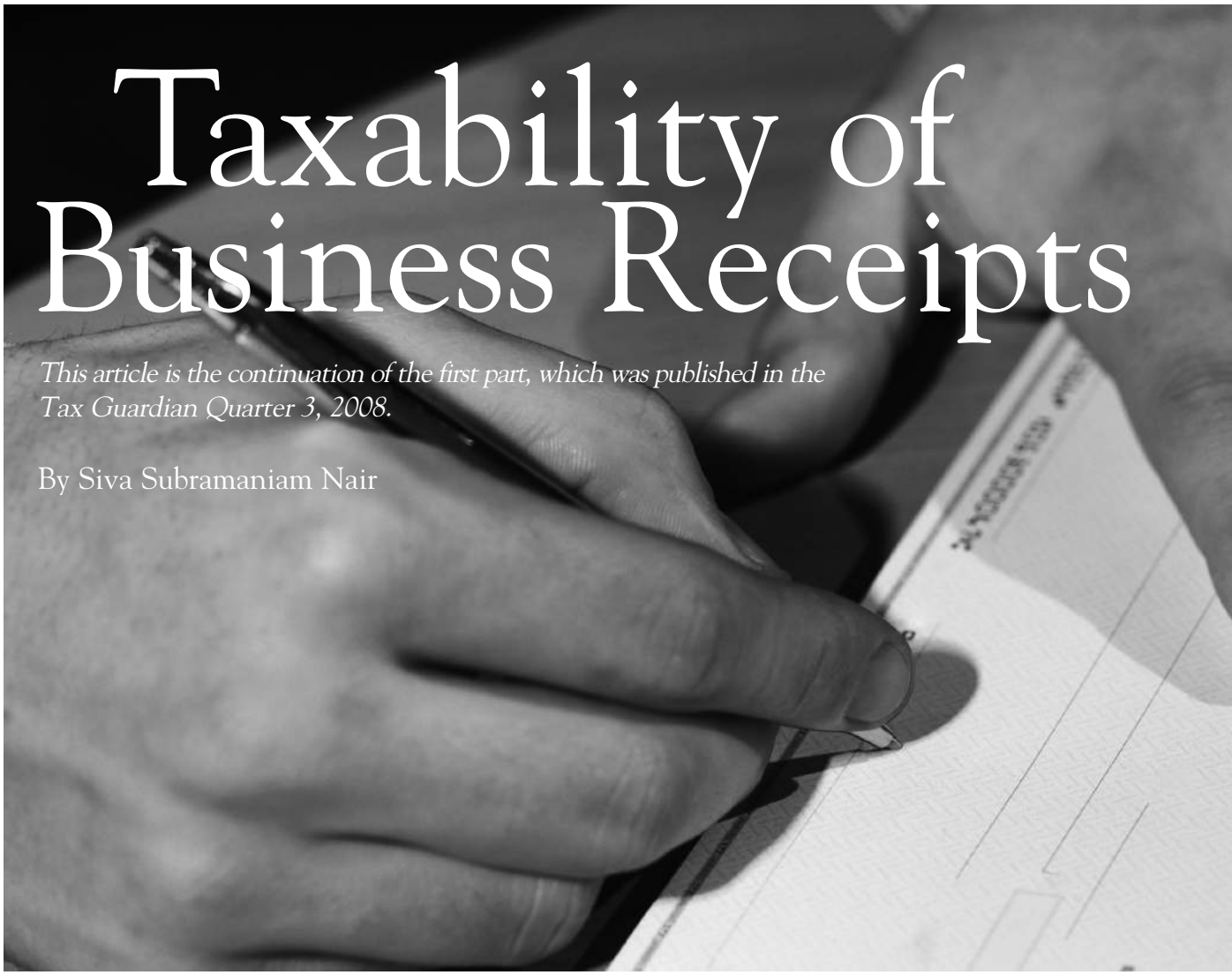
CCH
a Wolters Kluwer business

Commerce Clearing House (M) Sdn Bhd (000000-H)
Suite 9.3, 9th Floor, Menara Weld, No. 76, Jalan Raja Chulan, 50200 Kuala Lumpur, Malaysia.
Toll Free Customer Service Hotline: 1-800-181-151
Fax: 603 2026 7003
Website: www.cch.com.my
Email: mktg@cch.com.my

Taxability of Business Receipts

This article is the continuation of the first part, which was published in the Tax Guardian Quarter 3, 2008.

By Siva Subramaniam Nair



In the last article we looked at the overall tax treatment for bad debts and provision for doubtful debts. We shall continue now by discussing the tax treatment of release of debt by a creditor and withdrawal of stocks.

Release of debts

Let us go back and look at fundamental accounting. When we purchase stocks, the entry we make is:

Dr. Purchases
Cr. Trade creditors

Obviously, the purchases are deductible in ascertaining the adjusted income of the business.

Subsequently, if the creditor waives the debt or part of the debt owing is released, a reversal entry is effected in the accounts.

Dr. Trade creditors
Cr. Other/Miscellaneous income

Since a deduction was allowed earlier, we should logically tax the amount so waived. This is provided for in s 30(4) of the *Income Tax Act 1967* .

Legislation

Section 30(4)

Where –

(a) a deduction has been made under s 33(1) in computing the adjusted income of the relevant person from a business for the basis period for a year of assessment (that basis period being prior to the relevant period) in respect of any outgoing or expense (including any sum payable, rent payable or expense incurred of the kind described in para 33(1)(a), (b) or (c)); or

(b) any allowance or aggregate amount of allowances has been made under s 4 in computing the statutory income of the relevant person from a business for the basis period for a year of assessment (that basis period being prior to the relevant period) in respect of any expenditure incurred under Sch 3,

and the whole or any part of a debt in respect of any such outgoing, expense, sum, rent or expenditure is released in the relevant period, the amount released shall be treated as gross income of the relevant person from that business for the relevant period.

Example 1

A Sdn Bhd (year-end 31st October) purchased RM500,000 worth of stocks from B Sdn Bhd on 15 October 2007 to be settled in five instalments and claimed a full deduction for it in YA 2007. It settled all the instalments except for the last one. On 15 December 2008, B Sdn Bhd decided to release A Sdn Bhd from the balance debt of RM100,000 because the company was facing severe financial difficulties.

The RM100,000 will be taxed on B Sdn Bhd as gross income from business in YA 2009.

In the absence of a definition for the word "release" the learned judge in *Hall v CIR* 11 TC 24 stated:

> *"It is clear that you cannot simply release a debt by saying 'I forgive you'. It is not a legal transaction. You must get consideration for the release or some legal formality which implies consideration such as release under seal …"*
>
> *… 'Release' does not mean a mere failure to pursue the debt nor is there a release if the debt has merely become statute barred. A debt remains a debt notwithstanding that the right to institute legal proceeding for its recovery is time barred. It must be remembered that 'release' is relevant only to ascertain undisputed debts."*

Therefore, this section is not applicable to debts which are disputed and subsequently compromised. Situations where a debt owing is no longer payable is considered a "release of debt" include:

- where there is a formal composition or arrangement of the creditors by which they agree to forego the whole or part of the amount owing to them and where such scheme proposed by the creditors is approved by the court
- where the surety or guarantor pays the creditor, *there is no release.* However now the surety or guarantor himself becomes the creditor and if subsequently waives the debt, then it is a release of the debt
- where a formal waiver of any sort is obtained.

Similarly, the following circumstances do not constitute a release of the debt:

- where a creditor fails to demand payment. This could be due to an oversight by him or due to business courtesy. However, the debt is still owing and subsequently will have to be settled
- where the debtor has become bankrupt, it does not constitute a release because subsequently, when debtor comes out of bankruptcy, he still owes the amount outstanding to the creditor
- where the debt is sold or factored to a third party, the debt is still in place; only it is now owed to the third party.

Prior to YA 2007, there was no legislation to provide for circumstances where capital allowances were claimed in respect of any expenditure incurred that is subsequently released. However, with the introduction of s 30(4)(b), such expenditure so released will be treated as gross income in the period that the debt is released.

Example 2

Mr C took a personal loan from his friend to purchase a photocopier for RM10,000 in YA 2005. For the years of assessment 2005 to 2008, he would have claimed capital allowances of RM as shown below:

	RM
Qualifying expenditure	10,000
IA (20%)	(2,000)
AA (14% X 4 years)	(5,600)
Residual expenditure	2,400

In February 2009, the loan balance of RM1,000 was waived by his friend.

The amount of RM1,000 will be taxed as gross income for Mr C in his tax computation for YA 2009.

Withdrawal of stock

Stock being withdrawn for personal use, for donations or given away as a gift, is a common item in accounting. For example, if I operate a grocery store, obviously I will take provisions for my own use from my store (if available) as opposed to buying it elsewhere. The treatment of such drawings is addressed in s 24 of ITA.

Legislation

Section 24(2)

Where in the relevant period any stock in trade of a business of the relevant person is –

(a) withdrawn for his own use; or

(b) withdrawn (otherwise than on requisition or compulsory acquisition or in a similar manner) without any consideration being received therefor or for a consideration consisting of –

(i) any property not being either a debt owing to the relevant person or a sum in cash or the equivalent of cash;

(ii) any such property together with a debt owing to the relevant person or any such sum; or

(iii) any such property together with a debt owing to the relevant person and any such sum,

then, subject to subsection (3), an amount equal to the market value of that stock in trade at the time of its withdrawal shall be treated as gross income of the relevant person from the business for the relevant period.

Section 24(3)

Where in a case to which subsection (2) applies the consideration for the withdrawal of any stock in trade is consideration of the kind described in subparagraph (b)(ii) or (iii) of that subsection, then, for the purposes of that subsection –

(a) the amount of the market value of that stock in trade shall be reduced by the amount of the debt or sum or the amount of the debt and sum, as the case may be, referred to in whichever of those subparagraphs applies to the case;

(b) subsection (1) shall apply to the debt as if it were a debt arising on the sale of that stock in trade; and

(c) s 28 shall apply to any such sum.

The general rule here is that where trading stock is withdrawn for a taxpayer's own use, the market value of the trading stock at the time of withdrawal forms part of the gross income.

Also where trading stock is withdrawn from a taxpayer's business without any consideration or for consideration consisting of property, then the market value of the trading stock at the time of withdrawal forms part of the gross income.

Sharkey v Wernher 36 TC 275
The taxpayer's wife carried on the trade of a stud-farm with the cost of keeping the horses being allowed as a deduction. When five horses were transferred from the stud-farm to a racing stable also owned by the wife, the stud-farm was credited with the estimated cost of the horses. This is a widespread practice that is recommended by accountants to be used whenever a proprietor withdraws some of the trading stock for his personal use or consumption because to credit the market price would lead to the unhappy result that profits could emerge in the accounts solely on this account.

However, the courts confirmed that the use of market value would be the correct treatment in this case. This is consistent with the Malaysian provisions detailed above. In this case their Lordships went even further and appeared to have held (at least by implication) that one can even make a profit from "selling" trading stock to oneself.

One difficulty in this case was the nature of the item as it was produced by the trader, ie the horses. In a case where the items are purchased from a supplier, the application of this principle can be easily avoided by the proprietor making additional purchases directly from the supplier in his own name and paying for it.

Of course there are cases where this principle has been rejected. In *Kikabhai Premchand v CIT* 24 ITR 506, the Supreme Court held that where stock is carried in the books year after year at cost, its withdrawal from the business is also to be at cost, and **NOT** market value. Also in *Mason v Innes* 44 TC 326, the attempt by the Revenue to apply the principle of *Sharkey and Wernher* to an author's assignment of rights in a book by way of a gift to his father, was held to be "unthinkable" by the judge.

However, in Malaysia the law is very clear on this matter, ie market value is gross income except for example,

- where trading stock is withdrawn from a taxpayer's business for a consideration of a property and a debt owing, then the market value of the trading stock reduced by the amount of debt forms part of the gross income. Obviously, when a debt is recorded the credit has to be to an income account therefore, to recognise the whole market value would result in double counting, or
- where a trader chooses to give away or throw away trading stock then the market value of the trading stock forms part of the gross income. However, if the trader wishes to throw away the stock it is probably obsolete or not usable therefore, the market value will probably be zero.

Example 3
D Sdn Bhd, a company manufacturing office equipment, donated a typewriter costing RM1,500 to an old folks' home, which was an approved institution The cost was included in the cost of sales but the donation was not recorded. The selling price was RM2,000.

Trading stock disposed of by way of a donation is a deemed sale. It is deemed to have been disposed of at market value. The whole RM2,000 should be brought to tax but since the cost is already included in the cost of sales, effectively we are only taxing the gain of RM500 just like a normal sale.

Example 4
What if in example 3, D Sdn Bhd had reversed the RM1,500 cost of the typewriter from the cost of sales?

The amount to be brought to tax should only be the gain of RM500.

Example 5
What if in example 3, the company also sold an office cabinet costing RM800 (included in cost of sales) to a staff at 10% discount? The selling price was RM1,000.

The company would have recorded the transaction as

Dr.	Bank	900
Dr.	Staff benefits	100
Cr.	Sales	1,000

In this case, no adjustment is needed because the whole market value of RM1,000 has been brought to tax (as sales), plus staff benefits is a deductible expenditure for tax purposes.

That concludes our discussion on the taxability of debt released by a creditor and the drawings of stock. In my next article, I shall discuss the adjustments to be made to profit before tax in a tax computation for ascertaining the adjusted income from a source. TG

Further Reading

- Choong, KF: Malaysian Taxation – Principles and Practice, (Latest Edition), Infoworld.
- Kasipillai, J: A Comprehensive Guide to Malaysian Taxation under Self Assessment, (Latest Edition), McGraw Hill.
- Malaysian Master Tax Guide, (2008), CCH Asia Pte Ltd.
- Singh, Veerinderjeet: Veerinder on Taxation, Arah Pendidikan Sdn Bhd.
- Thornton, Richard: Thornton's Malaysian Tax Commentaries, (Latest Edition) Sweet & Maxwell, Asia.
- Thornton, Richard: 100 Ways to Save Tax in Malaysia for Small Businesses (latest edition), Sweet & Maxwell Asia.
- Yeo, Miow Cheng Alan: Malaysian Taxation, (Latest Edition), PAAC Sdn Bhd.

Siva Subramanian Nair is a freelance lecturer preparing students for the professional examinations of the ACCA, MICPA and AIA and undergraduates of degree programmes in both local and foreign universities He is an examiner for one of the professional bodies in Malaysia and a member of the marking team for the Advanced Taxation paper for the ACCA examination. He can be contacted at sivanair@tm.net.my.

Global Business, Global Talents

As business becomes more global, so are talents on cross-border assignments. However, organisations struggle with the many issues that go beyond the domestic HR matters. One of the many challenges is taxation issues in expatriate management. Commonly found taxation issues include:

- implications of worldwide taxation on expatriate remuneration
- how certain assignment conditions, assignee's activities or inter-company recharging mechanism can impact the company's liability
- how transfer pricing is relevant to international assignments
- who is responsible for home country tax liabilities, host country tax liabilities and tax liabilities in third countries
- how international assignments provide opportunities for tax planning such as cash vs. benefits in kind, cash vs. reimbursements, deferred payments and leases, etc.
- how timing and duration of the assignment as well as repatriation can affect the tax liability of the employee (or company) both in the home and host locations (and sometimes in other jurisdictions)
- how to draw up an attractive expatriate compensation model for the employer and employee
- currency issues in expatriate management.

If you are regularly managing a pool of mobile talents in Asia, CCH's latest addition, ***Guide to International Assignment Management in Asia*** is just what you need. Available for Singapore • China • Hong Kong • India • Malaysia, this only authoritative commentary guide brings you:

- quality coverage on taxation and social security issues
- addresses on international assignments' challenges and considerations unique to each country
- highlights on HR administrative models recommended for each country in managing international assignments
- provides information to measure costing, budgeting and Return of Investment (ROI) of international assignments
- time-saving features such as comparison tables and templates

Ultimately, a well structured expatriate package means tax efficiency for both employer and employee. Email us today at mktg@cch.com.my to find out how ***Guide to International Assignment Management in Asia*** can help your work

Notice Board

Notice of issuance of investigation and disciplinary rules

Please be informed that the Investigation and Disciplinary Rules drafted by the Disciplinary Committee have been approved by the Council. The Rules shall take immediate effect. A copy of the Rules may be downloaded from the Institute's website at Technical > Technical Developments – Direct Taxation > Practice Developments > Rules and Regulations
A copy of the Rules can be downloaded at www.mit.org.my.

Parallel existence of the Single-Tier System and the Imputation System

The Inland Revenue Board (IRB) has issued a letter dated 13 August 2008 to the Institute stating the following position:

	Type of Shares	Mode of Dividend Paid	Tax Treatment
(a)	Ordinary Shares	Dividend paid in specie	Single Tier Dividend (Section 108 Balance unchanged)
(b)	Preference Shares	Dividend paid in cash	Single Tier Dividend (Section 108 Balance unchanged)
		Dividend paid in specie	Single Tier Dividend (Section 108 Balance unchanged)

A copy of the IRB's letter can be downloaded at www.mit.org.my

Operational guidelines

The Inland Revenue Board (IRB) has issued the following Operational Guidelines (GPHDN) on 2 September 2008. The guidelines are also available on the Institute's website.

(i) *Utilisation of Companies' Income Tax Credit as Set Off (GPHDN 1/2008)*
This guideline sets out the basic rules and procedures for utilising the tax credit by a company.

(ii) *Furnishing a Lower Tax Estimate than the Prescribed Minimum (GPHDN 2/2008)*
This guideline stipulates the procedure for furnishing an estimated tax liability which is lower than that prescribed under s 107C(3), ie not less than 85% of the revised estimate of tax payable for the immediately preceding year of assessment and the factors which the IRB will consider in allowing such application.

(iii) *Remission of Increase in Tax (GPHDN 3/2008)*
This guideline lists out the factors that the IRB will consider for a possible waiver of a tax penalty on late payment and underestimation of tax liability.

SC guideline on REITS - (Rev 210808)

The Securities Commission (SC) has issued the revised Guidelines on Real Estate Investment Trusts on 21 August 2008. A copy of the Guidelines may be downloaded from the website of SC.

Preparation of worksheets (Helaian Kerja)

The Inland Revenue Board (IRB) has issued a letter to the professional bodies dated 24 October 2008 clarifying that the worksheets (ie Helaian Kerja) are provided only as a guide. Taxpayers and tax agents are free to prepare their own working papers or formats for tax computation purposes. What is essential is that taxpayers must be able to support the relevant claims made in a tax computation in the event of a tax audit. For repayment or refund cases, the worksheet HK3 or other relevant worksheets must be prepared and submitted to the IRB. A soft copy of the IRB's letter can be downloaded at www.mit.org.my.

Service tax – extension of scope of taxable services for the advertising industry

The implementation of the directive to subject all advertising costs, involving those of production houses and printing companies as announced in e-MIT No. 35/2008, has been deferred until further notice from the Royal Customs, Malaysia.

Public relation officers for tax clearance letters

The IRB has released a list of public relations officers who can be contacted to expedite the issuance of Tax Clearance Letters. The list can be viewed on both the websites of the Inland Revenue Board (IRB) and MIT.

Remission of penalty on service tax

The Royal Customs Malaysia has issued a circular on 6 October 2008 informing that for companies providing professional, consultancy and management services that are licensed in 2008, the penalty imposed in respect of service tax for taxable period from January to June 2008 will be remitted, provided that service tax has not been collected from clients/customers.

It was clarified over telephone conversation with the Internal Tax Division that the penalty referred to in the circular is the late payment penalty under s 16 of the *Service Tax Act 1975*. The relevant RCM circular has been uploaded to the Institute's website. Members may contact Tuan Hj Md Basri bin Bahron of RCM, Internal Tax Division, at 03-8882 2424 for further clarification.

2009 Budget Commentary and Tax Information

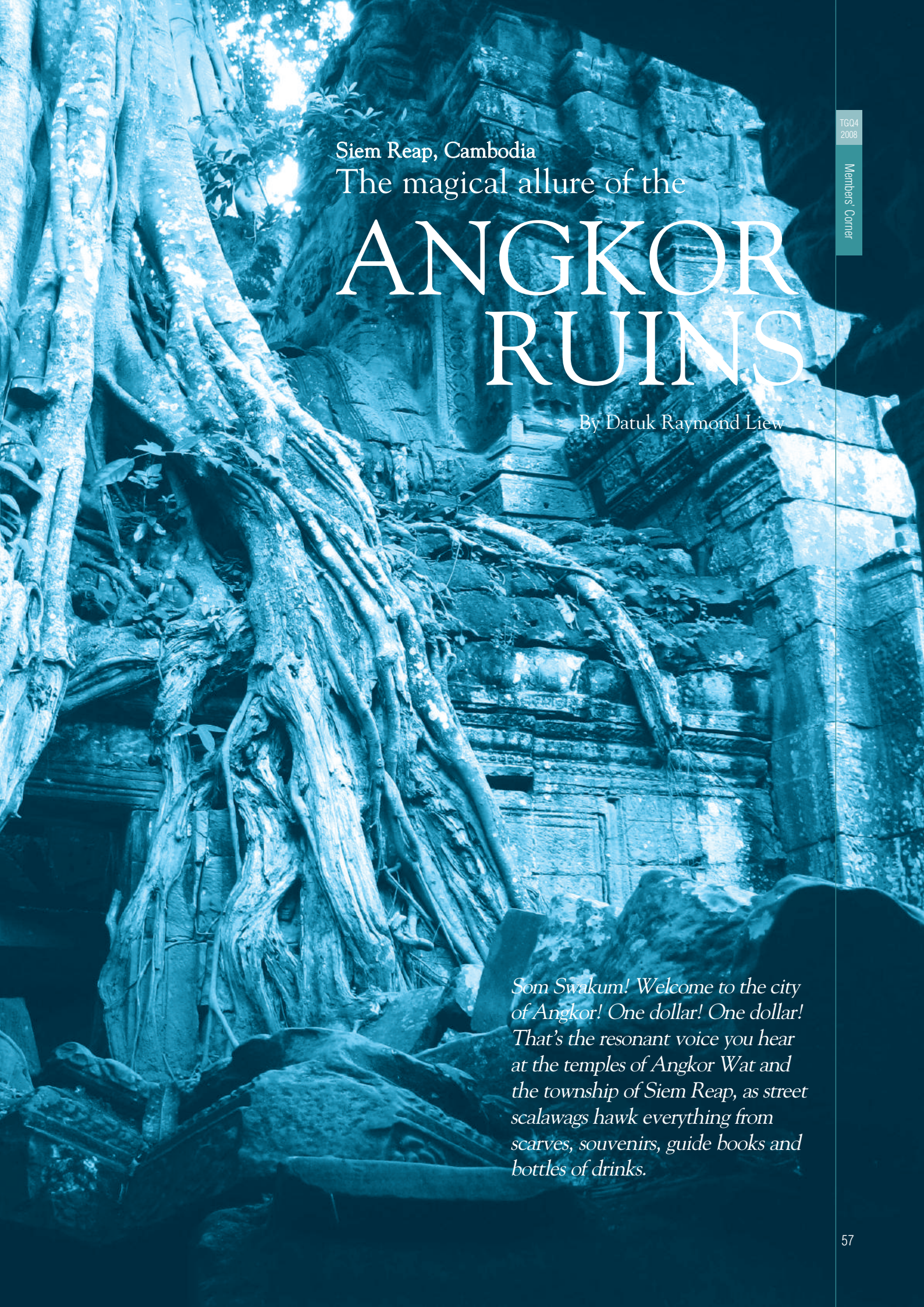
The Institute has issued the amended pages of 105 and 106 in Chapter B8 of the 2009 Budget Commentary and Tax Information. The amendments were due to typesetting alignment problems and we apologise for any inconvenience caused. Members who have yet to receive it, can download it at www.mit.org.my. TG

Siem Reap, Cambodia

The magical allure of the

ANGKOR RUINS

By Datuk Raymond Liew



Som Swakum! Welcome to the city of Angkor! One dollar! One dollar! That's the resonant voice you hear at the temples of Angkor Wat and the township of Siem Reap, as street scalawags hawk everything from scarves, souvenirs, guide books and bottles of drinks.

Angkor temples

Cambodia is a country with a well documented history and Siem Reap is the entry point to the world famous Angkor Temples. Today, thanks to these consecrated temples, Siem Reap has geared itself to meet the many challenges of attracting tourists from all over the world. For many people the main attraction when you travel to Siem Reap is the magnificent temples of the nearby Angkor temple nucleus which the United Nations Education, Scientific and Cultural Organisation (UNESCO) has recognised it as a World Heritage Site, preserved for the people of the world. It is not just one temple, but more than100 temples of different shapes and sizes. Apparently, there are around 1,000 religious sites scattered over a 3,000 square km area in the northern Cambodia plains near Asia's largest inland lake, Tonle Sap.

The two most renowned temples – Angkor Wat & Angkor Thom

Naturally, the jewel in the country's tourism crown is none other than Angkor Wat, which is considered the world's largest religious site.

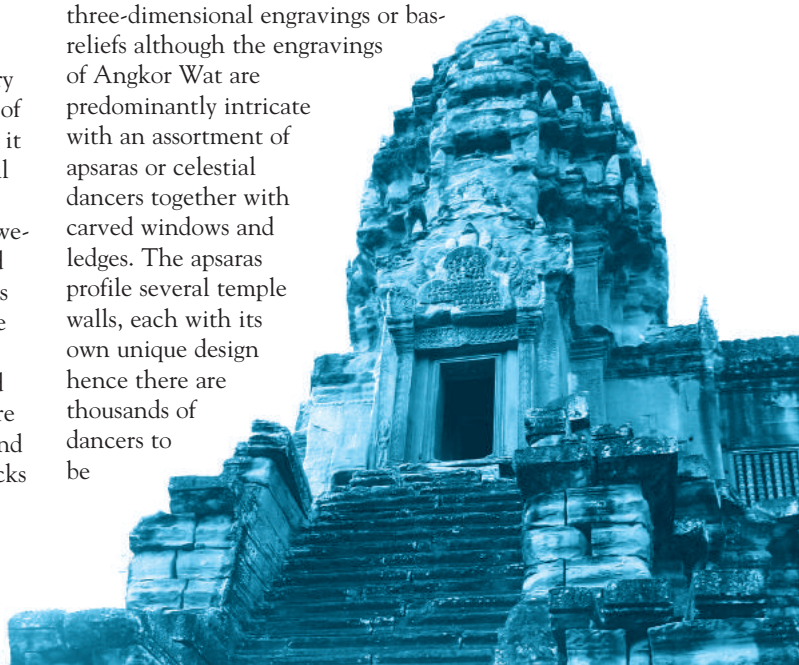
Take a closer look at the numinous faces imprinted on the rocks as well as the splendor of Angkor Wat and when you zigzag through the sandstone corridors of these sacrosanct temples, you can almost picture yourself fighting off the bandits among the giant tree roots like the infamous archaeologist, Indiana Jones. Even Angelina Jolie, the heroin in the film Lara Croft – The Tomb Raiders, fought off the bad guys among the giant tree roots that somehow swallowed up the Ta Prohm ruins of Angkor Thom. The temple, Ta Prohm remains among the entwining roots of massive trees intentionally left by archaeologists to exhibit to visitors what it looked like in the 19th century when first explored by western archaeologists. The giant roots of these large rainforest trees and strangler figs have engulfed much of the archways of Ta Prohm. Miraculously, the roots of these massive rainforest trees have somehow managed to work their way through the narrowest of cracks forcing many of the stonework walls to crack and crumble.

A temple is never complete without the presence of gentle Buddhist monks mainly attired in bright saffron robes with huge smiling faces of bodhisattva Avalokiteshvara at the picturesque Bayon Temple, located in the heart of the walled city of Angkor Thom. One may ask, what's so picturesque of the Bayon Temple? This temple is legendary for its stone faces gazing benevolently from the four sides of a tower. Within the temple are 51 smaller towers, believe it or not, each with its own four smiling faces with historical scenes of everyday life and events "documented" or engraved in the bas-reliefs along the outer walls. These awe-inspiring tasks, are both inspirational and fascinating, and show how forward thinking these people of the olden days were. Mind you, the original temples date back to the late 9th century with the last completed in the 12th century. What is mind-boggling is that these high towers and solid gigantic rocks were put together at a time when there were no powerful cranes, tractors or sophisticated equipment and machinery. What is also amazing is that these gigantic rocks

and high towers were piled on top of each other with no cement to seal them together and yet until today, they stand elevated and tall with pride.

The main temple is still Angkor Wat although Angkor Thom is equally impressive. Unlike other temples, Angkor Wat has many faces depending on the time of day and also the season. Most would prefer the wet season since the wet grounds of Angkor Wat present a great photographic opportunity for many keen photographers.

Indeed, most of the sandstone walls of these temples contain three-dimensional engravings or bas-reliefs although the engravings of Angkor Wat are predominantly intricate with an assortment of apsaras or celestial dancers together with carved windows and ledges. The apsaras profile several temple walls, each with its own unique design hence there are thousands of dancers to be



seen especially in Angkor Wat, which covers an impressive rectangular area of 205ha with a moat and laterite walls on its periphery. When viewed from the front entrance of the temple, it looks sparsely vegetated. However, the aerial view shows Angkor Wat standing out from the forest and certainly within the walls of Angkor Wat, the temples look like they are rising above the forest!

Exploring the sacred grounds of these temples would certainly take its toll on your poor feet and if you are unaccustomed to climbing hundreds of steep steps, your bones would soon ache in no time at all. But worry no more for Seap Reap is now a chic and trendy town that offers soothing foot massages in an air-conditioning environment which is heavenly after the stifling heat outside. For travelers who appreciate fine dining and other indulgent luxuries, this town offers one of the finest French cuisine – after all, the French once ruled this part of the world! If you are dead tired after climbing all the giant steps of the temples, tuk-tuks are readily available around the city centre for just one American dollar! What is fascinating is that everything, be it souvenirs, guide books or even a bottle of mineral water or a canned drink, is only one American dollar! Incidentally, the local currency is the riel – pronounced real, but the American dollar is the currency of choice.

After the exploration of the sacred temples, you must pay a visit to the Night Market, which is an enchanting bazaar where you can wander around and browse through the varied local merchandise on offer and of course end the night with a visit to Pub Street, where beers and drinks are aplenty. Do try the local cuisine especially Siem Reap's signature dish– amok curry which unlike our Malaysian curry is less spicy but nevertheless, tasty and yummy. For the more daring, how about tarantula spiders for a meal?

To complete the expedition, you must take a boat ride at Tonle Sap, the largest freshwater lake in Southeast Asia. The lake is rich in biodiversity where the floodplain is packed with a large variety of fish which provides food to the villages surrounding it. For the most part of the year, the lake is fairly small but during the wet monsoon, the lake is filled with water from the Mekong River, widening its surroundings thereby enabling the inhabitants to fish abundantly during this short period to supplement their income. Oh, yes, don't be surprised for during the boat ride, you will be pursued by boat scalawags, peddling the sale of soft drinks, mineral water or even a photo session with a sea python – scary huh? Yes, all this for just one American dollar!

So remember, when you visit this fascinating place, do bring lots of US$1 bills, for change is hard to come by and local currency is somewhat confusing. TG

Datuk Raymond Liew is a Chartered Accountant who loves cross-cultural exploration. He can be contacted at raymondliew@parkerrandall.com.

BiZZTAX,
Your lifetime partner in solutions integration...
and integration of solutions.

Taxation
Secretarial
Accounting

Everything goes better with BiZZTAX...
Your trustworthy & reliable partner.

Call
03-8061 0002
learn how BiZZTAX
can integrate seamlessly for you

Total
Integrated
Solutions

BiZZTAX

Tel : 603-8061 0002 Fax : 603-80626 805 WebSite : www.BiZZTAX.com