tax guardian

Vol.2/No.2/2009/Q2 RM28.00

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CHARTERED TAX INSTITUTE OF MALAYSIA

Tax Audit Issues for Individuals and Partnerships – A Roundtable Discussion

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CHARTERED TAX INSTITUTE OF MALAYSIA

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Official Journal of the Chartered Tax Institute of Malaysia

ISSN 0128-7583
9 770128 758008
KDN PP 7829/06/2010 (024677)

Continuing Professional Development (CPD)
CALENDAR OF EVENTS 3RD QUARTER 2009

july

Date	Training Programme	CPD Points	Venue	Fee (RM) Member	Fee (RM) Member's Firm Staff	Fee (RM) Non-member	Speaker
8 Jul 2009 9.00am - 5.00pm	Workshop: Practical Implications on New Public Rulings *(postponed from 9 Apr)*	8	Kota Kinabalu	315	365	415	Chow Chee Yen
8 Jul 2009 9.00am - 5.00pm	Workshop: Cross Border Transactions & Withholding Tax	8	Kuala Lumpur	330	380	440	Harvindar Singh
9 Jul 2009 9.00am - 5.00pm	Workshop: Practical Implications on New Public Rulings *(postponed from 10 Apr)*	8	Kuching	315	365	415	Chow Chee Yen
15 Jul 2009 9.00am - 5.00pm	Workshop: Latest updates on Tax Exemption for Employment Income & Individual Tax Statutory Requirements	8	Ipoh	315	365	415	Chow Chee Yen
16 Jul 2009 9.00am - 5.00pm	Workshop: Latest updates on Tax Exemptions for Employment Income & Individual Tax Statutory Requirements	8	Malacca	315	365	415	Chow Chee Yen
22 Jul 2009 9.00am - 5.00pm	Workshop: Latest updates on Tax Exemptions for Employment Income & Individual Tax Statutory Requirements	8	Penang	315	365	415	Chow Chee Yen
23 Jul 2009 9.00am - 5.00pm	Workshop: Basic Tax Practice & Principles - Module 1 (in collaboration with MAICSA)	8	Kuala Lumpur	330	380	440	Harvindar Singh
23 Jul 2009 9.00am - 5.00pm	Workshop: Latest updates on Tax Exemptions for Employment Income & Individual Tax Statutory Requirements	8	Johor Bahru	315	365	415	Chow Chee Yen

august

Date	Training Programme	CPD Points	Venue	Fee (RM) Member	Fee (RM) Member's Firm Staff	Fee (RM) Non-member	Speaker
4-5 Aug 2009 9.00am - 5.00pm	**National Tax Conference 2009**	25	Kuala Lumpur	Early bird 900 Normal 1100	Early bird 1000 Normal 1200	Early bird 1100 Normal 1300	Local and International Speakers
17 Aug 2009 9.00am - 5.00pm	Workshop: To be advised	8	Kuala Lumpur	330	380	440	Harvindar Singh
20 Aug 2009 9.00am - 5.00pm	Workshop: Basic Tax Practice & Principles - Module 2 (in collaboration with MAICSA)	8	Kuala Lumpur	330	380	440	Harvindar Singh
24 Aug 2009 9.00am - 5.00pm	Workshop: To be advised	8	Kuala Lumpur	330	380	440	Harvindar Singh
27 Aug 2009 9.00am - 5.00pm	Workshop: Latest updates on Tax Exemptions for Employment Income & Individual Tax Statutory Requirements	8	Kota Kinabalu	315	365	415	Chow Chee Yen
28 Aug2009 9.00am - 5.00pm	Workshop: Latest updates on Tax Exemptions for Employment Income & Individual Tax Statutory Requirements	8	Kuching	315	365	415	Chow Chee Yen

september

Date	Training Programme	CPD Points	Venue	Fee (RM) Member	Fee (RM) Member's Firm Staff	Fee (RM) Non-member	Speaker
2 Sep2009 9.00am - 5.00pm	Workshop: To be advised	8	Kuala Lumpur	330	380	440	Chow Chee Yen
3 Sep 2009 9.00am - 5.00pm	Workshop: To be advised	8	Malacca	315	365	415	Chow Chee Yen
9 Sep 2009 9.00am - 5.00pm	Workshop: Investment Incentives	8	Kuala Lumpur	330	380	440	Sivaram Nagappan
14 Sep 2009 9.00am - 5.00pm	Workshop: To be advised	8	Penang	315	365	415	Chow Chee Yen
15 Sep 2009 9.00am - 5.00pm	Workshop: To be advised	8	Johor Bahru	315	365	415	Chow Chee Yen
29 Sep 2009 9.00am - 5.00pm	Workshop: To be advised	8	Ipoh	315	365	415	Chow Chee Yen
30 Sep 2009 9.00am - 5.00pm	Workshop: Basic Tax Practice & Principles - Module 3 (in collaboration with MAICSA)	8	Kuala Lumpur	330	380	440	Harvindar Singh

DISCLAIMER: CTIM reserves the right to change the speaker(s)/date(s), venue and/or cancel the events without notice at their discretion.
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The Chartered Tax Institute of Malaysia ("CTIM") is a company limited by guarantee incorporated on 1 October 1991 under Section 16(4) of the *Companies Act 1965*. The Institute's mission is to be the premier body providing effective institutional support to members and promoting convergence of 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 an effective secretariat.

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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

CTIM Branch Offices/Chairman 2009-2010

East Coast Branch
Mr Wong Seng Chong
Messrs Lau, Wong & Yeo
1, 2nd Floor, Lorong Pasar Baru 1
25000 Kuantan, Pahang

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Mr Viknesvaran s/o Arumugam
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40-A, Taman Kota Laksamana
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Ms Tan Lay Beng
Tee & Partners
Room 335, 3rd Floor
Johor Tower, Jalan Gereja
80100 Johor Bahru, Johor

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Mr Andrew Ewe Keang Teong
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Unit 41-5-1, 5th Floor, Wisma Prudential
41 Jalan Cantonment
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Perak Branch
Mr Loo Thin Tuck
No. 5-2A, Jalan Medan Ipoh 10
Bandar Baru Medan Ipoh,
31400 Ipoh, Perak.

Sarawak Branch
Ms Regina Lau
KPMG Tax Services Sdn Bhd
Level 6, Westmoore House, Twin Tower Centre,
Rock Road, 93200 Kuching
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Editorial Note

12 March 2009 will be a historic day in the Institute calendar for many years to come. It was the day when the Institute was renamed Chartered Tax Institute of Malaysia (CTIM). It was also the day when the logo CTIM was adopted.

The new name and the logo is part of the Institute's rebranding exercise to enhance the Institute's image and it also symbolises professionalism.

Ultimately, in difficult economic times such as the one we are facing today, it is important that the organisation re-examines itself and is prepared to face changes that will be forced upon due to the changing circumstances. The change of the name and logo clearly reflects the Institute's willingness to transform itself to face the future.

In this issue, focus has also been given to address the needs of a very large group of our own members who are dealing with taxes affecting individuals and partnerships involving SG and OG cases with the Inland Revenue Board (IRB). This has been done through our cover story via a roundtable discussion.

There are many other interesting articles in this issue that will be of significant interest to our readers along with our regular features which are also covered in the issue.

Finally, I'll leave you with a thought.

"You must be the change you want to see in the world"
(Mahatma Ghandi, 1869-1948)

SM Thaneermalai
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.

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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:

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Please cross cheque made payable to **CTIM-NTC** and mail payment together with registration form to the above address. Admission will only be permitted upon receipt of full payment and a confirmation letter will be issued within three (3) weeks before the Conference.
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Contact Person
Ms Latha / Ms Ally / Ms Nur
Tel : 03-2162 8989 Ext 108/113/106
Fax : 03-2162 8990
E-mail : ntc@ctim.org.my, cpd@ctim.org.my
Website : www.ctim.org.my

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Persiaran Wawasan
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Selangor, MALAYSIA

Contact Person
Mr Hapiz / Mr Saiful
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New Image of the Institute

Change of Institute's name

In 2008, the Council of the Institute deliberated on the change of name for the Institute and had agreed on the new name as "Chartered Tax Institute of Malaysia" ("CTIM").

The change was part of the Institute's rebranding exercise since the change will further enhance the image of the Institute among its members and potential members as the premier tax institute in Malaysia.

The achievements of the Institute has taken many years of hard work through the active involvement of the Institute in various activities in particular, representing members' interests in its meetings / dialogues / liaison with the various bodies to include Ministry of Finance, tax authorities, relevant ministries and organisations as well as in putting forth tax reform measures that are needed to further enhance the efficiency of the tax system.

In this regard, with the term "Chartered" inserted into the new name, members can expect an enhancement of the Institute's stature and a clear reflection of the recognition that the Institute has achieved to-date as well as the technical excellence which it strives for as its core vision.

On 7 March 2009 at an Extraordinary General Meeting, members of the Institute voted in favour of adopting the new name. The new name was officially adopted on 12 March 2009.

New logo

In line with the change in the Institute's name, the Institute under the purview of the Public Relations Committee proceeded to look into the development of a new logo. A logo design competition was subsequently launched in late 2008, which competition was opened to the public at large to include students of Arts and Design schools, advertising agencies, CTIM members and the CTIM secretariat staff.

The new logo, as shown below, was formalised on 1 April 2009, and the rationale was to adopt a contemporary style in two tone colours namely navy blue and red. The alphabet "**t**" and the dot (above the "i") are highlighted in red colour. The red "**t**" symbolises the Institute's core focus on "tax" as its fundamental activity.

The red dot above the "i" represents the globe. The globe symbolises the Institute's global relationship with various like-minded tax and related organisations around the world and is vital in communicating the Institute's relevance to the tax industry both locally, regionally and globally and the Institute's commitment to achieving global excellence.

The clean and simple design of the logo projects the professionalism and authoritative stand of the Institute in all areas relating to the field of taxation. The logo is also contemporary in style making it look current, savvy and therefore relevant to today's industry demands.

ctim

CHARTERED TAX INSTITUTE OF MALAYSIA

Launch of the Chartered Tax Institute of Malaysia's New Name & Logo

The Chartered Tax Institute of Malaysia (CTIM) launched its new name and logo on 13 June 2009 at Hotel Istana, Kuala Lumpur. More than 80 guests attended the launch officiated by the Guest of Honour, Mr Shahmin Ta Bin Abdullah, Deputy Director General, Corporate Affairs, who represented Datuk Hasmah Abdullah, CEO/ Director General, Inland Revenue Board (IRB), Malaysia.















The 17th Annual General Meeting of the Chartered Tax Institute of Malaysia

The Chartered Tax Institute of Malaysia (CTIM) held its 17th Annual General Meeting (AGM) on 13 June 2009 at the Hotel Istana, Kuala Lumpur. Subsequent to the AGM, the council meeting was convened and the following office bearers and Council members were elected for the 2009/2010 term:

President	: Dr Veerinderjeet Singh
Deputy President	: Mr Khoo Chin Guan
Council Member(s)	: Mr Lim Heng How
	Mr Lim Kah Fan
	Mr SM Thanneermalai
	Dr Ahmad Faisal Bin Zakaria
	Mr Aruljothi Kanagaretnam
	Mr Chow Kee Kan
	Assoc Prof Faridah Ahmad
	Mr Harpal Singh Dhillon
	Prof Dr Jeyapalan Kasipillai
	Mr Lew Nee Fook
	Dato' Liew Lee Leong @ Raymond Liew
	Mr Lim Thiam Kee, Peter
	Mr Neoh Chin Wah
	Mr Yeo Eng Hui, Adrian

The Council will continue to enhance the professionalism of tax practitioners as well as contribute towards improving the tax system through various dialogue sessions and submissions to tax agencies and the Ministry of Finance.

With its new name and logo, the Institute will continue to uphold and enhance its image as the premier tax institute in Malaysia. CTIM will develop and promote its professional examinations in line with its commitment towards developing competent tax practitioners. CTIM will also focus on working cohesively with all the relevant professional bodies to ensure effective representation to the tax authorities on all taxation related matters.

Chartered Tax Institute of Malaysia's Graduation and Prize Giving Ceremony










The Chartered Tax Institute of Malaysia (CTIM) held its Prize Giving Ceremony on 13 June 2009 at Hotel Istana, Kuala Lumpur. En Shahmin Ta Abdullah, Deputy Director General (Management) of Inland Revenue Board Malaysia represented Datuk Hasmah Abdullah as the Guest of Honour at the event. Graduates who have successfully completed the CTIM Professional Examinations received certificates and six prize winners obtained medals.

In his address, the Chairman of the Examinations Committee, Prof Dr Jeyapalan Kasipillai, congratulated the new graduates and reminded them that their knowledge, skills, character and integrity would be tested in the competitive and challenging work environment. He added that graduates should strive to contribute to the tax profession upon their graduation.

En Shahmin Ta Abdullah commended the Institute on the regular and well-updated examination syllabus. In developing and conducting professional examinations in the field of taxation, CTIM has played a vital role in producing competent and knowledgeable tax practitioners to meet the current shortage in the country. En Shahmin Ta Abdullah congratulated the graduates on their achievement. He advised them to discharge their duties efficiently to ensure that taxpayers are fully compliant with the law.

Also present at the Prize Giving Ceremony were representatives from various educational institutions, professional bodies, CTIM council members, families and friends of the graduates.

Career Talk conducted at Universiti Putra Malaysia

Assoc. Professor Pn Faridah speaking at UPM career talk

Students listening intently to the career talk

On 27 March 2009, a career talk organised by Universiti Putra Malaysia's Accounting Student Club was held for students at the university. The Chairman of the Education Committee, Associate Professor Faridah Ahmad, spoke on pursuing a career in taxation and encouraged students to take up the CTIM Professional Examinations towards achieving this goal. The talk was attended by approximately 150 students from the Faculty of Economy and Business.

Accounting Recruitment Drive at Multimedia University

Dr Nakha Ratnam, Yuhan Aathi, Dean of Faculty and Dr Veerinderjeet Singh

Dr Veerinderjeet Singh presenting the opening speech

The Cyberjaya Accounting Club of the Multimedia University held an accounting recruitment drive on 24 February 2009, which was officiated by the President of CTIM, Dr Veerinderjeet Singh. After the opening ceremony, Dr Veerinderjeet delivered a talk on a career in taxation to the accounting students present.

Career talk in Politeknik Ungku Omar, Ipoh

On 12 May 2009, Mr Lam Weng Keat, CTIM Perak Branch Chairman, delivered a career talk to 90 students pursuing the Diploma in Accountancy in Politeknik Ungku Omar, Ipoh. During the career talk, students were advised and encouraged to take up the Chartered Tax Institute of Malaysia (CTIM) professional examinations in order to pursue a career in taxation. The Chairman also briefed on the Institute's roles and responsibilities and the benefits of being a member of the Institute.

CPD Event News

Special Ceremony at the IRB in conjunction with the National Tax Conference

Representatives from the Chartered Tax Institute of Malaysia (CTIM) attended a special ceremony at the office of the Chief Executive Officer/Director General of Inland Revenue Board (IRB), Datuk Hasmah Abdullah on 27 April 2009. The event was to present a cheque to the IRB in respect of the joint collaboration between CTIM and the IRB in organising the National Tax Conference in 2008. The representatives also exchanged views on the draft programme for the National Tax Conference 2009 which is scheduled to be held on 4 and 5 August 2009 at the Kuala Lumpur Convention Centre.

Present at the meeting were the following representatives from both CTIM and the IRB:

Representatives from CTIM

Dr Veerinderjeet Singh	– President
Mr Lim Heng How	– Deputy President
Mr Khoo Chin Guan	– Vice President and Former Co-Organising Chairperson, NTC 2008
Mr SM Thanneermalai	– Co-Organising Chairman, NTC 2009
Ms Ann Vong	– Executive Director
Cik Nursalmi Haslina	– CPD Manager

Representatives from the Malaysian Tax Academy, IRB

En Mohd Nizom Sairi	– Director
Pn Siti Rosnah bt Md Hashim	– Director of International Training & Tax Education Centre
Pn Nor Azirah Mohd Said	– Principal Assistant Director
Ms Ranjeet Kaur	– Assistant Director

Visit by UiTM's Kuala Terengganu Students to CTIM

The Chartered Tax Institute of Malaysia (CTIM) hosted the visit from 27 Diploma of Accounting students from UiTM Kuala Terengganu on 14 May 2009. The purpose of the visit was to gather information on the roles and responsibilities of CTIM and on career opportunities in the field of taxation. The CTIM Education Committee member Mr Venkiteswaran was present to welcome the lecturer and students. The session commenced with a briefing on the roles of the Institute followed by a power point slide presentation on a career in taxation. There was also a question and answer session held for the students after the presentation.

REPORT ON CTIM BRANCHES

NORTHERN BRANCH

CTIM Northern Branch visits Bukit Mertajam Branch of the IRB

CTIM Northern Branch Committee Members paid a courtesy visit on 30 March 2009 to the Bukit Mertajam branch of the Inland Revenue Board (IRB). The members met the Director of the branch Tn Syed Hisham Bin Syed Mansor and some of the senior officers. The purpose of the visit was to foster closer relationship between the CTIM and IRB.

Caption: Standing left to right: Mohamad Zin Bin Yaacob, Tan Tcheow Woei (CTIM), Yong Mei Sim, Mazidah Abdul Jalil, Retnasamy A/L Murugiah (CTIM), Khoo Choon Keat (CTIM), Siti Sara Marzuki. Seated left to right: Tn Syed Hisham Bin Syed Mansor, Andrew Ewe (CTIM)

Andrew Ewe, CTIM Branch Chairman (right) presenting a token of appreciation to Tn Syed Hisham, Director of the IRB's Bukit Mertajam Branch.

SABAH BRANCH

CTIM Sabah Branch visits Kota Kinabalu Branch of the IRB

On 15 April 2009, CTIM Sabah Branch Committee members, together with the MIA Sabah Branch Committee members, made a joint courtesy call on the new Director of the Kota Kinabalu Branch, Tn Haji Kamaruzzaman, who is the first Sabahan to be appointed to the post on 1 March 2009.

The visit was followed by a dialogue between Committee members and IRB officials to discuss common tax issues.

Caption: Sabah CTIM Branch Chairman, Michael Tong (4th from right) presenting a souvenir gift to the Director of the IRB's Kota Kinabalu Branch Hj Kamaruzzaman (5th from right). From left, 3rd in the back row is CTIM Sabah Branch member, Goh Chee San and 4th in the front row is MIA Sabah Branch Chairman, Alexandria Thien.

Memorandum of Understanding between the Chartered Tax Institute of Malaysia (CTIM) and ACCA Malaysia

On 1 April 2009, a Memorandum of Understanding was signed between the CTIM and ACCA Malaysia to jointly organise CPD courses on taxation for the mutual benefit of the members of both organisations.

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Tax Audit Issues for Individuals and Partnerships – A Roundtable Discussion

The Chartered Tax Institute of Malaysia (CTIM) organised a roundtable discussion on 16 March 2009 to discuss various tax issues in relation to individuals and partnerships. The discussion was moderated by Mr Lew Nee Fook, CTIM's Council Member and was attended by:

Dr Fam Seng Choy	–	Practitioner, FAM & Associates
Mr Phua Chen Seng	–	Practitioner, present secretary of Malaysian AIA branch
Mr S. Saravana Kumar	–	Advocate & Solicitor, Lee Hishammuddin Allen & Gledhill
Mr Jason Boey	–	Parker Randall
Ms. Low Lay Hiong	–	T.K Lim and Associates
Mr. Goh Wooi Han	–	T.K Lim and Associates

1. Introduction — Malaysia's self assessment regime

Until 2001, Malaysia was under the official assessment system where taxpayers were assessed to income tax by the Inland Revenue Board (IRB) based on the tax returns filed by the taxpayers. This was gradually replaced by the self assessment system from 2001 onwards. Companies were subject to self assessment from the year of assessment (YA) 2001, businesses, partnerships and co-operatives from YA 2004 and individuals from YA 2004.

Under the self assessment system, taxpayers are required to determine their taxable income, compute their tax liability and submit their tax returns based on the prevailing tax legislation, public rulings and guidelines issued by the IRB. The tax returns submitted by the taxpayers are deemed to be a notice of assessment on the date of submission. The self assessment system has effectively shifted the responsibility of determining tax liability to taxpayers, and increased the need for greater transparency, clarity and structure in tax administration process.

Mr Lew commended the IRB under the leadership of Datuk Hasmah Abdullah, Director General of the IRB (DGIR), for promoting greater transparency and the overall efficiency of the self assessment regime. However, Mr Lew noted that there is room for improvement; particularly in relation to the IRB's tax software and computer systems. He compared Malaysia's system to that of Thailand, which he commented as being more advanced. Mr Lew also opined that taxpayers and tax agents are more comfortable with the self assessment system as opposed to the official assessment system.

2. Individuals

2.1 Employment income

Form BE

The Form BE is the tax return form for resident individuals with employment and other income, (which is not business income). The form is to be submitted by taxpayers by 30 April of the following year.

The general consensus of the discussion group was that the Form BE (comprising four pages) was not difficult to comprehend and was fairly straightforward.

According to Mr Goh, however, there were varying opinions on item C5 of the Form BE, namely "Pensions, annuities and other periodical payments" (generally, retirement benefits) with some IRB officers taking the position that these are only exempted from income tax if it is paid out of an approved pension fund. Among others, the explanatory notes to the Form BE states that pensions derived from Malaysia and paid to a person on reaching the age of 55 years/compulsory age of retirement or if the retirement is due to ill-health, are exempt from tax. Where a person is paid more than one pension, only the higher or highest pension is exempt from tax. Other pensions have to be reported.

Gratuity
Gratuities, monetary or otherwise, form part of employment income pursuant to s 13(1)(a) of the Income Tax Act 1967 ("ITA"). These are generally granted an exemption from income

tax under Sch 6 of the ITA. Gratuity derived from Malaysia and paid to a resident government members are exempt under para 30A, Sch 6. Retirement gratuities are exempt under para 25, 25A, 25B of Sch 6 to the ITA. Where the DGIR is satisfied that a gratuity is paid to an individual on account of retirement due to ill health, the gratuity will not attract tax. It is also provided that a gratuity paid to an individual who has had 10 years continuous employment with the same employer, or with companies in the same group, will be exempt if the retirement takes place on or after reaching the age of 55, or on reaching the compulsory age of retirement from employment specified under any written law. Effective from YA 2003, a tax exemption is given on retirement benefits of employees who retire at the compulsory age of 50 to 55; of up to RM6, 000 for each completed year of service. Effective from YA 2007, the retirement benefit for private sector employees who retire at the compulsory retirement age of 50 and above is granted a full tax exemption, subject to the condition that the compulsory retirement age is provided for in the employment contract or collective agreement between the employer and employee.

Mr Goh again raised the concern of whether gratuity payments must originate from approved funds. Mr Saravana addressed this by reiterating the relevant provisions in Sch 6, does not distinguish or discriminate whether the gratuity comes from an approved or non-approved fund — both would equally qualify for the exemption of income tax.

Books

Individual taxpayers are entitled to annual book relief amounting to RM1,000 in respect of the purchase of books, magazines, journals or other similar publications (in the form of hardcopy or electronic, but excluding newspapers and banned reading materials) pursuant to s 46(1)(i) (item D8 of the Form BE).

In addressing Mr Goh's question as to whether the relief applies to only publications in Bahasa Malaysia and English, Mr Saravana clarified that the provision is silent with regard to language, and as such, the purchase of publications in different languages would be allowable. Mr Lew added that

in keeping records of the purchase, taxpayers would need to translate the contents of the receipt into Bahasa Malaysia or English if the receipt is in a different language. Further, it was advisable to maintain photocopies of the receipts as the originals tend to fade with time.

Bonus

Mr Goh questioned as to whether the Bonus for 2008 (column E8, which is on Total Rebates) received in 2009 should form part of the 2009 income. Mr Lew answered that if the bonus is meant for 2008 income, and the declaration is at the bottom of the EA form, then the taxpayers would need to revise their 2008 income tax return. However, the IRB has recently issued guidelines in relation to the bonus that taxpayers will only report the bonus in the year of which it is received.

Travelling allowance

Pursuant to the Income Tax (Exemption) Order 2009 (PU(A) 152/2009), the benefits of travelling allowance, petrol card and petrol allowance received by employees from their employers are exempt from payment of income tax. The exemption is subject to the following limits:

- *travelling allowance, petrol card, petrol allowance or any of its combination, for travel to and from home and the place of work — RM2,400 per year (effective from YA 2008 to YA 2010).*
- *travelling allowance, petrol card, petrol allowance or toll payment or any of its combination, for travelling in the performance of employment at a place other than the employee's place of work — RM6,000 per year (effective from YA 2008 onwards).*

The discussion was centred on the documentation and record-keeping requirements in relation to the allowances.

2.2 Case law (Employment Income)

***Ho Soon Guan v Ketua Pengarah Hasil Dalam Negeri* (2002) MSTC 3,887, High Court**

The taxpayer was employed by a bank. He applied to join a scheme known as the "Separation Scheme", which was offered by the bank. The scheme was open to all resident officers aged 47 or more. The scheme provided for early retirement and contained a formula to calculate the benefits available under the scheme. The scheme was introduced in light of the bank's business strategy, which required a new organisational structure. The scheme targeted officers who were not suitable in the new organisational structure, those who were not performing well and those suffering from illness. At the time the taxpayer applied to join the scheme, he suffered from polymyositis, which necessitated him having to wear a neck collar. The bank accepted the taxpayer's participation in the scheme, and the taxpayer left the service of the bank under the scheme, which was about one year before his actual age of retirement.

Under the scheme, he was paid RM390, 437 as **compensation for loss of employment**. The IRB calculated a tax of RM113, 021.60 based on the compensation received. The taxpayer made numerous appeals for total exemption from tax on the grounds that the **compensation was made on account of his ill-health** and that he is entitled to such exemption under s 15(1)(a) of Sch 6 of the ITA. However, the IRB rejected his appeals and instead, awarded a reduction of RM4,000 per annum on the number of years the taxpayer served the bank, pursuant to s 15(1)(b) of Sch 6, ITA. The taxpayer's appeal to the Special Commissioners was dismissed and he appealed to the High Court.

The taxpayer argued that the main conclusion of the Special Commissioners of Income Tax ("SCIT") that the taxpayer lost his employment under the separation scheme and not on account of ill-health "does not warrant the conclusion that the loss of employment was made because of his participation in the scheme." The taxpayer submitted that there was a difference in participating in the scheme and stating that the loss of employment was due to the

separation by and of itself. It was argued that the SCIT had not considered the real issue of whether there was sufficient evidence for the conclusion that compensation was made on account of loss of employment due to ill-health, and that the SCIT was wrong in the determination of the facts and the inferences therefrom.
The taxpayer took the position that there was sufficient evidence that he was ill before the scheme was brought up, that the medical reports showed that he was suffering from polymyositis, a muscular disorder, and that he would need "long periods of rest" and that "he would be unlikely to be gainfully engaged in any work unless his condition improves significantly."

The High Court observed that the bank requires a report from a medical board in order to terminate a person on medical grounds. In the taxpayer's case, a medical board was not constituted. With his leaving the service of the bank under the scheme, the compensation that the taxpayer received was calculated on a different basis from what he would have received had he retired outside the separation scheme.

The High Court had to decide whether the compensation received by the taxpayer fell within the exemption under s 15(1)(a) or s 15(1)(b).The High Court upheld the SCIT's ruling that the taxpayer had participated in the **separation scheme voluntarily and had opted to retire early** and indeed had applied under the scheme to retire early and that he had not retired because of ill-health. The High Court and SCIT noted that although the taxpayer had had the medical problem since 1995, he had not applied for retirement on the grounds of ill-health at all nor was the approval to retire based on ill-health. It was observed that the taxpayer had decided to apply for retirement when the bank introduced the scheme and even then no mention was made as regard to his illness in the application or in the approval thereto.

***Frank Edward Noah v Ketua Pengarah Hasil Dalam Negeri* (1999) MSTC 3739, High Court**

The taxpayer, a British national, was employed as a chief executive officer of three local companies on 29 August 1989. His employment ended on 15 October 1989 after he had been employed for only 44 days, for which period he was not paid any salary. In three similar letters all dated 13 October 1989, the three local companies referred to the taxpayer's desire to resign from their employment; and they confirmed to compensate him with a "mutually-agreed termination settlement" of RM700,000 (the **compensation payment**).

The taxpayer left Malaysia on 16 October 1989. As such, he was in Malaysia for a total period of less than 60 days in the basis year 1989. It is an agreed fact that he was not a resident for Malaysia tax purposes for the basis year 1989. The taxpayer was assessed to tax on the compensation payment for the YA 1990. He appealed against the assessment. The SCIT confirmed the assessment after holding that the compensation payment **did not qualify for tax exemption** under para 21 of Sch 6 of the ITA.

The taxpayer appealed to the High Court, contending that the compensation payment was income from an employment by virtue of s 13(1)(e) of the ITA. Since employment was exercised in Malaysia for 44 days (i.e. less than 60 days) and the taxpayer was at all material times a non-resident, the income from that employment must necessarily be for the same period, namely 44 days, and accordingly, the appellant is therefore qualified for tax exemption under para 21, Sch 6.

The High Court upheld the Special Commissioners' decision that the compensation payment was not income from the **employment exercised by the taxpayer in Malaysia**. The High Court held that in order to qualify for tax exemption under para 21, the compensation payment had to satisfy two conditions: (1) it must be income from an employment exercised by the taxpayer while in Malaysia; and (2) it must also be income for a period or periods which together did not exceed 60 days in the basis year 1989. The expression "for a period or periods which together do not exceed 60 days" appearing in para 21 relates not only to the taxpayer's period of employment, but also to the income. Thus, the important question to ask was whether the compensation payment itself was income "for a period or periods which together does not exceed 60 days" in that basis year. While it was true that the compensation payment of RM700, 000 was income from an employment made under s 13(1)(e), ITA, the payment could not be construed as income from employment for 44 days in 1989 because the taxpayer was actually exercising employment on an agreed salary of RM72,500 per month. The compensation payment, representing the equivalent of nearly 10 month's salary, was paid to the taxpayer as compensation for the premature termination of his employment on 15 October 1989 which would otherwise have carried on for (at least) the next 22 1/2 months since he had a real prospect of continued employment. The compensation payment, being compensation for loss of employment, cannot be made in respect of employment or in respect of having or exercising the employment — the High Court ruled that the two are mutually exclusive.

2.3 Business Income

Record-keeping
The Form B is the tax return form for resident individuals deriving income from a business source and other income, including sole proprietors. Form B is to be filed by the taxpayer by 30 June of the following year.

The concern raised by Dr Fam was in relation to the extent of proper record-keeping by small businesses, e.g. those who run stalls, where the bulk of the transactions were unrecorded cash transactions. Mr Lew suggested that more practical information could be gleaned from members who acted on behalf of these small traders. It was suggested by Ms Lau that this category of taxpayers be educated on the need to maintain proper records (e.g. daily records of purchases and sales), and be informed of their responsibilities under the self-assessment system. The education of taxpayers in this regard was mooted as a matter to be examined by the CTIM. Further discussion ensued about the different arrangements and transactions carried out by small business that would raise flags with the IRB, for example, issuing cheques to an individual in his/her personal capacity instead of to the relevant company/business in an effort to "help a friend out". Mr Saravana added that the tax return and details declared must reflect the realities of the business and the lifestyle of the taxpayer. For example, if profits were declared at, say, RM2, 000 a month, there is a certain expectation of the taxpayer's lifestyle, such as the car that he/she drives, that corresponds with the declared business results. Otherwise, it would raise flags with IRB officers. He further cautioned tax agents not to expose themselves to litigation by acting upon unqualified information provided by taxpayers which may not be the whole truth of the matter. The careful and proper drafting of contracts and putting in place exclusion clauses would go a long way in protecting tax agents from litigation brought on by improper conduct of their clients.

2.4 Case law (Business expenditure)

Director General of Inland Revenue v Dr GGSW (1988) 1 MSTC 2,117 (Special Commissioners of Income Tax)

The taxpayer was a qualified medical practitioner practising as a private consultant plastic surgeon. He had several sources of income but the main source was by way of salary received from M Sdn Bhd. The taxpayer **attended conferences** held in Singapore in relation to plastic surgery. At the conferences, new techniques were introduced to the participants. The taxpayer attended the conferences for the purpose of **improving his professional knowledge** and professional techniques in plastic surgery. He sought to deduct the expenses incurred in relation to attending the conferences under s 33(1) of the ITA. The IRB disallowed the expenditure on the basis that the taxpayer did not attend the conferences in his official capacity and not in performance of his duties. The IRB further contended that the taxpayer attended the conferences to self-educate and enhance his knowledge and, as such, the expenditure was divorced from the production of income. The SCIT ruled in favour of the taxpayer and held that the **expenses were deductible** under s 33(1). The SCIT held that the taxpayer's participation at the conferences increased his knowledge of modern development in relation to his work as a professional.

3. Partnership

The tax return form for partnerships, the Form P, is to be submitted by 30 June of the following year. It was commented that the Form P was fairly clear on the distribution of profits. Some of the common problems faced by practitioners were discussed.

3.1 Disclosure by clients
A common observation was that clients occasionally failed to provide full disclosure to tax agents, especially in regard to the number of businesses participated by the partnership. It was agreed that tax agents should be advised to perform a search at the Registrar of Businesses when accepting a partnership tax assignment. In many cases, it was apparent that clients were unaware of the specific processes and procedures that needed to be adhered to in terminating a business properly.

3.2 Records for old partnership businesses
A problem that was discussed was the carry-over of partnership records, which is normally entrusted to one partner. When a partnership is dissolved, this poses a problem as the records may have been destroyed. Hence, it was proposed that tax agents servicing a partnership provide each partner with a copy of the accounts and computation, together with the Form P, such that they would be able to keep track of their distributions for the purposes of filing their individual tax return forms.

3.3 Case law

Ketua Pengarah Hasil Dalam Negeri v Dato' Hanifah Noordin (2003) MSTC 4,007 (High Court)
(Note: The facts and decision in this case are similar to Ketua Pengarah Hasil Dalam Negeri v Mr B (2001) MSTC 3,840 (High Court))

The taxpayer was a partner in an accounting firm. Pursuant to a merger with another firm, the taxpayer **retired from the partnership**. He received **compensation** amounting to RM1,199,651. The compensation was paid in 23 equal instalments. The IRB sought to tax the compensation on the basis that the payments were consultancy payments and were calculated by reference to work in progress. The High Court dismissed the IRB's appeal and held that the **payments were capital receipts**. The fact that the payments were entered as consultant payments in the partnership's book did not change the nature of the payment. The High Court added that it was settled law in that how the accounts were kept was not conclusive in relation to the nature of payment. The compensation was paid to the taxpayer as he had agreed to:

- cease being a partner of the firm
- lose all his rights in the partnership
- waive all rights to challenge the merger, and
- refrain from taking any legal action in respect of the merger.

4. Practical issues

4.1 Tax audit

With the implementation of the self assessment system, tax audits have inevitably become an integral part of the Malaysian taxation system. The IRB introduced its "Tax Audit Framework", effective from 1 January 2007. A tax audit is an examination of a taxpayer's business records and financial affairs to ascertain that the tax reported and paid is in compliance with tax laws and regulations. Generally, these audits cover a period of one to three years of assessment. These may take the form of a desk audit or a field audit. In a field audit, stocks and equipment may be physically sighted to verify the claims made. An on-site examination of records may take two to three days or more, *depending on the complexity of the business transactions and the extent of cooperation given by the taxpayer.*

There was a discussion of the rights and obligations of the taxpayers and tax agents during tax audits; including the IRB's power to have access to business documents, the facilities to be provided to the IRB officers who are on the taxpayer's premises during the audit, and the tax agent's role in facilitating this process.

Questions were raised as to documents that the officers had the power to take away from the taxpayer's office, e.g. could the officer remove entire records of payment vouchers? Mr Lew addressed this issue, explaining that it was within the IRB's power to do so, and the officers were required to sign a document listing each item/record removed, and leave the taxpayer with a copy thereof. He reiterated that it was important for taxpayers and their agents to provide full cooperation and reasonable facilities during tax audits, as was the requirement of the law, cautioning there would be consequences otherwise.

4.2 Tax investigation

The IRB has issued a "Tax Investigation Framework", effective from 1 January 2007. Tax investigation is an examination of a taxpayer's business and/or individual books, records and documents to ensure that the amount of income reported and tax paid is correct. It enhances voluntary compliance with tax laws and regulations. Where there is fraud, wilful default and negligence, there is no statutory limitation on the number of years of assessment involved. The two areas of investigation are civil tax investigation (involving detection of tax evasion and leading to the recovery of tax loss and imposition of heavy penalties); and criminal tax investigation (involving the gathering of admissible evidence with a view towards the prosecution and conviction of the tax evader for commission of offences).

Mr Phua shed some light on the processes and procedures involved in a tax investigation. He explained that there was an element of surprise, with no advance notice given to the taxpayer, and the officers usually presented themselves in groups of three or four, simultaneously, at the taxpayer's business premise and residence. The discussion also turned to the association between companies intending to be listed on the stock exchange, and tax investigations being launched into their businesses. It had been observed that going about an exercise to list one's business drew the attention of the IRB's investigation unit.

4.3 E-filing

Following the official launch of the e-filing program on 17 May 2004, taxpayers may now submit their tax returns electronically.

Overall, it was felt that the electronic filing system implemented by the IRB was a positive move. There were reminders that the proof of submission when using e-filing was to be printed and maintained on record. Mr Lew also stated that taxpayers and tax agents should be advised to complete the checklist to ensure that no details had been missed out.

Problems faced with the e-filing system were raised. One issue was the inconvenience involved in correcting information that has been entered onto the system. The taxpayer would have to visit the relevant IRB branch office, and submit supporting documents to have the error rectified. Further, the general consensus was that the e-filing system had not sufficiently evolved and had limitations that needed to be worked around, e.g. the system did not enable last minute submissions, and was very slow in operating. It was also felt that there was a lack of training and education by the authorities to enable the public to use the system efficiently. There was a suggestion by Mr Phua that the system could be improved by automatically updating details of the monthly tax instalments made onto the tax return form, such that the taxpayer would immediately know their tax status (and if there is an overpayment of tax).

4.4 Engagement letter

An interesting discussion took place regarding letters of engagement. Such letters, besides defining the scope of the engagement and the responsibilities of each party, serves to protect tax agents from liability and also promotes good governance.

An interesting question was raised by Dr Fam," If, in addition to an engagement letter to their clients, tax agents obtained a letter of indemnity from their clients, what was the legal standing of such a document?" Mr Saravana explained that the intention of the taxpayer plays a very important role, in particular, the way information is recorded and documents are drafted. If a tax agent is negligent, he/she will bear the consequences related to that negligence, despite having the taxpayer's indemnity. He added that the courts generally held professionals to a higher standard of care.

5. Conclusion

The landscape of taxation in Malaysia has changed considerably since the implementation of the self assessment system. With the shift in onus and responsibility for ensuring a correct return onto the taxpayer, there is an urgent need for clarity, transparency and the education of all involved. Taxpayers need to be informed of their rights and responsibilities, and tax practitioners need to be kept current in their knowledge of the tax laws and all aspects of the taxation regime.

The CTIM has proved itself to be relevant, current and an important source of information and support to the tax community. Going forward, the CTIM will continue to educate and conduct various seminars, training and discussion sessions in an effort to enhance understanding, disseminate knowledge, and arm practitioners with the tools they need; while at the same time, fostering open communication with the tax authorities in conveying the issues faced by taxpayers and practitioners and proposing important steps in taking Malaysia's tax system in the right direction. TG

Managing Income Taxes during an Economic Downturn

By Steve Chia

This timely and insightful article discusses how companies can effectively manage income taxes in such a manner as to support them through the current global financial crisis.

Former US Federal Reserve Chairman, Alan Greenspan was recently quoted as saying that the current global recession will "surely be the longest and deepest"[1] since the 1930s. In Malaysia, local market observers and economists today have mixed views on the real health of the current economy. While some are fairly optimistic that the economy may have hit rock bottom and is now moving towards recovery, others remain sceptical and prefer to reserve their judgment before assessing whether the recent recovery is sustainable. Whether or not the recession is here to stay, what is certain is that businesses have been hit hard by the financial tsunami with a common trend of sluggish demands amid rising operating costs.

When times are bad, traditional thinking dictates that businesses react by taking tough measures such as cutting back on business spending and investments to generate cash. Management of taxes is generally not accorded the importance it deserves in helping businesses sail through this challenging phase. This article endeavours to identify the common tax issues prevalent in companies during an economic downturn and provide insights as to how these can be effectively managed. In going through these issues, the writer has categorised them based on the key challenges generally faced by companies during an economic downturn.

Diagram 1: Effective tax management: Key challenges faced by companies during an economic downturn

Falling assets value

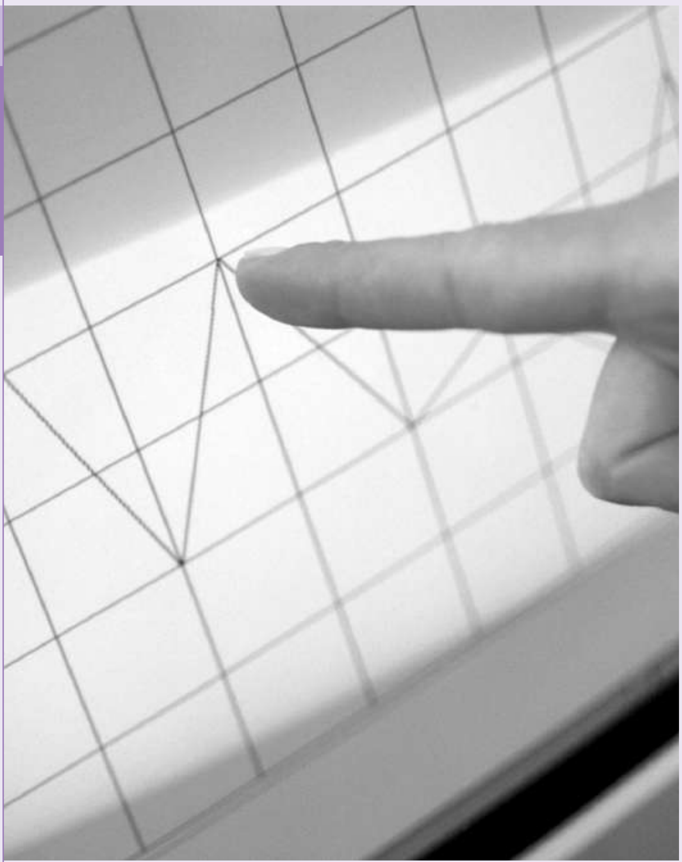
It is not surprising that in an economic downturn, values for assets such as fixed assets, stocks and debtors may have to be written down to reflect the lower values in the market.

Companies would have to account for impairment of fixed assets when the net recoverable amount of the asset falls below the carrying value thereby creating an impairment loss (because the assets are not in use or the utilisation of assets is not maximised due to lower demand). For tax purposes, impairment losses are not deductible as they would not satisfy the "incurred" test of the general deduction rule set out under s 33(1) of the *Income Tax Act 1967* ("the Act"). Notwithstanding the impairment, the taxpayer can continue to claim capital allowances ("CA") at the prescribed rates based on the qualifying expenditure incurred, provided that the assets are still in use.

Where the assets are not in use at the end of the relevant basis period, strictly, the business would not be eligible to claim CAs unless it meets the "temporary disuse" test. An asset is regarded as being in a state of temporary disuse if the asset is maintained in readiness to be brought back to use, and was in use prior to becoming idle. Proper supporting evidence should be available to demonstrate the temporary disuse e.g. reports of regular, scheduled maintenance of the machine, evidence that the machine is not dismantled, etc.

Where assets are in a state of permanent disuse or written off, this would be deemed as a disposal for CA purposes and balancing adjustments would need to be computed. In practice, where balancing allowance arises, the Inland Revenue Board ("IRB") would likely disregard the balancing

1 Financial Times, 2 March 2009



allowance unless it can be demonstrated that the market value of the assets has in fact fallen below its tax written down value. Where the balancing allowance involved is substantial, the taxpayer may wish to consider obtaining a market valuation to support the balancing allowance claim.

Where businesses are looking at disposing assets, the timing of disposal should be carefully considered. A disposal which would be likely to generate a balancing charge should be deferred while disposals resulting in a balancing allowance should be accelerated. In addition, where tax incentives have been claimed on such assets, say reinvestment allowance, the company must consider the potential clawback of reinvestment allowance if the minimum five-year ownership period is not met (prior to YA 2009, the minimum holding period was two years).

Then, there are the stocks-in-trade of a business to be considered. In an economic downturn, it is not uncommon that stocks have to be written down to their net realisable value (i.e. market value) in compliance with the relevant accounting standards. For tax purposes, an allowance for stock obsolescence would generally not be granted a tax deduction if it is a mere provision, as it does not meet the test of being "incurred" to qualify for a deduction. On the other hand, actual write-down of stocks can be allowable on the basis that it is realised.

In order to support the tax deductibility of the stock write-down, based on Public Ruling 4/2006 — *Valuation of Stock In Trade and Work In Progress* Part 1, the IRB would generally require that the valuation be determined item by item unless such an exercise is not appropriate or impractical. In such cases, the stocks can be grouped by type or nature for stock valuation purposes. The value of the stock-in-trade should then be determined according to clearly identifiable groups or batches of homogenous or related items. In the case of stock written off, in practice, some IRB officers have insisted that the stocks must be removed from the business premises before a tax deduction can be accorded. Therefore, businesses which are faced with substantial stock write–down or write–offs should ensure that they meet the IRB requirements to ensure its tax deductibility.

With the current credit crunch, it is also likely that businesses will face a surge in defaults on trade receivables. Under Public Ruling 1/2002 — *Deduction for Bad and Doubtful Debts and Treatment of Recoveries*, allowances for doubtful trade debts are generally not deductible unless the allowance is a specific provision. The taxpayer must be able to prove that the debts are trade in nature, have been evaluated separately and all reasonable steps (such as issuing reminder letters or initiating legal actions based on sound commercial considerations) have been taken to recover the debt. It is important that the credit department is aware of these requirements and ensure that specific steps taken to recover the debts are properly documented to support the tax deduction.

Reduced profits/losses

Given the current economic scenario, businesses may be experiencing reduced profits or even suffering losses. If the taxpayer is expecting a reduction in profits or losses, consideration should be given to appeal to the IRB for a tax estimate lower than the prescribed threshold of 85% percent to avoid a situation of expending too much cash in taxes at the onset. Once the initial estimate has been submitted, the company should continue undertaking a periodical review of the estimated tax and determine if the submitted estimate is still reasonable and whether a revision of estimate is required in the sixth and/or ninth month of the basis period. In practice, we have seen the IRB allowing revisions of tax estimates outside the permitted schedule; say in the 12 month, provided that there are strong justifications given. Simply put, businesses should carefully and realistically monitor its tax position in this uncertain economic climate so as to avoid expending unnecessary cash outlays but at the same time, ensuring sufficient taxes are paid to avoid potential tax underestimation penalty.

Where companies are expecting to be in a tax overpayment situation due to lower tax payable, the taxpayer should attempt to expedite filing the tax returns to the IRB to crystallize the overpayment earliest possible. Once the tax return has been filed, the taxpayer should diligently follow up with the IRB to expedite the processing of the refund. If the amount of refund is not substantial, the taxpayer should perhaps consider applying for set–off against future tax instalments instead of requesting for refund.

In a group scenario, where some group companies are expected to have losses, consideration should be given to surrender the losses to profitable group companies. Under the group relief provision, a company may surrender up to 70% of its current year adjusted loss to one or more related companies subject to certain conditions being met.

The consideration for group relief opportunities should be done as early as the determination of the initial tax estimates i.e. prior to the commencement of the basis period. With early identification of potential loss surrendering companies, actions can be taken to ensure that the companies will be able to fulfil the conditions to access the group relief provision, for example, by meeting the minimum paid up ordinary share capital of above RM2.5 million at the beginning of the basis period.

The choice of the claimant company would need to be carefully considered to maximise tax efficiency. Losses should be given to claimant companies which may potentially have an underestimation penalty so that the penalty exposure can be mitigated. Between a claimant with a balance of tax payable and a claimant with an overpayment of tax, the priority should be given to the company with a balance of tax payable so that the company can reduce its cash outflow to the IRB.

In addition to group relief, companies with tax losses can also now consider carrying back the losses for YA 2009 or 2010 up to RM100,000 to the immediately preceding YA.

Cost control and management

Tight cost control and management is important to ensure that businesses survive through this economic crisis. The choice of expenditure would have its associated tax consequences. Where possible, non-deductible expenses should be mitigated and opportunities for double deduction be considered. Strategising on the type and timing of the expense can provide valuable tax savings.

A classic example would be travelling expenses. Generally, business travelling expenses are deductible, while leave passages provided by employers are not deductible (with the exception of leave passages that are to facilitate a yearly event within Malaysia which involves the employer, employee and immediate family members of that employee). In this regard, employers that are currently providing leave passages to their employees should consider reviewing the employment benefit to determine if the benefit can be substituted with other types of employment benefit that are deductible for tax purposes — for example, a travelling allowance. Of course, the tax implications of the employees would also need to be considered.

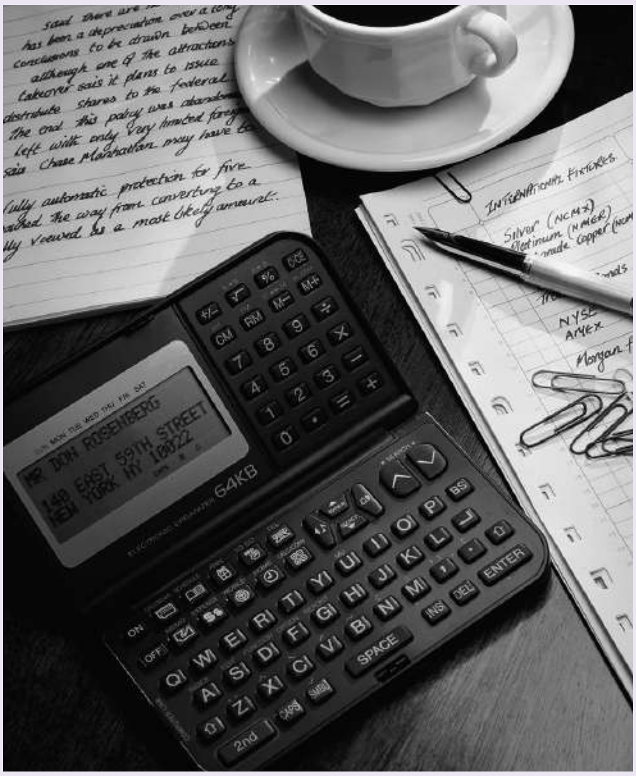
Additionally, if a company incurs certain overseas travelling expenses such as travelling expenses for participation in approved trade fairs overseas for promotion of exports, the company could avail itself for double deduction for promotion of exports outside Malaysia. Note however, only return air fares on economy class would be eligible for the double deduction incentive. Therefore, to maximise the incentive claim, a company should ensure that only economy class travel is used for promotion overseas. Other common expenses incurred by businesses are entertainment expenses or advertising and promotional expenses. It is important that taxpayers have a sufficient level of awareness on the type of deductible and non-deductible expenses under Public Ruling 3/2004 — *Entertainment Expenses* (and Addendum) to ensure maximization of expenses which are eligible for 100% or at least 50% deduction.

Where businesses are still investing, the timing of investment should also be considered. Under the Mini Budget, acquisition of fixed assets from 10 March 2009 to 31 December 2010 would be given an accelerated CA over two years. Therefore, companies should review their investment plan to avail for the accelerated CA claim. Additionally, renovation expenses incurred between 10 March 2009 and 31 December 2010, up to RM100, 000, would be eligible for CA over a period of two years.

The mode of financing can also influence the tax efficiency of the fixed assets acquisition. Consideration should be given by businesses to lease the asset. In addition, to provide flexibility on the use of asset, a lease arrangement could be tax beneficial as the amount payable under a lease should qualify for outright deduction in the year when the lease rentals are incurred. As compared to an acquisition, say through a hire purchase arrangement, the taxpayer can only claim CA as and when the capital instalments are paid. Of course, it should be noted that a leased asset would not be eligible for reinvestment allowance.

Review of business contracts

During an economic downturn, it is inevitable that there will be an increase in likelihood for termination of contracts or breach of contractual terms that could give rise to compensation payments e.g. cancellation of agency



contracts, cancellation of orders by customers, etc. From a tax perspective, it will be essential for both the payer and recipient to determine the appropriate tax treatment of the compensation payment i.e. whether it will be taxable (to the recipient) and deductible (to the payer).

From the recipient's standpoint, generally, compensations for cancellation of trading contract which result in a loss of future profits, temporary interference of business or disablement of the company's revenue–producing assets would be seen to be revenue receipts and hence, taxable. The exception would be for a contract which forms the only contract of the business or the compensation is seen to be a compensation for loss of a profit–making structure or for a permanent sterilisation of fixed asset of a business — these would be normally regarded as capital receipts.

Where it is determined that the compensation is revenue in nature to the payer, it does not necessarily follow that the compensation would be revenue to the recipient. For example, Manufacturer A terminates its supply contract with one of its suppliers, Supplier X, resulting in a compensation payment by Manufacturer A. To Manufacturer A, the compensation can be regarded as revenue payment if the supplier in question is one of the many suppliers it has and such termination is in the normal ordinary course of its business. However, to Supplier X, the contract may be its sole contract i.e. supplying all its products to Manufacturer A. In this instance, as the termination of the contract would result in Supplier X having to cease its business; the compensation received could be viewed as capital.

Refinancing and restructuring of loans

In an economic downturn, businesses would generally be faced with liquidity issues and have difficulty servicing their liabilities. In order to address this, businesses would generally negotiate with their lenders to restructure or refinance their borrowings.

Taxpayers who embark on such an exercise should be aware of its tax implications so that they would not have to incur additional tax costs arising from the debt restructuring exercise. As each scheme is unique, it would be difficult to address the general tax implications arising from such an exercise. However, the key tax issues (not exhaustive, though) which should be considered include:

- tax efficiency arising from the choice of refinancing e.g. Islamic financing, sale and leaseback arrangement
- taxability of debt forgiveness, if applicable
- tax deductibility of refinancing/restructuring costs
- tax deductibility of refinanced interest cost e.g. consider opportunity for debt pushdown
- withholding tax implications if it involves non–resident lender
- tax impact on the company's interest restriction calculation, transfer pricing, thin capitalisation, etc.

Rightsizing, cessation and divestment

Rightsizing, cessation and divestment of business are part and parcel of an economic recession. As undesirable as they may be, such tough measures are the necessary evils in a difficult economic time. Subject to commercial consideration, a rightsizing would be the favoured option in tax terms as compared to an immediate cessation of business as costs associated with the former are viewed to be costs required for increasing or retaining the source of income. Hence, rightsizing costs are generally tax deductible. Costs of cessation of business on the other hand, are often regarded to be payments or compensations for termination of a business i.e. permanent closure of business and therefore, not deductible.

As companies are reviewing their business strategy moving forward, it is important that they also take into account the conditions imposed on the business in respect of certain tax incentives, indirect tax facilities, etc. These conditions may include minimum fixed assets investment, export requirements, minimum R&D expenditure, etc. Where it is anticipated that these conditions cannot be met due the change in business circumstances, the management should immediately engage with the authorities (e.g. Malaysian Industrial Development Authority ("MIDA"), Customs, etc.) to negotiate for a waiver or relaxation of the conditions so that it can continue to avail itself of the tax incentive or facilities granted.

For companies that plan to divest their businesses in order to focus on their core competencies in this challenging time, the mode of divestment should take into account the relevant tax implications. Say a local conglomerate with multiple businesses intends to divest its non–core property development business. If the divestment involves selling the property development land and stocks, such sale would likely be taxable as the company would be disposing its stocks–in–trade. However, if the shares of the property development company are disposed, it can be argued that such shares are held as long term investment and therefore, the disposal be regarded as capital transaction. Of course, other tax implications (e.g. stamp duty) and factors would need to be considered, in particular the willingness of the acquirer to buy the company.

Conclusion

While in this troubling time, businesses may not put tax at the top of their agenda, it is imperative that they realise that almost every business transaction or decision has a corresponding tax implication. With proper tax compliance procedures in place and an effective management of tax risks, the tax function can play a key role in helping businesses through this difficult economic time; not just by helping to manage businesses' cash flows, but also to provide an opportunity to efficiently manage its tax costs. TG

***Steve Chia** is an Executive Director at PricewaterhouseCoopers Taxation Services Sdn Bhd. The content of this article represents his personal views and not that of PricewaterhouseCoopers. He can be contacted at steve.chia.siang.hai@my.pwc.com.*

The 2009 Economic Stimulus Package / The Mini Budget

By Renuka Bhupalan

A summary of the measures introduced in the 2009 Second Stimulus Package and the enactment thereof via the Income Tax (Amendment) Act 2009 and recent gazette orders.

The global financial crisis which started last year has snowballed significantly and its knock-on effect has clearly affected Malaysia. Amidst the deepening global and domestic economic crisis, the Malaysian Government announced a "Mini Budget" comprising a RM60 billion economic stimulus package on 10 March 2009. The size of the stimulus package is bold and shows recognition of the gravity of the domestic economic situation. Some of the key economic indicators for the country against which the stimulus package was proposed include the following:

- The GDP growth rate shrank to 0.1% in the last quarter of 2008 as compared with an average rate of 6.3% for the first three quarters of 2008.
- For 2009, it is expected that the GDP growth rate will only be between -1% to +1%.
- Exports in January 2009 declined by 27.8% and are expected to shrink further.
- Foreign Direct Investment (FDI) in 2009 is expected to be RM26 billion which is half of what was achieved in 2008.
- The unemployment rate is expected to rise from 3.7% in 2008 to 4.5% in 2009.

As a result of the proposed RM60 billion stimulus package, the Federal Government's budget deficit of 4.8% is expected to increase to 7.6%. Nonetheless, the Government is confident that the stimulus package will prevent the economy from further deterioration and will meet the following objectives:

- reduce unemployment and increase employment opportunities
- ease the burden of the people
- assist the private sector
- build capacity for the future

The package includes significant allocations to and initiatives for both the public and private sectors.

This article highlights the Mini Budget tax proposals and summarises the relevant gazette orders and changes introduced in the *Income Tax (Amendment) Act 2009*. It is noteworthy that the relevant legislative changes proposed in the Mini Budget were gazetted very promptly; far more promptly than has been the case for previous Budget proposals. Additionally, comprehensive guidelines relating to the implementation of several proposals were also promptly released by the tax authorities. The efficiency with which this was done is welcomed and this sets a good precedent for the authorities to follow with respect to future Budget proposals and changes in the tax laws.

Tax proposals

Changes enacted by Gazette Orders

- *Income Tax (Accelerated Capital Allowance) (Plant and Machinery) Rules 2009*

Qualifying expenditure incurred on plant and machinery between 10 March 2009 and 31 December 2010 will be eligible for accelerated capital allowances (ACAs). The ACAs will result in the assets being written down for tax purposes over two years. The initial allowance remains at 20% and the annual allowance will be 40%. The ACAs will also apply in respect of the capital portion in respect of payments for plant and machinery acquired under hire purchase arrangements. It should be noted that the ACAs will not be available to the following persons:

– companies which have been granted any incentives under the *Promotion of Investments Act 1986* (PIA)
– companies which have claimed reinvestment allowance under Sch 7A, *Income Tax Act 1967* (ITA)
– a person who has been granted an exemption under s 127(3)(b) or 127A, ITA
– a person who qualifies for a higher allowance under the ITA or any rules made pursuant to s 154, ITA.

The above is effective from the year of assessment 2009, but as highlighted above, this will only be in respect of assets acquired between 10 March 2009 and 31 December 2010.

- *Income Tax (Special Treatment on Interest on Housing Loan) Regulations 2009*

In a welcome move, financial institutions have agreed to allow retrenched workers a moratorium on the repayment of their housing loans for one year. To support such licensed financial institutions in this regard, the interest income in relation to the deferment of housing loan repayments will be taxed only when such interest is received (as opposed to the accruals basis). The interest in this instance is related to that which is payable for a 12-month period from the date of approval of the moratorium.

From the individual's perspective, the housing loan must have been granted prior to the individual's loss of employment. Individuals are required to apply (between 10 March 2009 to 9 March 2010) to the relevant financial institution for the moratorium. It should also be noted that the individuals must be Malaysian citizens who have been retrenched on or after 1 July 2008.

- *Income Tax (Deduction for Expenses Relating to Remuneration of Employee) Rules 2009*

Employers who employ personnel who have been retrenched on or after 1 July 2008 will be given a double deduction for tax purposes on the amount of remuneration paid to such employees up to a maximum of RM10, 000 per month per employee, subject to a limit of 12 months of the employee's remuneration. This incentive is applicable in respect of Malaysian resident citizens employed from 10 March 2009 to 31 December 2010. It should be noted that the employee's termination of employment must be registered with the Ministry of Human Resources. Additionally, there are certain restrictions to the eligibility for the double deduction claim, including situations where the former employer and new employer are associated. This incentive takes effect from the YA 2009.

It is hoped that registration with the Ministry of Human Resources will involve a relatively simple process to enable retrenched employees and employers to benefit from this scheme.

- *The Windfall Profit Levy (Oil Palm Fruit) (Amendment) Order 2009*

At present, a windfall profit levy on oil palm is imposed when the price of crude palm oil exceeds RM2, 000 per tonne. The RM2, 000 threshold has been increased to RM2, 500 per tonne for Peninsular Malaysia and to RM3, 000 per tonne for Sabah and Sarawak. The new threshold levels came into operation on 10 March 2009.

Changes via the Income Tax (Amendment) Act 2009

- *Carry back of business losses*

Based on the Income Tax (Amendment) Act 2009, a new s 44B has been introduced into ITA to allow current year losses of up to RM100, 000 per year to be carried back to the immediately preceding year. This tax treatment will be available for the years of assessment 2009 and 2010 to all businesses, including partnerships and sole proprietors.

It should be noted that the election to carry back losses will be an **irrevocable election**. A loss-making company can still surrender up to 70% of its adjusted losses to a related company (in terms in group relief) and, in addition, it can elect to carry back the balance of the current year losses of up to RM100, 000 to the immediately preceding year of assessment. Therefore, losses arising in the YA 2009 can be carried back to the YA 2008, and losses arising in the YA 2010 can be carried back to the YA 2009.

While this change is welcomed, in the current economic climate, the ceiling of RM100, 000 in respect of the loss carry-back facility may not have a significant impact on many businesses. Effectively, for the year of assessment 2008, this would mean a tax reduction for the said year of RM26, 000 for a company. For small businesses, this would be a useful tax saving, but for large companies, this is arguably insignificant. The other area of concern is the timeframe that will be taken to process refunds arising out of the loss carry-back facility. It is hoped that the tax authorities will commit to refunding the tax overpaid as a result of the loss carry back on a timely basis. The concern some may have would be whether there would be a tax audit initiated before a refund is made for such cases.

It is also pleasing to note that the company's s 108 balance in respect of the years in which the losses carried back are utilised will not be affected. Thus, the credit attached to franked dividends based on the s 108 balance prior to the loss carry back utilisation will not be withdrawn and will continue to be available to the shareholder(s) who received such dividend income. This is a practical decision on the part of the tax authorities.

It should be noted that the loss carry-back facility will be denied to the following taxpayers:

– a pioneer company or a company which has been granted investment tax allowance under the PIA
– a company whose income is exempt under s 54A, 127(3)(b) or 127(3A) of the ITA, or where tax paid or payable by that person has been remitted under s 129 of the ITA
– a company which has claimed reinvestment allowance under Sch 7A, ITA
– a company which has claimed a deduction under the Income Tax (Deduction for Investment in an Approved Food Production Project) Rules 2006, the Income Tax (Deduction for Cost of Acquisition of Proprietary Rights) Rules 2002, and the Income Tax (Deduction for Cost of Acquisition of a Foreign Owned Company) Rules 2003
– company which has made a deduction under any rules made under s 154, ITA
– a listed investment holding company under s 60FA, ITA
– a company that carries on an insurance business or takaful business under s 60, 60A or 60B, ITA
– in the case of an individual, someone who does not have a business source of income.

The denial of the loss carry-back relief to some of the above categories of taxpayers is arguably unnecessarily restrictive. While it is noted that pioneer companies, for instance, are subject to express provisions of the Promotion of Investments Act 1986 with respect to the treatment of tax losses, several of these companies and other companies enjoying the incentives covered in the above categories would also have other taxable sources of business income. Where such taxable sources of income result in a tax loss, given the current economic situation, the ability to carry back losses would be useful to such companies. Arguably, the loss carry-back facility should have been made available to all taxable entities with taxable sources of business income.

- *Tax relief on interest on housing loans*

A new s 46B has been introduced into the ITA to grant tax relief to individuals for interest cost on housing loans in respect of sale and purchase agreements executed between 10 March 2009 and 31 December 2010. The relief will be for up to RM10, 000 per year for three years and is only available to Malaysian resident citizens in respect of one residential property. Further the individual should not derive any income from the property.

Where the interest costs are incurred by two or more individuals in respect of the same residential property, and the total interest incurred by these persons is more than RM10, 000, a formula is provided to apportion the interest deduction accordingly.

This change, while offering relief to new house buyers, will not offer relief to those individual taxpayers who are already home-owners. Furthermore, as a result of the restrictions imposed to qualify for this relief, it is unlikely that this amendment will have a significant impact on the property sector.

- *Accelerated Capital Allowances (ACAs) — Renovation and refurbishment expenditure*

The Income Tax (Amendment) Act 2009 has incorporated a change to Sch 3 of the ITA via the inclusion of a new para 8A. Para 8A provides that expenditure incurred on renovation and refurbishment of business premises be given ACAs to be claimed over two years. This would encourage taxpayers to upgrade premises to stay competitive.

The expenditure on the renovation or refurbishment must be incurred between 10 March 2009 and 31 December 2010 and the ACAs will be capped at RM100, 000. It should be noted that there is a prescribed list of qualifying expenditure (as set out in the table below). A 50% allowance will be given in each year. Where the expenditure in question qualifies as renovation/refurbishment expenditure or qualifying building expenditure, the person should elect which allowance they intend to claim.

Renovation expenditure which qualifies for accelerated capital allowances

General electrical installation	Fixed partitions
Lighting	Flooring
Gas system	Wall covering
Water system	False ceilings and cornices
Kitchen fittings	Canopies or awnings
Sanitary fittings	Fitting rooms or changing rooms
Doors, gates, windows, grills and roller shutters	Children's play areas
Recreational rooms for employees	Ornamental features or decorations excluding fine art

- *Tax exempt retrenchment benefits*

Paragraph 15(1)(b) of Sch 6 of the ITA has been amended to increase the current tax exemption in respect of retrenchment benefits or compensation for loss of employment from RM6, 000 to RM10, 000 for each completed year of service. This will only apply to payments made to individuals whose employment ended on or after 1 July 2008. It is understood that the amendment will include those retrenched under a voluntary separation scheme or mutual separation scheme.

Other measures (non-fiscal)

Several other measures were proposed, including the following.

- *Foreign workers levy*

The levy on foreign workers will be doubled for all sectors except the construction sector, plantation sector and for domestic maids. The levy will now be required to be paid by the employers and not by the foreign workers themselves. However, in the event that the services of foreign workers are prematurely terminated, the levy will be refunded on a pro-rata basis to the employers. Additionally, the bank guarantees required to be furnished by employers will be returned. While the increase in levy will increase the costs of doing business, which is not favourable in a down-turn economy, the flip-side is that it may encourage employers to hire Malaysians rather than foreign workers, as far as possible.

- *Government savings bonds*

Syariah-compliant savings bonds of RM5 billion have been issued by the Government this year. These have a maturity of three years and will provide an annual return of 5% which will be paid quarterly to bond holders. The bonds are available to all citizens aged 21 and above, with a minimum investment of RM1, 000 and a maximum of RM50, 000.

- *Human Resource Development Fund (HRDF)*

Employers in the textile, electrical and electronics industries will be exempted from the requirement to pay the HRDF levy for a period of six months with effect from 1 February 2009. Additionally, all employers will be subject to a lower levy payment rate of 0.5% as compared with the current 1% for a period of two years with effect from 1 April 2009. It is expected that this will save employers RM390 million in business costs.

- *Working Capital Guarantee Scheme*

To assist small and medium size enterprises (SMEs) meet their financing needs, the Government will establish a working capital guarantee scheme of RM5 billion. This will be available to SMEs with share capital of less than RM20 million and will be in respect of loans of up to a maximum of RM10 million with a maximum repayment term of 5 years. Under this scheme, the Government will guarantee 80% of the loans, while the remaining 20% will be guaranteed by the financial institutions. The guarantee scheme would clearly benefit many SMEs. It is hoped that SMEs will be thoroughly screened for eligibility for this scheme, and that this will not create an added strain on the Government in respect of its financial resources.

- *Industry Restructuring Guarantee Fund*

An Industry Restructuring Guarantee Fund scheme of RM5 billion will be established in respect of loans used for increased productivity, value-added activities as well as the application of green technology. This scheme will apply in respect loans of up to RM50 million with a maximum repayment term of 10 years and will be available to all companies, but the amount of guarantee provided will depend on the level of shareholder equity. The Government will guarantee 80% for companies with share capital of less than RM20 million and 50% for companies with share capital of more than RM20 million. Once again, it is hoped that there will be clear guidelines in respect of the criteria to qualify for such loans.

- *Facilitating access to the capital market*

A Financial Guarantee Institution will be established to provide credit enhancement for companies that intend to raise funds via the bond markets. The Institution will take the form of a Government-owned company with an initial paid-up capital of RM1 billion, which will ultimately be raised to RM2 billion.

The Securities Commission (SC) will also take the following steps to enable companies to raise capital more efficiently and effectively:

– Listed companies will no longer need the SC's approval to undertake a rights issue.
– Unlisted public companies will be exempted from the need to seek the SC's approval for the issuance and offerings of equity securities.
– Private limited companies will not be subject to the current Code of Take-Overs and Mergers.

– The SC will only need to be informed of amendments to terms and conditions of bond and *sukuk* issuances, where the bond and *sukuk* holders have already approved these.
– Convertible and exchangeable bonds will no longer be subject to mandatory rating requirements.

• *Automotive Industry*

The Government will contribute RM200 million to the Automotive Development Fund to ensure continued support for the automotive industry and its vendors. Additionally, the Government will assist Proton and Perodua in financing the RM5, 000 discount given where new Proton and Perodua vehicles are purchased under the auto-scrapping scheme. Under this scheme, the RM5, 000 discount is given to those who trade their old cars (which must be at least 10 years old) for new Proton or Perodua cars.

It is hoped that the Government's ongoing commitment to support these locally manufactured cars will result in positive results and increased competitiveness.

• *High net worth and skilled individuals*

To attract high net worth and skilled individuals to Malaysia, permanent resident status will be considered for those who bring more than USD2 million into Malaysia for investments or savings, as well as highly skilled foreign professionals.

• *Foreign Investment Committee (FIC)*

It was announced that the FIC will operate under a revised scope of responsibilities which will focus on more macro areas. Additionally, the Mini Budget proposed new and more liberal FIC polices, initial details of which were released on 22 April 2009. Essentially, the liberalised policies involve the lifting of the 30% Bumiputera equity requirement in 27 sub-sectors of the services industry, including the following:

– information communication technology and related services
– health and social services
– tourism services
– transport services
– sporting and other recreational services
– business services
– rental/leasing services (without operators)
– supporting and auxiliary transport services

The intention behind the move to relax the equity policy is primarily to create a conducive and competitive business environment for the services sector. Further liberalisation is expected with respect to other services sub-sectors in the near future, including the financial sub-sector. It is noted that at present, the FIC policies with respect to the acquisition of properties remain unchanged. The relaxed policies are clearly welcomed and it is hoped that the implementation of these changes will be smooth and will not involve undue bureaucracy.

Conclusion

The above summarises the tax proposals as well as some other key proposals which will impact businesses as a whole. The RM60 billion package is significant and one can expect the tax authorities to aggressively pursue taxpayers in collecting revenues for the Government in the course of tax audits and investigations. Tough times ahead are anticipated and it is hoped that the Mini Budget proposals will achieve the objectives outlined above to gradually steer Malaysia towards economic recovery. However, aside from the Mini Budget proposals, transparency, efficiency and reduced bureaucracy is also vital to attract investment and kick-start the economy.

This article has been adapted from Tax Insights, TAXAND MALAYSIA's newsletter. TG

***Renuka Bhupalan** is a Director at TAXAND MALAYSIA Sdn Bhd which is part of the global TAXAND network of independent tax consulting firms in 47 countries. She can be contacted at rb@taxand.com.my. The views expressed are the personal views of the writer.*

Alternative Legal Remedies Available to Taxpayers: Judicial Review, Relief under s 131 and Restitution

By *Tan Nian Shin and Siti Fatimah Mohd Shahrom*[1]

This article explores the alternative legal remedies available to taxpayers besides appealing to the Special Commissioners of Income Tax.

1. Introduction

In the recent case of *Ta Wu Realty Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri & Anor*[2], the Court of Appeal dismissed a judicial review application commenced by the taxpayer. The Court held that since there was a statutory remedy made available via the Income Tax Act 1967 ("ITA"), namely the Special Commissioners of Income Tax ("Special Commissioners"), the taxpayer should exhaust that avenue of appeal first. In light of this decision, this article aims to explore whether there are alternative remedies available to taxpayers besides appealing to the Special Commissioners.

It is trite law that all tax appeals against assessments are tried before the Special Commissioners[3]. Section 99(1) of the ITA provides that taxpayers may appeal to the Special Commissioners if they are aggrieved by an assessment raised by the Director General of Inland Revenue ("DGIR"). Taxpayers are required to file the notice of appeal, i.e. Form Q, within 30 days upon the service of the notice of assessment. However, where the taxpayer fails to file the notice of appeal within the prescribed time, the ITA allows the taxpayer to apply for an extension of time at any time to file the said notice[4]. This is provided the taxpayer is able to provide reasonable cause for the failure to file the said notice within the prescribed time.

As noted in *Korea Development Corporation v Government of Malaysia*[5], the Special Commissioners' powers and duties are specific and as set out in the ITA. Justice V.C. George in that case commented that:

> *"Their powers and pursuant to which their duties are clearly limited to appeals against assessments of income tax made by the Director General of Inland Revenue pursuant to the Income Tax Act...Apart from hearing and disposing of appeals against an assessment that had been duly made by the Director General the only other duties that the Special Commissioners have are: (1) to decide, on application, whether to extend the time for appealing where the appeal had not been preferred within the prescribed time…,and (2) to decide, on application, whether to set aside any agreement purported to have been arrived at between the Director General and an appellant on a review of the assessment by the Director General after an appeal had been preferred…"*

In this regard, it is clear that the jurisdiction of the Special Commissioners is confined to the perimeters of s 97A(2), 99(1), 100(4), 101(5) and 131(5) of the ITA. As such, if the taxpayer's grievance falls outside the scope of these provisions, then he will have to resort to another form of legal remedy.

2. Judicial Review of Tax Cases

2.1 Overview

Judicial review is the process that allows the Courts to exercise their supervisory jurisdiction over the decisions of:

(a) the inferior courts and tribunals, and
(b) other bodies or persons carrying out quasi-judicial functions or charged with the performance of public acts and duties[6].

Judicial review is concerned with the legality of the decision-making process and not the merits of the decision. The procedural aspect of an application for judicial review is governed by Order 53 of the Rules of the High Court 1980

1 The authors are grateful to Datuk D.P. Naban and Mr S. Saravana Kumar of Lee Hishammuddin Allen & Gledhill for having reviewed this article.
2 [2008] 6 CLJ 235
3 Appeals by way of s 97A(2) and s 131(5) of the ITA are also heard before the Special Commissioners.
4 See s 100(1) of the ITA
5 [1985] 1 CLJ 178
6 Halsbury's Laws of Malaysia, Volume 9, Administrative Law, Malayan Law Journal, 2001

("Order 53"). Order 53 governs all application seeking relief[7] such as *mandamus*[8], prohibition[9] and *certiorari*[10]. A judicial review application requires leave of the High Court[11]. Once leave is granted, the applicant may then apply for judicial review.

Although the Court of Appeal in *Ta Wu Realty Sdn Bhd* ruled that the taxpayer should have pursued its appeal before the Special Commissioners, the Court nevertheless recognised that taxpayers may commence judicial review proceedings to challenge the notices of assessment issued by the DGIR. Following the Supreme Court's decision in *Government of Malaysia & Anor. v Jagdis Singh*[12], the Court of Appeal held that in exceptional circumstances, the Courts have the discretion to hear a judicial review application despite the appeal procedure set out in the ITA. The three exceptional circumstances are:

(a) the DGIR had acted beyond the scope of his jurisdiction;
(b) there was a blatant failure by the DGIR to perform some statutory duty; or
(c) there was a serious breach of the principles of natural justice.

2.2 Leave application

To facilitate a judicial review application, the taxpayer must apply for leave of the Court within 40 days from the date when the notice of assessment or additional assessment is first communicated to the taxpayer[13]. In *Abdul Rahman Abdullah Munir & Ors v. Datuk Bandar Kuala Lumpur & Anor*[14], it was held that compliance with the time frame is fundamental. Nevertheless, O 53 allows a taxpayer to apply for an extension of time to file the leave application. The Courts will only grant an extension if they are satisfied that there are good reasons for the delay. Reasons such as the discovery of new facts after the time limit[15] or that the applicant had pursued another legal remedy that was available to him[16] have been accepted by the Courts in granting an extension. However, reasons such as mistake or negligence of the solicitors are not acceptable to the Courts[17]. In order to obtain leave, the taxpayer must establish that the application is not frivolous or vexatious[18].

2.3 Instances where Judicial Review is available

Although the Courts are generally reluctant to grant leave to judicial review applications in tax matters, there are

7 See para 1 of the Schedule to the Courts of Judicature Act 1964
8 *Mandamus* is a peremptory order requiring any person, corporation or inferior tribunal to perform a specific duty in public law – Judicial Review: Law & Procedure, Richard Gordon Q.C., 2nd edition, Sweet & Maxwell, p. 63.
9 Prohibition is a remedy used to prevent a public authority, inferior court, tribunal or other body of person from acting or continuing to act in such a way as to abuse jurisdiction or offend against natural justice, or restraining implementation of an unlawful decision or policy – Judicial Review: Law & Procedure, op. cit, p. 60
10 *Certiorari* is a remedy to quash a decision made by an inferior court, tribunal, public authority or other body of person – Halsbury's Laws of Malaysia, Volume 9, Administrative Law, Malayan Law Journal, 2001
11 Rule 3(1), O 53 of Rules of the High Court 1980
12 [1987] CLJ 110 (Rep)
13 R 3(6), O 53 of Rules of the High Court 1980
14 [2008] 6 CLJ 805. In this case, the applicant failed to seek extension of time and gave no reason for the delay. Therefore, leave for judicial review was denied.
15 *Sabah Berjaya Sdn Bhd v Director General of Inland Revenue* [1996] 5 MLJ 366
16 *Gnanasundram v Public Services Commission* [1966] 1 MLJ 157
17 *Choo & Company v Majlis Daerah Bentong; Lee Mok Fun & Anor (Interveners)* [1998] 2 CLJ Supp 464
18 *Tang Kwor Ham & Ors v Pengurusan Danaharta Nasional Bhd & Ors* [2006] 1 CLJ 927

instances where taxpayers have successfully persuaded the Courts to grant leave and hear their judicial review applications. Those instances are discussed below.

(a) DGIR is under a statutory obligation to perform a duty towards the taxpayer

In *Bandar Utama City Corp Sdn Bhd v Director General of Inland Revenue and Another Action*[19], the DGIR raised additional assessments against the taxpayer by way of an adjustment under s 140(1)(c) of the ITA. The adjustment was purportedly done on the ground that the taxpayer had evaded or avoided liability which would otherwise have been imposed under the ITA. Since the DGIR had invoked s 140(1)(c), the DGIR was required to issue "particulars of the adjustment" with the notices of additional assessment as stipulated in s 140(5). When the DGIR refused to issue the said particulars, the taxpayer sought an order of *mandamus* to compel the DGIR to carry out the express statutory duty stipulated under the ITA. The High Court, in granting the order of *mandamus*, remarked that s 140(5) imposes a duty on the DGIR to issue "particulars of the adjustment". The Court added that the DGIR's statutory duty under s 140(5) had also been judicially enunciated before by the Supreme Court in *Director General of Inland Revenue v Hup Cheong Timber (Labis) Sdn Bhd*[20] and *Director General of Inland Revenue v Rakyat Berjaya Sdn Bhd*[21].

(b) Issuance of notice of additional assessment without evidence

In *Sabah Berjaya Sdn Bhd v Director General Of Inland Revenue Department & Anor*[22], the taxpayer discovered during the trial before the Special Commissioners that the DGIR, at the time of issuing the notices of additional assessment, had no evidence that justified a departure from the original notices of assessment. Further, the taxpayer also discovered that the DGIR had issued the notices of additional assessment first and then proceeded to look for evidence to justify his actions retrospectively. The taxpayer sought judicial review on the basis that by issuing the notices of additional assessment before seeking any evidence, the DGIR had acted without jurisdiction and committed a serious breach of the statutory provisions of the ITA and the rules of natural justice. The taxpayer argued that the DGIR is required to provide the taxpayer the opportunity to be heard before the DGIR exercises the powers conferred on him by the ITA.

The High Court granted leave for judicial review on the basis that the taxpayer was challenging the arbitrariness of the action taken by the DGIR and this fell within the exceptional circumstances enunciated in *Jagdis Singh*.

(c) The Special Commissioners acting beyond their jurisdiction

Judicial review had been granted in circumstances where the Special Commissioners had exceeded their jurisdiction[23] or did not have jurisdiction to hear and decide the appeal[24]. In *Rheem (Far East) Pte Ltd*, the DGIR issued a requisition (i.e. Form S) demanding for payment by virtue of s 108(5) of the ITA against the taxpayer as the taxpayer had insufficient credit in its s 108 account. The taxpayer appealed to the Special Commissioners against the requisition issued by the DGIR. The DGIR objected to the proceedings on the basis that the Special Commissioners had no jurisdiction to hear an appeal against a requisition. When the Special Commissioners held that they had the jurisdiction, the DGIR applied, by way of judicial review to the High Court, to have the decision quashed by way of an order of *certiorari*. The High Court granted the order of *certiorari* and ruled that the amount demanded in a requisition was not tax but a debt due and payable to the Government from the taxpayer. The High Court ruled that the Special Commissioners had committed an error of law in concluding that the requisition meant a demand for tax. Similarly, in the case of *Malayan*

19 (1999) MSTC 3,725
20 [1985] 2 MLJ 322
21 [1984] 1 MLJ 248
22 (1996) MSTC 3,544
23 *Ketua Pengarah Hasil Dalam Negeri v Rheem (Far East) Pte Ltd* [1998] 2 CLJ Supp 351
24 *Malayan United Industries Bhd v Ketua Pengarah Hasil Dalam Negeri & Anor* [2006] 5 CLJ 240

United Industries Bhd, the High Court held that judicial review is the most appropriate, convenient and suitable procedure to challenge a requisition issued by the DGIR.

However, in *Ngee Tai Shipping Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri*[25], the High Court had chosen not to follow the decision of *Rheem (Far East) Sdn Bhd* and *Malayan United Industries*. Instead, the High Court held that the Special Commissioners had the jurisdiction to decide on an appeal against a requisition.

Although there are two different approaches taken by the High Court with regard to this matter, the authors prefer the approach taken in *Rheem (Far East) Sdn Bhd* and *Malayan United Industries*. In *Korea Development Corporation*, Justice V.C. George in a well considered decision held that the withholding of tax under s 107A was not an advance assessment under the ITA and ruled that the Special Commissioners do not have jurisdiction to entertain any appeal in respect of matters arising from the collection and recovery of tax. His Lordship observed that s 107A is within Part VII of the ITA, which deals with collection and recovery of tax. His Lordship also added that the Special Commissioners' jurisdiction is confined to the perimeter prescribed in the ITA. In this regard, given that s 108(5) also falls within Part VII of the ITA; the authors following the reasoning in *Korea Development Corporation* are of the view that the Special Commissioners have no jurisdiction to hear an appeal against a requisition.

(d) Misdirection in law

In *Board of Trustees of Sabah Foundation v DGIR*[26], the taxpayer was granted an order of *certiorari* to quash the DGIR's decision that the taxpayer was not a charitable institution. The High Court also quashed the DGIR's refusal to grant the taxpayer a tax exemption under Sch 6 of the ITA. The High Court held that the DGIR had misdirected himself in law and ordered the taxpayer's application for tax exemption be remitted to the DGIR in light of the grounds of judgment provided by the Court.

2.4 Other examples

Recently, in *Goh Eng Hwa v. Ketua Pengarah Hasil Dalam Negeri dan Satu Lagi*[27] the taxpayer applied for a declaration that he did not owe a sum of RM 62,321.61 to the DGIR. The taxpayer also sought to cancel the travel restriction certificate issued by the DGIR under s 104 of the ITA. The taxpayer commenced his action by way of an originating summons. The IRB argued that the taxpayer's application was an abuse of court process. The High Court dismissed the taxpayer's originating summons on the basis that judicial review was the proper means to challenge a decision made by a public body. Interestingly, this decision infers that if a taxpayer is aggrieved with the decision of the DGIR which is a public body, then the taxpayer should initiate judicial review application instead of other private law rights or remedies. Although the High Court in *Goh Eng Hwa* was silent on this, the authors submit that a taxpayer may only pursue a judicial review application if

the taxpayer's case fall within the one of the three exceptional circumstances enunciated in *Jagdis Singh*.

Further, the decision in *Goh Eng Hwa* also illustrates that judicial review is the appropriate forum to challenge the IRB's decision to issue a travel restriction certificate pursuant to s 104 of the ITA. Since s 104 of the ITA is not an assessment, the taxpayer may not appeal to the Special Commissioners. As discussed earlier, s 99 of the ITA clearly states that the taxpayer may only appeal against an assessment to the Special Commissioners. Further, this approach is also consistent with decisions like *Rheem (Far East) Sdn Bhd* and *Korea Development Corporation*.

25 [2007] 6 CLJ 724
26 (2002) MSTC 3,894
27 [2008] 8 CLJ 777

3. Section 131 of the ITA and the remedy of restitution

3.1 Section 131 of the ITA

Section 131 of ITA[28] provides relief for a taxpayer who has paid excessive tax by reason of error or mistake in a tax return or statement made by him. The taxpayer may seek the relief within six years after the end of the year of assessment in which the assessment was made. The application for relief is made by writing to the DGIR. If the DGIR decides not to grant the relief, then the taxpayer may appeal to the Special Commissioners[29].

In *J Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri*[30], the Special Commissioners allowed the taxpayer's appeal against the DGIR's decision to reject the taxpayer's claim under s 131 of the ITA. In this case, the taxpayer had initially submitted its tax return based on the first set of accounts. Subsequently, the taxpayer amended the first set of accounts when it realised that the accounts were incorrect and submitted the amended accounts to the IRB. The amended accounts were adopted at the taxpayer's Annual General Meeting. The taxpayer claimed that the tax return contained errors as it was prepared based on the first set of accounts, which was incorrect. The DGIR rejected the taxpayer's application under s 131. Ruling in favour of the taxpayer, the Special Commissioners held that the DGIR had failed to give any basis or evidence to support its decision for rejecting the taxpayer's application.

3.2 Restitution

Taxpayers may also seek the common law remedy of restitution, if they had paid excessive tax by way of mistake and there is no remedy available under the ITA as the principle of unjust enrichment is accepted as the underlying basis for a restitutionary claim[31]. The House of Lords in *Deutsche Morgan Grenfell Group plc v Inland Revenue Commissioners and the Attorney General*[32] held that taxes paid under a mistake of law may be recovered from the Revenue by way of restitution. Lord Hoffman commented that *there was no reason to infer that Parliament intended to exclude a common law remedy in all cases of mistake in which the Revenue were unjustly enriched but which did not fall within the statutory tax appeal procedure.*

Essentially, in seeking restitution, taxpayers must establish that the IRB has been unjustly enriched by the excessive taxes paid by the taxpayers due to a mistake of law. Although the remedy of restitution is recognised by our law[33], to the best of the authors' knowledge, it has yet to be tested in a tax case in Malaysia.

4. Conclusion

Apart from appealing to the Special Commissioners, there are other alternative remedies available to taxpayers.

For instance, taxpayers are entitled to pursue judicial review if they are aggrieved by the DGIR's decision of raising assessments arbitrarily. Likewise, judicial review is also the appropriate remedy to challenge instances where the DGIR or SCIT had acted in excess of jurisdiction or misdirected themselves in law. However, it must be noted that taxpayers must establish that their case falls within one of the exceptional circumstances prescribed in *Jagdis Singh* to warrant the Court to grant leave for judicial review. Meanwhile, the relief under s 131 of the ITA and the remedy of restitution are appropriate in circumstances where the taxpayer had paid excessive taxes under a mistake of law. TG

Tan Nian Shin *and* ***Siti Fatimah Mohd Shahrom*** *are tax lawyers with Lee Hishammuddin Allen & Gledhill. They appear regularly before the Special Commissioners of Income for various tax cases. They are both members of the English Bar and Malaysian Bar. Tan Nian Shin and Siti Fatimah can be contacted at tax@lh-ag.com.The content of this article represents the authors' personal views and not that of Lee Hishammuddin Allen & Gledhill.*

28 *"If any person who has paid tax for any year of assessment alleges that an assessment relating to that year is excessive by reason of some error or mistake in a return or statement made by him for the purposes of this Act and furnished by him to the Director General prior to the assessment becoming final and conclusive, he may within six years after the end of the year of assessment within the assessment was made make an application in writing to the Director General for relief."*

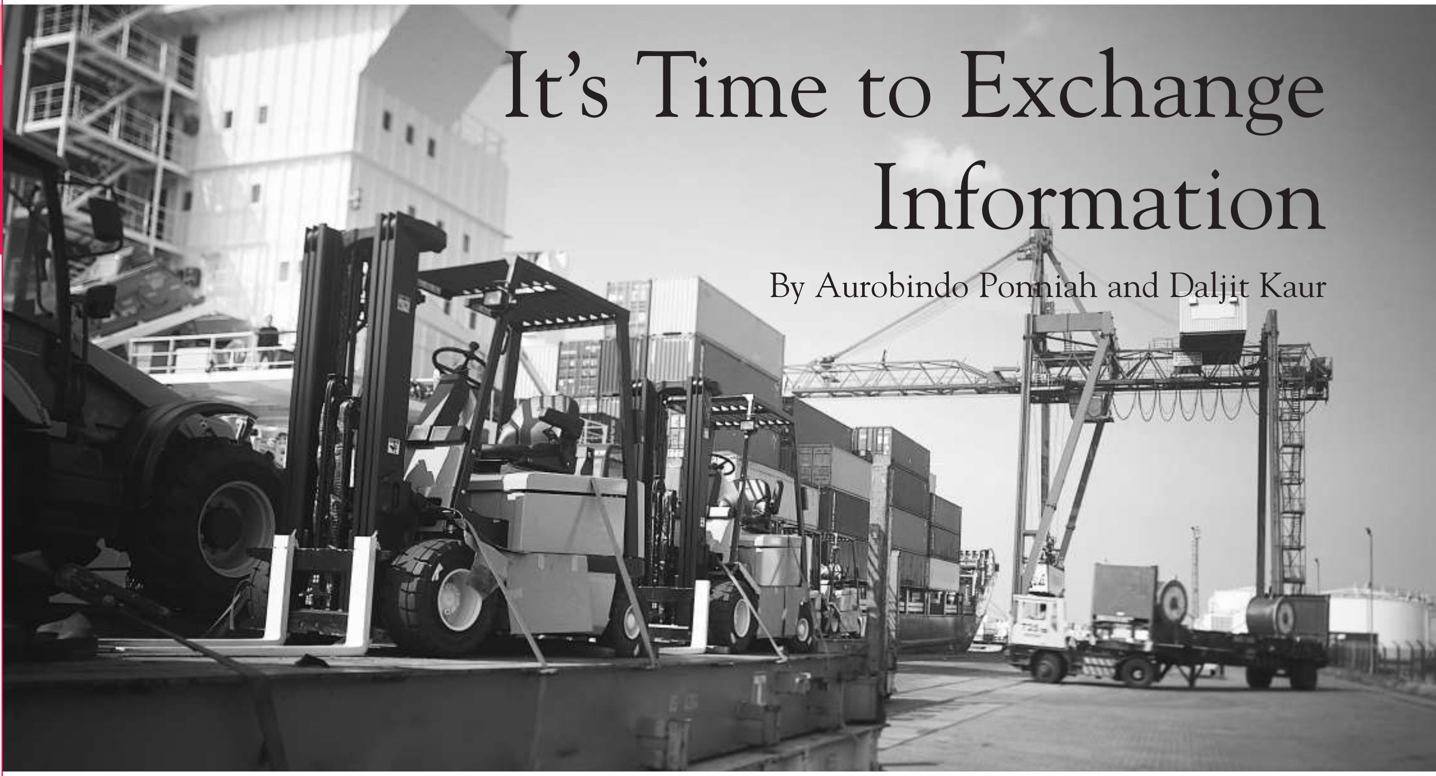
29 See s 131(5) of the ITA

30 (1999) MSTC 3,037

31 *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32; *Woolwich Equitable Building Society v Inland Revenue Commissioners* [1993] AC 70 HL; *Koh Siew Keng (P) & Anor v Koh Heng Jin* [2008] 3 MLJ 822

32 [2007] 1 All ER 449

33 Section 3 of the Civil Law Act 1956: *Port Swettenham Authority v TW Wu* [1978] 2 MLJ 105 PC and Sections 66 and 73 of the Contracts Act 1960: *Menaka v Lum Kum Chum* [1969] 1 MLJ 72



It's Time to Exchange Information

By Aurobindo Ponniah and Daljit Kaur

"Perchance he for whom this bell tolls may be so ill, as that he knows not it tolls for him; and perchance I may think myself so much better than I am, as that they who are about me, and see my state, may have caused it to toll for me, and I know not that."

John Donne (1572–1631), *Devotions Upon Emergent Occasions*

1. Introduction

On 2 April 2009, the Organisation for Economic Cooperation and Development (OECD) issued a report on the progress made by jurisdictions and financial centres around the world towards the implementation of the internationally agreed standard on exchange of information (EOI) for tax purposes.[1]

The report is of great relevance to Malaysia, specifically Labuan, which was negatively mentioned as a jurisdiction which has not committed to the EOI standard alongside the Philippines, Costa Rica and Uruguay. The report is divided into three main categories, with Labuan falling into what is popularly known as the "black list", i.e. jurisdictions which have not committed to the internationally agreed tax standard on EOI. The other two categories of the report refer to jurisdictions which have substantially implemented the standard (the "white list"), or jurisdictions (tax havens and financial centres) which have committed to the standard but have not substantially implemented it (the "grey list").

The OECD's progress report was widely anticipated and many countries that feared being on the "black list" had, in the weeks and days leading up to the April G20 London Summit (where the report was to be released), issued statements of their intention to meet the internationally agreed standard of EOI for tax purposes. This included Switzerland, Singapore, Hong Kong, Macau, etc. Malaysia, unfortunately, appears to have been caught unawares and did not make its intentions, with regard to Labuan, clear prior to the release of the report.

In response to this, the Labuan Offshore Financial Services Authority (LOFSA) issued a statement to clarify its position, on 3 April 2009. Among others, it was stated that Malaysia has been committed in practice to the standards, and has been "co-operative" with competent authorities from other countries with regard to suspected tax evasion or other financial crimes, including money laundering. In addition, as part of an update in 2008 to Labuan's laws (which are currently awaiting Parliamentary approval), the provisions with respect to EOI have been said to be tightened. The updated laws are not publicly available at the time of the writing of this article; therefore whether or not the changes meet internationally acceptable standards remains to be seen.

On 7 April 2009, the OECD released a statement that all the previously blacklisted countries, including Labuan, have been moved onto the grey list, i.e. they are committed to the fight against tax abuse and will introduce provisions in their domestic law and treaties to implement the EOI standard. Other countries in Asia-Pacific that belong to the grey list include Singapore, Brunei and Bahrain. It should be noted that Hong Kong and Macau are not listed in the OECD's progress report but it is stated that both jurisdictions are committed to implementing the EOI standard.

1 The principles of transparency and exchange of information ("EOI") were developed by the OECD's Global Forum on Transparency and Exchange of Information. Recently, the United Nations (UN) Committee of Experts on International Cooperation in Tax Matters also incorporated the principles into the UN Model Tax Convention. These standards have now been accepted by the member countries of the OECD, and many non-OECD member countries as well, clearly establishing an internationally agreed standard for transparency and the exchange of information on tax matters.

2. The meaning of EOI

Increasing cross-border activity and the globalisation of economies have led to the need for tax transparency and cooperation between tax authorities, so that countries can fully enforce their tax law in a fair manner.

A key element of cooperation between tax authorities is the exchanging of information, which thus forms a focal part of the OECD's efforts to combat harmful tax practices. The exchange of information enables governments to enforce their domestic tax laws and also to gather information with respect to situations in which the provisions of a tax treaty are being applied.

Both the OECD and UN model tax conventions include a provision (usually Art. 26) that permits tax authorities to exchange information. In addition, the OECD and its working groups have also developed model bilateral agreements specifically for the exchange of information on tax matters (Tax Information Exchange Agreements ("TIEA")) to assist committed jurisdictions and financial centres to meet the agreed international tax standard.

In the case of Labuan, being part of Malaysia, it "rides" on Malaysia's tax treaties with other countries in so far as they have not excluded Labuan from the scope of the treaties[2]. However, the exchange of information articles contained in Malaysia's tax treaties do not completely fulfill the OECD's standards as per the 2005 and 2008 model treaty conventions, in that the standards require information to be exchanged regardless of whether the country supplying the information has a domestic interest in such information, whereas Malaysia's domestic laws and information exchange articles in treaties are not as wide. It is useful to note that there is currently no OECD member country that requires a domestic tax interest in order to exchange information[3].

In addition to this, Malaysia (or Labuan) has yet to conclude TIEAs with other countries. The signing of TIEAs is an important demonstration of commitment to the international standard; traditional "tax haven" countries which have been previously identified by the OECD as being un-cooperative such as Barbados, Guernsey, the Isle of Man, Jersey, and the U.S. Virgin Islands have actively signed TIEAs in recent years and as such have been categorised as jurisdictions which have substantially implemented the standard in the 2009 progress report.

3. Impact on Labuan if standard not adopted

The OECD's standard on EOI does not have the force of law and Malaysia, being a non-member country, is not obliged to comply with its standards. Having said this, the OECD has working relationships with many non-member countries in Asia, Europe, Africa, Latin America, the Middle East, and its initiatives are often observed globally.

As mentioned above, traditional "tax havens" have substantially implemented the EOI standard, so failure to adopt the standard could cause damage to Labuan's reputation as an international business and financial centre.

In addition, the OECD's 2009 progress report which was released at the meeting of G-20 leaders in London is relied on by the G-20 as part of its efforts to end bank secrecy by identifying countries that are against tax transparency and the EOI standard. In this regard, the G-20 announced that they were ready to take agreed action against jurisdictions which do not meet international standards on tax transparency. These measures include increased disclosure requirements, application of withholding taxes in respect of a wide variety of payments, restriction on tax deductions on expense payments made to residents of a non-cooperative jurisdiction and a review of tax treaty policy and bilateral aid programs with such jurisdictions.

4. Conclusion

Labuan has managed to earn itself a place on the OECD's "grey list" by virtue of the communication of its intentions to comply with the EOI standard.

Whether or not it is able to progress onto the white list depends on whether and how their intentions to follow the standard are implemented. From a tax perspective, changes have to be made to Malaysia's domestic laws to widen the scope of gathering information and to liberalise the scope of information that may be exchanged, either via the information exchange article in tax treaties, or through the signing of TIEAs. These changes are important to ensure that Labuan remains competitive and relevant in the fight for global business.

Ideally, the Malaysian authorities need to conduct a comprehensive review of not just the tax laws but other associated laws (e.g. banking secrecy laws, etc) in order to facilitate compliance with the EOI standard. However, in the long term, one has to take a look at the position of (and where necessary make changes to) the Labuan regime vis-à-vis wider Malaysian interests as the changing facts on the ground will give rise to more aggressive moves by other jurisdictions to prevent a loss of tax revenue. TG

***Aurobindo Ponniah** is the Head of the International Bureau of Fiscal Documentation's (IBFD) Asia-Pacific activities while **Daljit Kaur** is a Senior Research Associate at the IBFD. They can be contacted via ibfdasia@ibfd.org. The views expressed in this article represent the personal views of the authors and should not be taken as representing the views of the IBFD.*

2 At present, 11 countries have excluded Labuan from the scope of their tax treaties. The countries are the United Kingdom, Australia, Japan, Spain, Chile, Luxembourg, Seychelles, Netherlands, Sweden, South Africa and Indonesia. Additionally, a number of countries have "blacklisted" Malaysia (among others) as a jurisdiction which may be practicing harmful tax measures, resulting in any transactions by their residents with Malaysian entities being subject to higher scrutiny. An example is South Korea, which passed a domestic law targeting transactions between its residents and entities located in specified low-tax jurisdictions and to-date, Labuan is the only jurisdiction specified. Pursuant to the change in the South Korean law, any payments to a Labuan entity are subject to the higher domestic withholding tax rate unless permission is obtained to apply the lower tax treaty rate.

3 "Improving Access to Bank Information for Tax Purposes: The 2003 Progress Report", OECD, pp 7–9.

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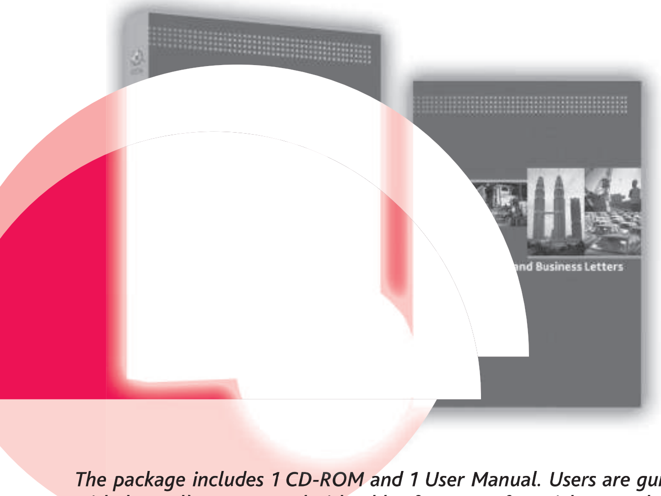

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Income Tax (Amendment) Act 2009 (Act A1349)

The *Income Tax (Amendment) Act 2009* was enacted to give effect to the 2009 Second Stimulus Package. The Act received royal assent on 18 April 2009, and was published in the Government Gazette on 23 April 2009. The Act amends the *Income Tax Act 1967* and is generally effective from the year of assessment 2008. The changes legislated are discussed on page 18 of this issue, "Malaysia's Mini-Budget-Economic Stimulus Package".

Income Tax (Exemption) Order 2009 (PU(A) 152/2009)

Effective generally from the year of assessment 2008 onwards, specified benefits and gifts received by employees from their employers are exempt from payment of income tax.

The tax-exempt benefits are:
- travelling allowance, petrol card and petrol allowance
- parking rate and parking allowance
- meal allowance
- child care allowance
- payment for traditional medicine and maternity expenses
- discounted price for services provided by the business of the employer and for the benefit of the employee, spouse and child of the employee
- monthly bill for subscription of broadband, fixed line telephone, mobile phone and pager registered under the name of employee or employer
- subsidy of interest of housing, education and car loan.

The tax-exempt gifts are:
- pager
- personal digital assistant (PDA)
- telephone
- mobile phone.

The amount exempted is subject to the following limits:
- travelling allowance, petrol card, petrol allowance or any of its combination, for travel to and from home and the place of work — RM2, 400 per year (Note: this is the only provision effective from YA 2008 to YA 2010.)
- travelling allowance, petrol card, petrol allowance or toll payment or any of its combination, for travelling in the performance of employment at a place other than the employee's place of work — RM6,000 per year
- child care allowance — RM2,400 per year
- discounted price for consumable business products of employer — RM1,000 per year
- subsidy on interest of housing, education or car loan — an amount determined by the formula A x B/C, where
  - A is the difference between interest borne by the employee and interest payable by the employee for a year of assessment;
  - B is the total aggregate of balance of the principal amount of the housing, education or car loan taken by the employee in the year of assessment, or RM300,000, whichever is the lower; and
  - C is the total aggregate of the principal amount of the housing, education or car loan taken by the employee.

Note that despite the exemption, the employee would still have to comply with requirements to submit returns and keep records of statements, statements of accounts or any other information under the provisions of the *Income Tax Act 1967*. The exemption does not apply if:

- the employee has control over the employer, or another company that has control over the employer, through the holding of shares, possession of voting power, or any power conferred by the articles of association or other document
- in a partnership, the employee is a partner
- in a sole proprietorship, the employee and the employer are the same person.

Income Tax (Deduction for Benefit and Gift from Employer to Employee) Rules 2009 (PU(A) 153/2009)

Effective generally from the year of assessment 2008 onwards, a tax deduction is allowed against the adjusted income of a resident person from its business for expenses incurred in providing the following benefits and gifts to its employees:

- payment of monthly bill for broadband, fixed line telephone, mobile phone or pager issued in the name of the employee or employer
- travelling allowance, petrol card or petrol allowance for travel to and from home and the place of work
- PDA, telephone, mobile phone and pager.

Income Tax (Exemption) (No. 2) Order 2009 (PU(A) 156/2009)

Deemed effective from 2 September 2006, the statutory income of an approved company, derived from an approved business is exempt from payment of income tax for 10 consecutive years of assessment commencing after its exempt year of assessment.

The amount exempt is calculated as A/B x C, where:
- A is the tax charged on the chargeable income of the approved company in respect of its approved business at the prevailing tax rate, reduced by the tax charged on such chargeable income at the rate of 20%.
- B is the amount of tax charged on such chargeable income at the prevailing tax rate, and
- C is the amount of chargeable income.

Applicable definitions are:
- "approved company" — a Bio Nexus status company that has been given an exemption from the payment of income tax under the Income Tax (Exemption (No. 17) Order 2007 (PU(A) 371/2007) or Income Tax (Exemption) (No. 18) Order 2007 (PU(A) 372/2007) ("the Exemption Orders")
- "approved business" — the new business and expansion project as defined in the Exemption Orders
- "the exempt year of assessment" — the year of assessment where an approved company has been given exemption from the payment of income tax under the Exemption Orders.

Income derived by the approved company from an approved business is to be treated as a separate and distinct business source, and a separate account is to be maintained. Note that despite the exemption, the employee would still have to comply with requirements to submit returns and keep records of statements, statements of accounts or any other information under the provisions of the *Income Tax Act 1967*.

Income Tax (Exemption) (Amendment) Order 2009
This Order amends paragraphs 3(1) and 4(a) of the Income Tax (Exemption) (No.11) Order 2005 (PU(A) 75/2005) ("the 2005 Order"). Where an exemption is granted to a venture capital company under the 2005 Order, such exemption shall (subject to the provisions of the 2005 Order) continue to remain in full force and effect.

Pursuant to the 2009 Order, a venture capital company is exempted from income tax on statutory income from all sources, other than interest income arising from savings or fixed deposits and profits from syariah-based deposits, from the year of assessment 2008 or the year of assessment in which the venture capital company commences business, whichever is the later. The venture capital company shall, for each year of assessment during the period of exemption, obtain a certification from the Securities Commission (SC) confirming the level of its investment in the venture company and seed capital.

The exemption is for a period of 10 years or the years of assessment equivalent to the life of the fund established for the purpose of investing in a venture company, whichever is the lesser; provided that it has invested at least 70% of its invested funds in venture companies, or at least 50% of its invested funds in the form of seed capital, at the point of the first investment.

The exemption is reduced to a period of 5 years or the years of assessment equivalent to the life of the fund established for the purpose of investing in a venture company, whichever is the lesser; provided that it has invested at least 30% of its invested funds in the form of seed capital, start-up financing, early stage financing or its combination in venture companies at the point of the first investment and it has made the application for exemption to the SC between 30 August 2008 and 31 December 2013.

Second Addendum to Public Ruling No. 1/2006 — Perquisites from Employment (Issued: 25 Feb 2009. Effective: YA 2008 onwards)
The Addendum clarifies the tax exemption on perquisites received by employees in relation to:

- innovation or productivity award (Schedule 6 Para 25C of the Income Tax Act 1967)
- gift of new personal computer (Income Tax (Exemption) (No. 4) Order 2008
- allowances, subsidised interest and gifts.

A copy of the Ruling may be obtained from the IRB's website, http://www.hasil.gov.my, under "Law and Regulations" — "Public Rulings".

Third Addendum to Public Ruling No. 2/2004 — Benefits-In-Kind (Issued: 17 Apr 2009. Effective: YA 2008 onwards)
The Addendum clarifies tax exemptions on benefits-in-kind provided to employees including exemptions covered under the Income Tax (Exemption) Order 2009, effective from the year of assessment 2008. A copy of the Ruling may be obtained from the IRB's website, http://www.hasil.gov.my, under "Law and Regulations" — "Public Rulings".

Guidelines on exempted perquisites and benefits-in-kind
On 28 April 2009, the IRB issued guidance on the Second Addendum to Public Ruling 1/2006 — *Perquisites from Employment* and the Third Addendum to Public Ruling 2/2004 — *Benefits-In-Kind*.

Employers who did not accurately take into account the tax-exempt perquisites or benefits-in-kind in the preparation of their EA Forms for the year ended 31 December 2008 are advised to issue a verification letter to the relevant employees to enable the employees to declare the correct income in their 2008 tax return. Taxpayers who have filed their returns for YA 2008, incorrectly accounting for tax-exempt perquisites or benefits-in-kind may submit an appeal to their respective IRB office, together with the employer's letter. No deadlines have been given for these.

Other Guidelines

1. *Guidelines on the 2009 Mini Budget (issued 10 March 2009)*
2. *Guidelines and procedures for application for pioneer status/investment tax allowance under the Promotion of Investments Act 1986 for the establishment of forest plantation (issued 10 March 2009)*
3. *Guidelines for application for tax incentive for software development (issued 10 March 2009)*
4. *Guidelines and procedures for application of tax incentives under the Promotion of Investments Act 1986 and/or expatriate posts for medical device testing laboratories (issued 10 March 2009)*
5. *Guidelines for application of import duty and sales tax exemption on energy conservation equipment (issued March 2009)*
6. *Guidelines for application of import duty and sales tax exemption on equipment using renewable energy resources*
7. *Guidelines for application of deduction under s 34(6)(ha) Income Tax Act 1967 for computation of income tax*
8. *Guidelines on incentives for last mile network facilities provider for broadband*
9. *Guidelines and procedure for applying tax incentive under the Promotion of Investments Act 1986 for providing energy conservation (EC)/energy efficiency (EE) services*

The abovementioned guidelines have been issued by the relevant authorities, and are available on the IRB's website (www.hasil.gov.my), MIDA's website (www.mida.gov.my) and CTIM's website (www.ctim.org.my).

Case Commentaries

Ketua Pengarah Hasil Dalam Negeri v Steruda Sdn Bhd

In this article, Foong Pui Chi reviews the recent Court of Appeal decision in Ketua Pengarah Hasil Dalam Negeri v Steruda Sdn Bhd[i] *in relation to when a payment is considered to be a bonus.*

Facts of the Case

The taxpayer, Steruda Sdn Bhd ("Steruda"), is a company which provides consultancy services in gynaecology, obstetrics and other branches of medicine. On 12 July 1976, Steruda entered into an employment agreement with one Dr McCoy, who is also a shareholder and director of Steruda, whereby Dr McCoy was to be paid remuneration of RM3, 000.00 per month plus an annual 25% net profit of the clinic.

The issue in this case was whether the said 25% net profit amounted to a bonus. If it was not a bonus, then it was part of Dr McCoy's salary and the entire 25% net profit amount, along with the monthly RM3,000.00, would be deductible from Steruda's gross income under s 33(1) of the *Income Tax Act 1967* ("ITA"), so that Steruda would pay less tax. Conversely, if it was a bonus, only the equivalent of two-twelfths of Dr McCoy's salary would be deductible from Steruda's gross income.

The crucial provision in this case was s 39(1) of the ITA and the restriction on the deductibility of bonus payments was in sub-paragraph (h)[ii] which read as follows:

> *"39. (1) Subject to any express provision of this Act, in ascertaining the adjusted income of any person from any source for the basis period for a year of assessment no deduction from the gross income from that source for that period shall be allowed in respect of —*
>
> *(a) – (g) …;*
>
> *(h) any sum paid by way of a bonus to an employee in excess of one thousand ringgit or two-twelfths of his wages or salary whichever is the greater…"*

The dispute arose when the Director General of Inland Revenue ("DGIR") raised seven notices of additional assessment ("NOAAs") for the years of assessments ("YAs") 1978 to 1984 against Steruda to disallow the deduction of Dr McCoy's remuneration of 25% of the net profit of the clinic from Steruda's gross income. Only two-twelfths of the full 25% was deductible. In other words, the DGIR contended that the 25% net profit of the clinic, being a bonus payment made to Dr McCoy, was caught by s 39(1)(h) of the ITA.

Steruda appealed against the NOAAs on the basis that the payment of 25% of net profit of the clinic was part of Dr McCoy's remuneration pursuant to his employment agreement and was not a bonus payment. The appeal, which was dismissed by the Special Commissioners of Income Tax ("SCIT"), was referred to the High Court by way of case stated under para 34 of Sch 5 to the ITA.

Decision of the High Court[iii]

At the High Court, the learned Judge stated that the sum of RM3,000.00 per month was not normal remuneration as it did not commensurate with the status of Dr McCoy as senior obstetrician and gynaecologist. In this sense, the learned Judge was of the view that the RM3, 000.00 per month was only part of Dr McCoy's total remuneration, with the 25% net profit being simply a method of calculating the remaining part of his salary. Furthermore, the payment of 25% net profit was neither discretionary nor subject to review. As such, the learned Judge held that the SCIT had erred when they:

concluded that simply because the component of payment of 25% of the net profit was over and above the monthly sum of RM3,000.00, the balance sum must be a bonus; and

failed to give due consideration to the fact that the payment to Dr McCoy consisted of two parts of a single contractual obligation.

The High Court reversed the findings of the SCIT and decided in favour of Steruda, which decision was appealed by the DGIR to the Court of Appeal.

Analysis of precedents

In the course of the appeal, the DGIR cited, among others, two Supreme Court cases in support of its contention that the 25% net profit of the clinic was a bonus:

- **DGIR v Harrisons & Crosfield (M) Sdn Bhd**[iv] ("H&C")
  In this case, the management staff of H&C was remunerated with, among others, fixed salaries and additional remuneration under a scheme called Additional Remuneration Scheme ("ARS"), which was based upon a percentage of the combined audited profits of H&C. Another scheme, which was in the nature of a bonus scheme, operated side by side with the ARS. H&C contended that the ARS should be regarded as either "commission" or "deferred salary". The DGIR, however, took the position that the ARS was in fact a form of bonus and disallowed any deduction of the payments from H&C's income.

  In the course of its deliberation, the Supreme Court found that not only was the ARS separate and distinct from the fixed salaries, the basis of participation in the ARS and the individual rates were also subject to review by the employer. Accordingly, the Supreme Court held that regardless of the fact that it was called ARS and not "bonus", the ARS was nothing more than a bonus in law.

- **DGIR v Highlands Malaya Plantation**[v] ("HMP")
  Apart from monthly salaries, the managerial staff of HMP were each entitled to participate in the group bonus scheme in accordance with standard letters of appointment. On the other hand, the non-managerial staff were each paid a bonus at the discretion of HMP as there was no contractual obligation in this respect on the part of HMP.

  For YA 1975, the DGIR disallowed as a deduction from the gross income of HMP, the bonus paid to the managerial staff under the scheme which was in excess of the limits stipulated in s 39(1)(h) of the ITA. HMP contended that the additional remuneration paid to the managerial staff was actually a "commission" and not "bonus".

The Supreme Court held that whether the payment was gratuitous or contractual, it could still be a bonus and that a bonus could be a mere gift or gesture of

goodwill and unenforceable or an entitlement on the happening of a condition precedent and enforceable on fulfillment of the condition.

Having examined the facts of the two Supreme Court cases, the Court of Appeal came to the conclusion that those cases could be easily distinguished from the facts of Steruda. For instance, the Court of Appeal highlighted that the bonus in H&C was compartmentalised under a separate and special heading called the ARS, under which selected management staff were entitled to participate in the profits of H&C, and that it had a discretionary quality, unlike the fixed salaries which were beyond any adjustment or review of the employer.

Similarly, the Court of Appeal also pointed out that in HMP, both the managerial and non-managerial staff were paid additional remuneration pursuant to a scheme that carried the word "bonus" from the very beginning and the same was also subject to the discretion of the employer.

Characteristics of "bonus"

As there is no statutory definition of the word "bonus" in the ITA, the Court of Appeal referred to several Commonwealth cases, namely ***Re Eddystone Marine Insurance Co.***[vi], ***Shelford v Mosey***[vii], ***Sutton v Attorney-General***[viii] and ***Great Western Garment Co. Ltd v Minister of National Revenue***[ix], to discover its meaning and based on those authorities, the Court of Appeal expressed the characteristics of "bonus" to be as follows:

(i) it is in addition to the wages paid to an employee, something that is over and above the agreed remuneration;

(ii) it may be in the nature of a gift, temporary boon or something freely given at the discretion of the employer as opposed to being an agreed normal remuneration; and

(iii) it includes payment which is legally due or contractually provided for.

Decision of the Court of Appeal

Bearing in mind that there was an intention to make the deferred payment of 25% net profit of the clinic part of Dr McCoy's remuneration, the Court of Appeal stated that the four corners of Dr McCoy's employment agreement must be scrutinised as a whole[x] in order to ascertain whether the 25% net profit amounted to a bonus. Based upon a reading of Dr McCoy's employment agreement, the Court of Appeal found the following facts which subsequently led to the dismissal of the DGIR's appeal:

(i) the 25% payment was not at the discretion of anyone and was part and parcel of Dr McCoy's salary as clearly provided for in the employment agreement; and

(ii) if there was no profit, Dr McCoy received no additional remuneration; but even if the annual profit was small, he would nevertheless receive a small but fixed 25% payment.

In light of the above, the Court of Appeal held that the 25% net profit payment, however small, did not amount to a bonus payment as it was neither discretionary nor subject to review by Steruda. In fact, Steruda was contractually bound to pay the same to Dr McCoy as part of his total remuneration.

As a final note, the Court of Appeal also pointed out that based upon a comparison with the income of another medical practitioner, Dr McCoy's monthly remuneration of RM3,000.00 clearly did not commensurate with his status and qualifications. That consideration further supported the decision of the Court of Appeal that the 25% payment formed part of Dr McCoy's salary as intended by the parties.

Conclusion

This decision is welcomed as the issue of when a payment is considered to be a bonus has now been clarified by the Court of Appeal. Further, the Court of Appeal has affirmed and applied the trite principle that a court must always pay close attention to the substance of a contract and not only its form. TG

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i Rayuan Sivil No. W-01-52-04. Judgment delivered on 31 March 2009.
ii Sub-paragraph (h) of Section 39(1) ITA has been deleted by the *Finance Act 2002* (Act 619) with effect from the year of assessment 2002.
iii Steruda Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri (2005) MSTC 4,188.
iv [1988] 2 MLJ 223
v [1988] 2 MLJ 99
vi [1894] WN 30, per Stirling J.
vii [1917] 1 KB 154, per Lord Reading CJ at page 158 and 159.
viii [1923] 39 TLR 294, per Lord Birkenhead at page 297.
ix [1948] 1 DLR 225 (Exchequer Court of Canada), per O' Connor J at page 233.
x Per Finlay J in *Ainley v Edens 19 TC 303*

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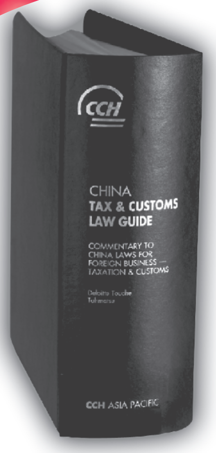

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International News

By Rachel Saw

The column only covers selected developments from countries identified by the CTIM and relates to the period 9 February 2009 to May 2009.

Brunei

Details of the Budget 2009–10

The State Legislative Council approved the fiscal Budget for 2009–10 on 16 March 2009, which generally appliesy from 1 January 2009, the highlights of which follow:

- The corporate income tax rate is reduced from 25.5% to 23.5% from the year of assessment 2010.
- A double deduction is available on contributions made by employers in respect of their employees towards the Employees' Trust Fund (*Tabung Amanah Pekerja*).
- Capital allowances (for qualifying expenditure incurred on or after 1 January 2009)

    1. The rate of initial allowance on plant and machinery is increased from 20% to 40%.
    2. Instead of claiming the initial allowance, a taxpayer may claim annual allowances on plant and machinery over a period of three years, i.e. at the rate of 33.33% per year.
    3. Plant and machinery (excluding those on hire-purchase) not exceeding BND 2,000, computers and other prescribed automation equipment qualify for a 100% write-off, subject to a maximum of BND 30,000 per year.

- Withholding tax applies on gross rental or other payments for the use of movable property derived from Brunei on or after 1 January 2009 by any person carrying on business in Brunei and where the income is not effectively connected with a permanent establishment of that person in Brunei, at the rate of 10% (previously 15%).

New building tax on commercial buildings in Bandar Seri Begawan – revenue allocation

From 1 April 2009 a commercial building tax of 12% is imposed on all commercial buildings in Bandar Seri Begawan. The tax on commercial buildings that are rented out is 12% of the annual rental value as per the tenancy agreement, whereas the tax on commercial buildings that are owned and operated for own use is 12% of the total area in square metres for 12 months, according to a rate set by the municipal authority. Tax rebates are available for buildings that have been vacant for more than 30 days.

China (People's Republic)

Tax treatment of share appreciation rights and restricted share units clarified

The Ministry of Finance (MOF) and State Administration of Taxation (SAT) jointly issued a notice (Cai Shui [2009] No. 5) on the tax treatment of share appreciation rights (SARs) and restricted stock units (RSUs):

Income derived by individuals from SARs and RSUs issued by listed companies within or outside China is subject to individual income tax. Generally, gains (i.e. the difference between the share price at the time of exercise and the option price paid) on stock options are treated as employment income. However, such gains may be calculated and taxed separately from the monthly salary.

Companies listed in China are required to register their SARs and RSUs plans with the relevant local tax authorities and to report on, and withhold, the individual income tax on income arising from such plans.

Special reduced VAT rates and simplified VAT collection clarified

The MOF and SAT jointly issued a notice (Cai Shui [2009] No. 9) clarifying the amendments of VAT (on 5 November 2008) which is effective from 1 January 2009:

- The notice lists the goods which are taxed at the reduced rates of 13%, 6% and 4%;
- Under the condition that no input tax credit will be deducted, the preferential policy on the simplified VAT collection continues to apply in certain circumstances, such as the sale of "self-used fixed assets" and second-hand goods;
- Once an ordinary taxpayer elects to be taxed as a small-scale taxpayer (the simplified collection), the election is irrevocable for three years.

Withholding tax on dividends and interest paid to qualified foreign institutional investor clarified

The AT issued a ruling (Guo Shui Han [2009] No. 49) confirming that dividends and interest paid by a resident enterprise to a qualified foreign institutional investor (QFII) are subject to 10% withholding tax unless an applicable tax treaty or tax arrangement provides otherwise. The paying resident enterprise is required to act as a withholding agent.

Implementation of treaty article on dividends

The SAT issued a ruling (Guo Shui Hu [2009] No. 81) guiding the implementation of the treaty article on dividends. It is generally assumed that the ruling applies from 1 January 2008.

In order to obtain the benefits provided under the article on dividends of a tax treaty, the taxpayer must be a resident of the contracting state and the beneficial owner of the dividend. The dividend must be defined in accordance with the Chinese domestic laws and regulations.

Shareholders who hold a substantial interest (generally, 25% or 10%) in a Chinese paying company and who, accordingly, are eligible for a lower *domestic* rate, will only enjoy the *treaty* rate for dividends if:

- the shareholder is a company;
- the interest and voting rights in the Chinese resident company meet the requirements of the relevant tax treaty; and
- the shareholder holds directly the prescribed proportion of the capital in the Chinese resident company for 12 consecutive months prior to the dividend distribution.

The ruling also states that the tax authority is authorised to make adjustments if a transaction or an arrangement's main purpose is to obtain treaty benefits, and the taxpayer should not be entitled to the treaty benefits on account of that transaction or arrangement.

The shareholder and withholding agent are required to maintain certain information such as shareholder's residence certificate, contracts, evidence of the ownership, resolution on the dividend distribution and evidence of payment, etc.

Notice relating to tax administration on withholding taxes published

The SAT issued a notice (Guo Shui Fa [2009] No. 3) setting out the tax administration and collection of withholding taxes (WHT) imposed on non–resident (NR) enterprises, which applies retroactively from 1 January 2009:

- A payer, whether an enterprise or individual, must act as a withholding agent.
- In case of a first–time contract on such payments, the payer must register with, and submit a copy of the contract to, the competent tax authority within 30 days of the contract's conclusion.
- Where both parties involved in a share transfer are NR enterprises and the transaction has taken place outside China, the Chinese enterprise of the transferred shares is to provide the information on the share transfer to the competent tax authority.
- A withholding agent is required to maintain records and deduct the WHT from the payments (calculated on an accrued basis). The tax due must be paid within seven days of filing the WHT return.
- Dividends, profits, interest, royalties and rental income paid to the NR enterprise are subject to WHT on a gross basis, whereas capital gains are subject to WHT on a net basis (i.e. the proceeds of the sale minus the original costs of acquisition).
- Where the contract stipulates that the payer bears the WHT, the amount received by the NR enterprise must be grossed up in determining the tax base.
- A NR enterprise eligible for a tax incentive must apply to the competent tax authority according to the required procedures. Before the tax incentive is approved, the withholding agent must withhold the tax without taking the incentive into account.
- If the provisions of an applicable tax treaty differ from this notice, a NR enterprise may apply the tax treaty. Tax paid can be refunded if an enterprise has applied, and is proven to be eligible, for a tax incentive or treaty benefit subsequently.
- If the withholding agent fails to withhold the tax or was not able to perform the duty of withholding, the NR enterprise has to pay the tax itself to the tax authority within seven days of the due day of the payments. The withholding agent may face penalties.
- The tax authorities are granted legal power to collect other sources of income of the NR enterprise within China if it fails or refuses to pay the withholding tax.

Decree on contracted projects and services by NRs published

The SAT issued a decree (Zong Ju Ling No.19) setting out the rules concerning the tax administration of enterprise income tax (EIT), business tax, value added tax (VAT) on contracted projects and services provided by NR enterprises and individuals. The rules apply from 1 March 2009:

Definitions

(a) A NR enterprise is defined as an enterprise incorporated under foreign laws which:
- has a permanent establishment in China although it is effectively managed outside China; or
- does not have a permanent establishment in China but derives income from China.

(b) A NR individual is defined as an individual who is not domiciled in China, or has resided less than one year in China although he is not domiciled in China.

(c) Projects refer to construction, installation, assembly, repair, decoration, exploration and other engineering operations in China. Services include processing, repair, transportation, storage, leasing, consulting, design, culture and sports, technical services, education and training, tourism, entertainment and other services.

Tax registration obligation

NR enterprises providing contracted projects or services within China are required to register with the competent tax authority within 30 days of the conclusion of contracts on projects or services.

- This also applies to the resident entities or individuals who must act as withholding agents by law. The entities or individuals who assign a project or service to a NR must submit the requisite form to the competent tax authority within 30 days of the conclusion of the related contract.
- The NR must submit the report on the project accomplishment and deregister with the tax authority within 15 days of the completion of the contracted project or services, together with the project completion certificate, inspection/acceptance certificate, etc.
- The principal (client) of the project must update the tax authority of any changes.
- Resident entities or individuals assigning the projects or services are also required to submit to the tax authority a statement of the invoices or other notes received from outside China and the copies of their payments made. The tax authorities are also required to exchange information on the contracted projects and services provided with other tax authorities and government departments.

Tax assessment and administration

(a) EIT. NR enterprises providing contracted projects or services in China are chargeable to the EIT on their income, and advance payments must be made in quarterly instalments. The final tax settlement shall be made upon completion of the project. The Notice specifies a set of documents to be included in the annual tax return.

(b) Business tax and VAT. If a NR is liable to business tax and VAT, but does not have a business establishment in China, its agent in China should be the withholding agent. If the NR does not have an agent, its Chinese principal and the service recipient must act as withholding agent.

If a NR or his legal representative fails to clear up the tax liability and late payment interest or provide guarantees, he may be prevented from leaving China by the immigration authorities.

Hong Kong

Budget 2009/10

The Budget for the financial year 2009/10 was presented on 25 February 2009 and when passed, will take effect on 1 April 2009:

- a one–off reduction of 50% of the 2008/09 final tax liability (subject to a ceiling of HKD6,000) in respect of salaries tax and tax under personal assessment;
- extension of the freeze on government fees and charges related to people's livelihood, to 31 March 2010;
- extension of the exemption for electric vehicles from First Registration Tax which is due to expire on 31 March 2009, for a further five years; and
- waiver of property rates for the first two quarters of 2009/10, subject to a ceiling of HKD 1,500 per quarter for each rateable tenement.

India

Proposed easing of Employees' Provident Fund requirements reported

It is now reported that the government is reconsidering the scope for the applicability of social security to expatriates. Reported proposals include:
- setting up a separate employees' provident fund for expatriate employees;
- providing an opt–out option to expatriates from countries such as the United States, the Netherlands and Sweden; and
- grading of salaries of expatriate employees to keep those who are higher paid out of the ambit of the social security norms.

Interim Budget for 2009/10

The iInterim Budget for 2009/10, was presented on 16 February 2009 and did not contain any proposals to amend the current direct or indirect taxation systems. Subsequently, however, changes to the indirect tax regime were announced:

- effective 24 February 2009 the service tax rate is to be reduced to 10% (from 12%);
- the general reduction in the excise duty rates by 4% (announced on 7 December 2008) is to be extended until 31 March 2009;
- the general central excise duty (CED) rate is to be reduced to 8% (from 10%);

- the CED rate on bulk cement is to be reduced to 8% (from 10%) or INR 230 per metric tonne (from INR 290 per metric tonne); and
- the customs duty exemption for the importation of *naptha* for electricity generation is to be extended beyond 31 March 2009.

Indonesia

Additional regulations (effective from 1 January 2009) implementing new Income Tax Act issued

Government Regulation No. 16/ 2009 dated 9 February 2009

- Bond interest and discounts are subject to final WHT (except where received by approved pension funds and banks established in Indonesia) as follows:

	Residents and permanent establishments	NRs
Interest on coupon -bearing bonds	15% of gross interest of gross interest	20% (or treaty rate)
Discounts on coupon- bearing bonds and zero -interest bonds	15% of the difference between the selling price / nominal value and the acquisition price	20% (or treaty rate) of the difference between the selling price / nominal value and the acquisition price

- A temporary exemption on bond interest is available to mutual funds registered with the Capital Market and Financial Institution Supervisory Board for the years 2009 and 2010. Tax of 5% applies for the years 2011 to 2013, whereas the standard rate of 15% applies from 2014 onwards.

Government Regulation No. 17/ 2009 dated 19 February 2009
Income received from futures contracts traded on an Indonesian stock exchange is subject to final withholding tax of 2.5% of the initial margin.

Government Regulation No. 18/ 2009 dated 9 February 2009
Assistance or donations, including charity and mandatory religious donations in the form of money or goods which are given to individuals and certain bodies, are exempt from tax provided there is no business, occupational or controlling relations between the parties.

Government Regulation No. 19/ 2009 dated 9 February 2009
Resident individuals who receive dividend income from Indonesia are subject to a final withholding tax of 10%.

Withholding tax exemption on financing costs

Effective 1 January 2009 (MOF Regulation No. 251/PMK.03/2008), interest and other payments for the provision of loans and other forms of financing (including *Syariah*-based financing) to certain resident business entities, are exempt from the 15% creditable withholding tax which generally applies.

The business entities which qualify for the exemption are:
- financing companies which constitute non-bank business entities and non–bank financial institutions established specifically and licensed by the MOF to provide financing services; and
- state-owned entities or regional administration–owned entities established specifically to provide financing facilities to micro, small and medium–sized businesses and cooperatives, including PT Permodalan Nasional Madani.

Reduction in amount of monthly tax instalments

From 11 February 2009, taxpayers who undergo a “change in business conditions or activities” (not defined) in 2009 can apply for a reduction in the amount of their monthly tax instalments.

- For the tax instalments due between January 2009 and June 2009, taxpayers may apply for a reduction of up to 25% of (i) the tax instalment for December 2008, or (ii) the annual tax liability for 2008.
- For the tax instalments due between July 2009 and December 2009, taxpayers may also apply for a reduction as above, if they can prove by 30 June 2009 that the amount of tax that has yet to be paid in 2009 is expected to be less than 75% of the total tax due for 2009.

Listed companies, banks, state–owned enterprises, regional administration–owned enterprises and persons who are required to file periodic financial statements are not eligible for the reduced tax instalment scheme mentioned above.

Reduction in tax on interest on cooperative savings received by individuals

Effective 1 January 2009, Government Regulation No. 15/ 2009 reduces the income tax rates on interest on savings paid by cooperatives established in Indonesia to their individual members from the current creditable tax of 15% to a final tax of 10% (where the interest exceeds IDR 240,000 a month). Interest income below this threshold is not subject to tax.

Withholding of income tax on sale of luxury goods

From 1 January 2009, pursuant to Circular SE-13/PJ/2009 and MOF Regulation No. 253/PMK.03/2008, corporate taxpayers are required to withhold 5% income tax (10% where the buyers of the goods do not hold tax registration numbers) from the sale of:

- private aircrafts worth IDR 20 billion and more;
- cruise ships, yachts and the like worth IDR 10 billion and more;
- residential properties with market values exceeding IDR 10 billion and floor spaces exceeding 500 square metres in the case of houses (including land) and 400 square metres for condominiums and apartments;
- 4-wheel vehicles carrying less than 10 passengers in the form of a sedan, jeep, sport utility vehicle, multi–purpose vehicle, mini bus and the like, where the sales price exceeds IDR 5 billion and the cylinder capacity exceeds 3,000 cc.

The tax is to be withheld by the seller of the goods and is to be remitted to the government by the 10th day of the month following the end of the seller's tax period. The tax is creditable against the annual income liability of the purchaser of the luxury goods and any excess is refunded.

Singapore

Temporary liberalisation of foreign–source income exemption details

As announced in the 2009 Budget, Singapore's foreign–source income exemption scheme is temporarily liberalised:

Current treatment
All individuals are exempt from tax on all foreign income received in Singapore, unless received through a partnership. Resident companies and partnerships are granted a tax exemption on foreign–source dividends, branch profits and income from services rendered overseas, provided that tax has been paid in a foreign jurisdiction where the highest corporate rate is at least 15%.

New treatment
A one year tax exemption is granted to all resident taxpayers on all foreign–source income accrued on or before 21 January 2009 and received in Singapore between 22 January 2009 and 21 January 2010 (both dates inclusive).

(a) Financial Reporting Standard 18 on revenue recognition for financial reporting purposes is generally followed in determining when the income accrues. Dividend income is deemed to have accrued on or before 21 January 2009 only if the dividend was paid (and not merely proposed) by the NR company on or before 21 January 2009, to a Singaporean taxpayer. As a concession, dividends paid out of profits accruing on or before 21 January 2009 by NR companies which are substantially (i.e. more than 50%) and directly owned by specified resident taxpayers on 21 January 2009 are also exempt, provided the dividends are received in Singapore during the one year exemption period, and are paid out of revenue reserves accumulated up to 21 January 2009 by their directly–owned foreign subsidiaries.
(b) Foreign–source income is deemed to be received in Singapore if the income is: (i) remitted to, transmitted or brought into Singapore, (ii) applied in or towards the satisfaction of any debt incurred in respect of a trade or business carried on in Singapore, or (iii) applied to the purchase of any movable property which is brought into Singapore. The taxpayer is deemed to have received the income at the time of the abovementioned acts.
(c) Currently, where a taxpayer has kept both foreign–source income and capital funds outside Singapore, the IRAS may accept, as an administrative concession, the taxpayer's claim that funds remitted by him to Singapore comprise solely capital funds, provided the funds can be accounted for and demonstrated as such.
(d) All expenses incurred in respect of any foreign–source income received in Singapore which qualifies for tax exemption are deductible only against that foreign–source income.

Transfer pricing rules for related party loans and services

The IRAS issued a supplementary circular, which provides guidance on the application of the arm's length principle to related party loans and services:

Related party loans
- All related domestic and cross–border loans should reflect an arm's length rate of interest.
- The current "interest restriction" method which limits the amount of interest deductible in the case of loans which are interest free or at interest rates not supported by a transfer pricing analysis will be accepted by the IRAS, with regards to: (i) related domestic loans provided that the lender is not in the business of borrowing and lending funds; and (ii) related cross–border loans for a transition period beginning from 1 January 2009 to 31 December 2010.
- The comparable uncontrolled price (CUP) method is the preferred method for determining the arm's length price; other methods can also be used provided that they are documented and justifiable.
- All relevant factors must be considered in conducting the comparability analysis including the nature and purpose of the loan, market conditions at the time the loan is granted, principal amount, duration and terms of the loan, the currency in which the loan is denominated, and securities and guarantees involved in the loan.

Related party services
- A service is considered to have been provided when the activities are performed for another party who receives, or reasonably expects to receive, the benefits from such activities.

- A benefit must have economic or commercial value such that an independent party would expect to pay to receive it or be paid for its supply; otherwise, no service is considered rendered.
- When an identified need of a related party is fulfilled by another related party, a service is considered to have been provided. Conversely, where a benefit is conferred but the related party has no need for such activity, no service is deemed provided.
- The direct charge method is preferred in charging for related–party services. Where the indirect method is used, the IRAS will accept the allocation key used as long as it is reasonable, founded on strong accounting principles and is consistently applied.
- The CUP and cost–plus methods are preferred in determining the arm's length fee for related party services. A 5% mark–up is accepted by the IRAS as being a reasonable arm's length charge for certain types of routine support services. However, if a detailed transfer pricing analysis supporting a different mark–up has been conducted for such services, such mark–ups should be adopted instead.
- Cost–pooling and the strict pass–through of costs can be charged to related parties without a mark–up, subject to certain conditions.

Vietnam

Decree on Special Consumption Tax issued

Decree No. 26/2009/ND-CP provides detailed guidance on the implementation of the Law on Special Consumption Tax (passed in November 2008). Effective from 1 April 2009, five groups of goods are exempt from the special consumption tax:

- humanitarian and non–refundable aids, and gifts
- goods transiting via a bordergate of Vietnam which are not meant for either import into / export from Vietnam
- aircrafts and cruise liners used for business purposes and for transportation of cargo, passengers and tourists
- ambulance cars, prison vans, funeral cars, vehicles designed for 24 or more passengers
- air conditioners (<90,000 BTU) which were manufactured for installation in transport vehicles
- regulations on special consumption taxes applied for alcohol and beer will take effect as from 1 January 2010

The Decree also provides details on taxpayers, special consumption tax calculation bases and tax rates, types of goods, subject–to–tax reimbursement and method of reimbursement (not yet available).

Changes to personal income tax

Circular 62/2009/TT-BTC (effective retrospectively from 1 January 2009) repeals some of the earlier provisions of Circular 84:

(a) The following previously taxable employment income is now tax exempt:
  - one–off relocation allowance for expatriates arriving in Vietnam (amount per labour contract);
  - school fees for children of expatriate employees;
  - air fare for one round–trip home leave for employee only;
  - housing allowance has reverted to the pre–2009 cap of 15% of total taxable income;
  - pool / company cars not allocated to a specific individual;
  - corporate / group club or recreation memberships for "collective use";
  - training expenses for knowledge and improvement of skills;
  - meal allowances in accordance with limits set by Ministry of Labour, War Invalids and Social Welfare; and
  - per diem (regulated amounts).

(b) Documents are no longer required to be submitted to support claims for dependant relief

(c) The withholding rate of 20% for payments of non–employment income (i.e. sales commission, wages, salary, etc) to individuals above VND 500,000 is reduced to 10%

(d) Dividends received in the form of shares are taxed upon transfer of the shares and not receipt, at which time:
  - the "dividend" is taxed as income from capital investment (at par value); and
  - the difference between the transfer price and par value is taxed as income from securities transfer.

Malaysia —— treaty developments

- The income tax treaty and between Kazakhstan and Malaysia signed on 26 June 2006, entered into force on 22 February 2007. The treaty generally applies in Kazakhstan from 1 January 2008 for withholding taxes and 1 January 2009 for other taxes. In Malaysia, it applies from 1 January 2009 for petroleum income tax and from 1 January 2008 for other taxes.

- The income tax treaty between Malaysia and Qatar, signed on 3 July 2008, entered into force on 28 January 2009. The treaty generally applies in Malaysia from 1 January 2010 for income/withholding taxes and 1 January 2011 for petroleum income tax. In Qatar, it applies from 1 January 2010. 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

Business Deductions

By Siva Subramaniam Nair

This article, the first in a series, examines the general principles of deductibility based on the Income Tax Act 1967 and relevant case law.

Having looked at business income in detail, let us now focus on the types of expenditure that would rank for a deduction in ascertaining the adjusted income from a business source.

The general rule for deductibility of an expense (not only for business but also for others types of income) is enshrined in the main body of s 33 of the *Income Tax Act 1967* (as amended) ("the Act") which reads:

> ***Subject to this Act, the adjusted income of a person from a source for the basis period for a year of assessment shall be an amount ascertained by deducting from the gross income of that person from that source for that period all outgoings and expenses wholly and exclusively incurred during that period by that person in the production of gross income from that source,...***

Since this is such an important section in the Act, let's analyse each facet of that section.

1. **"Subject to this Act, the adjusted income of a person from a source..."**

   As we have seen from earlier articles, expenses are deducted from the gross income in arriving at the adjusted income. Alternatively if we are required to commence the tax computation with the profit before tax figure, adjustments (involving non-taxable income and non-allowable expenditure) have to be made to ascertain the adjusted income.

   This Act means the Income Tax Act 1967 (as amended); therefore, the expenses are deductible only if they are incurred in the production of income chargeable to Malaysian tax. Expenses applicable to overseas-sourced income are not deductible although foreign income received in Malaysia is within the scope of charge and, consequently, taxable in Malaysia under s 3 of the Act. An exception to this would be resident companies involved in the business of insurance, sea and air transport, and banking who are on a worldwide scope of charge.

   In line with this, foreign losses are also not deductible against Malaysian income; but the only exceptions are resident companies involved in the business of insurance, and sea and air transport because those in the banking business are only on a worldwide scope of charge up to statutory income whereas brought forward and current year losses are deducted subsequent to this stage.

Unlike accounting, where normally all income sources are merely classified as trading and other income and all expenses are grouped together in determining the profit before tax, in taxation, each source of income (including between different sources of business income) have to be classified separately and expenses attributable to each particular source have to be identified and cannot be allowed against another source of income.

This is illustrated in the following diagram.

Gross	Business 1	Business 2	Non-business
Income	xxx	xxx	xxx
Less: Allowable expenses	(**)	(**)	(**)
Adjusted Income	xxx	xxx	xxx
Less: Capital allowances	(**)	(**)	*not applicable* Non- business
Statutory Income	xxx	xxx	xxx

Example 1
Prism College S/B has three businesses, education, photocopying and a restaurant business with gross income of RM1.35 million, 0.45 million and 0.9 million respectively. All three businesses come under the purview of the managing director of the company whose annual salary is RM180, 000. Therefore, the salary of the managing director has to be apportioned to the three businesses on an equitable basis which is normally gross income as shown below.

Business	**Education**	**Photocoying**	**Restaurant**
Gross income (RM'000)	1,350	450	900
Less MD's salary"			
1,350/2700x180,000	(90)		
450/2700x180,000		(30)	
900/2700x180,000			(60)

2. "... (O)utgoings and expenses..."

"Expenses" general denote a cash outlay or payment of money for the procurement of an asset or the settlement of a liability to pay. It includes disbursements laid out voluntarily or willingly. However, "outgoings" has a much wider meaning and includes items such as:

(a) theft or defalcation of money and stocks by employees — of course we don't pay someone to steal our money but in an business organisation, at times it is necessary to delegate duties to staff including those that involve the management of cash and inventory
(b) the provision of free samples — a necessary incurrence for marketing and promotional activities
(c) bad debts — the conduct of business on credit terms is not an unusual feature of trading; however, one unfortunate consequence of this is the possibility of debts becoming bad.

Other revenue legislations use terminology which is not significantly different such as "losses and outgoings" in Australia, "any disbursements and expenses" in the UK, "expenditure or loss of any kind" in New Zealand and "Any expenditure …" in India.

3. "...(W)holly..."

This refers to the amount of money spent i.e. the whole amount of the money spent must be for the purposes of producing income..

In ***Ransom v Higgs [1974] 3 All ER 949*** Lord Reid said:

"I would agree that if a trader is actuated by none but commercial motives the Revenue cannot merely say that he has paid too much. He may have been foolish or he may have had what could fairly be regarded as a commercial reason for paying too much. But if it is proved that some non-commercial reason caused the trader to pay more than he otherwise would have done, then it seems to me quite clear that the payment can no longer be held to have been wholly and exclusively expended for the purposes of the trade. No authority is needed for so obvious a proposition"

"Wholly" also deals with the principle of remoteness i.e. if remotely connected with the achievement of the purported objective, the test of being "wholly" incurred is not fulfilled.

In ***Strong & Co. v Woodfield [1906] AC 448 All ER 949*** part of the taxpayers' hotel had collapsed and caused injury to a guest. The taxpayers paid compensation to the guest, which they wanted to claim as a deduction. The House of Lords held that this loss was not connected with, or arising out, of the trade (which was the provision of rooms and food) and so disallowed the deduction.

Lord Loreburn said:
"…it does not follow that if a loss in any sense is connected with a trade it must always be allowed as a deduction; for it may be only remotely connected with the trade or it may be connected with something else quite as much or even more than with the trade. I think only such losses can be deducted as are connected with it in the sense that they are really incidental to the trade itself."

4 ."...(E)xclusively..."

This relates to the intention for incurring the expenditure i.e. the expenditure must have been incurred exclusively for business purposes. This leads to the "dual purpose test", i.e. if there is a non-business reason for incurring the expenditure, it cannot be said to be exclusively incurred for the purpose of business. Numerous cases have deliberated on the interpretation of this word as it is used in the tax legislation; these are discussed below.

(a) Mallalieu v Drummond [1983] 2 All ER 1095

Facts of the case
Ms Mallalieu, a practicing lawyer, spent a huge amount of money on clothes for court wear in compliance with the Bar Council's guidelines on dress code. She claimed a deduction against her professional income in respect of replacement, laundering and cleaning of the clothes.

Court decision
The House of Lords, in rejecting her claim, held that "…the object of the taxpayer in making the expenditure must be distinguished from the effect of the expenditure. Expenditure may be made exclusively to serve the purposes of the business, but it may have a private advantage."

Although in her conscious mind, she purchased the clothes to comply with her profession's dress code BUT at the same time it also fulfilled the object of being clothed — an essential requirement for any human being when in public!

(b) Caillebotte v Quinn [1975] 50 TC 222

Facts of the case
A self-employed carpenter who usually spends 10p when at home had to spend 40p while away on business and attempted to claim a deduction for the difference.

Court decision
It was held to be not deductible since the expenditure incurred on food is not incurred solely to carry on his trade but also for him to survive.

(c) Murgatroyd v Evans-Jackson [1967] 1 All ER 881

Facts of the case
The taxpayer, while being hospitalised after an accident, was able to conduct business meetings with clients because of the facilities available at that particular nursing home. Recognising the duality of purpose of the whole expenditure, the taxpayer claimed 60% of the nursing home costs as a deduction in computing his profits.

Court decision
It was held to be not deductible since implicit in his claim was the admission that the expense involved a dual purpose. However, the telephone charges incurred in respect of his business were allowed as being wholly and exclusively incurred.

(d) Norman v Golder 26 TC 293

Facts of the case
A shorthand writer claimed a deduction for medical expenses incurred because he argued that the illness was a direct result of unfavourable working conditions.

Court decision
The claim was held to be not deductible as it was not solely for business purposes.

(e) Prince v Mapp [1967] 1 All ER 881

Facts of the case
An engineering draughtsman, who played a guitar for pleasure and payment, tried to claim a deduction for the cost of an operation on his finger which was damaged in an accident.

Court decision
It was held to be not wholly and exclusively incurred for the purposes of his profession and consequently, not deductible.

However, in practice, the Revenue authorities generally do not completely disallow an expenditure which has both a business and private purpose but instead allow a deduction for the business portion. This is especially in the case of sole proprietors where assets such as a car, computer, telephone etc is usually used for both business and personal purposes and therefore, an equitable apportionment has to be made to ascertain the quantum of expenditure deductible against business income. An apportionment is also necessary when a part of the expenditure is deductible under business income and another part under non-business income; for example interest on loans which are used for the business but also to purchase investments which generate other income.

In the next article we shall discuss the other facets of this important section. 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, (Latest Edition), Arah Pendidikan Sdn Bhd.
- Thornton, Richard: Thornton's Malaysian Tax Commentaries, (Latest Edition), Sweet & Maxwell, Asia.
- Thornton, Richard: Richard Thornton: 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 Subramaniam 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*

Notice Board

Compound on errors in STD calculation

As a concession to employers using the new STD rules for the year 2009 only, the IRB has agreed not to impose a compound on errors in the STD calculation made unintentionally or with reasonable excuse. The IRB has requested members of the professional bodies to submit examples of such errors to enable guidelines to be drawn up, as well as instances where the penalty was considered to be unfairly imposed for the IRB's consideration.

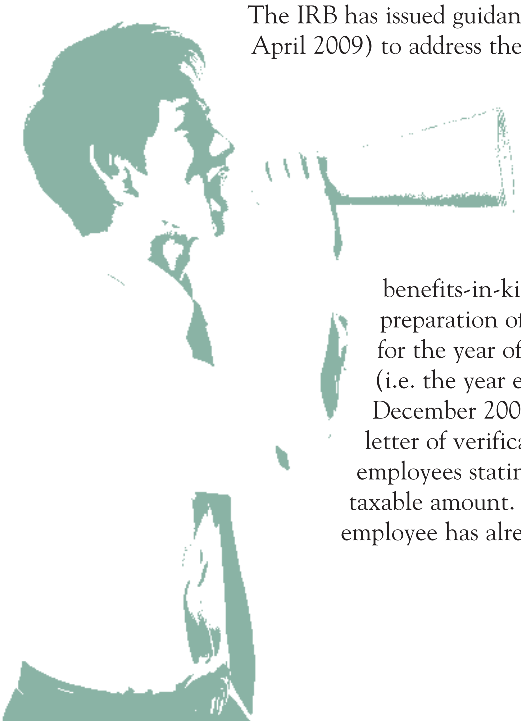
Transfer pricing and thin capitalisation rules

In relation to comments submitted to the Ministry of Finance (MOF) on the draft Transfer Pricing Rules 2009, the MOF's Tax Analysis Division has informed the CTIM that separate rules will be issued on thin capitalisation, instead of having these incorporated into the transfer pricing rules (as was done with the draft rules). The effective date of the application of thin capitalisation has been deferred to a date that will be subsequently notified.

Guidance on exempt perquisites and benefits-in-kind

The CTIM has been in discussions with the IRB in relation to the application of the Second Addendum to Public Ruling No. 1/2006 — *Perquisites from Employment* and the Third Addendum to Public Ruling No. 2/2004 — *Benefits-In-Kind*. The CTIM is concerned with the practical issues involved in complying with the changes, including the removal of the prescribed value for petrol, stating its views that the retrospective effect of the public ruling is burdensome and the IRB should have a mechanism to favourably consider cases where tax returns have been filed with the application of the prescribed values. In addition, the CTIM has raised the issue of the difficulty in determining a breakdown for the value of petrol used for travel from home/office and back and for official travel.

The IRB has issued guidance (dated 28 April 2009) to address these concerns. It states that employers who do not accurately account for exempt perquisites and benefits-in-kind during the preparation of the Form EA for the year of assessment 2008 (i.e. the year ended 31 December 2008) should issue a letter of verification to their employees stating the correct taxable amount. Where the employee has already submitted his/her tax return for the year of assessment 2008, the IRB should be informed in writing of the correct taxable value together with a letter of verification from the employer.



The CTIM is pursuing this matter further with the IRB as it is of the view that the guidance provided falls short of what it had been urging the IRB to consider.

Form C and Form R for the year of assessment 2009

Sample Forms C and R for the year of assessment 2009 are available on the IRB's website. It is to be noted that these forms are only for reference. With effect from the year of assessment 2009, PDFs (portable document formats) of the Forms C and R cannot be used for filing purposes.

Establishment of *Joint Tax Working Group on Financial Reporting Standards* (JTWG-FRS)

The Joint Tax Working Group on Financial Reporting Standards (JTWG-FRS) has been established by the following parties to consider the various tax issues arising from the adoption of FRS in Malaysia:

- Technical and Public Practice Committee of the Chartered Tax Institute of Malaysia (CTIM)
- Taxation Committee of the Malaysian Institute of Accountants (MIA)
- Tax Practice Committee of the Malaysian Institute of Certified Public Accountants (MICPA).

The terms of reference of the JTWG-FRS are to:

- analyse changes brought about by FRS which have tax implications
- highlight and provide comments to members on possible tax implications related to FRS, and
- propose appropriate tax treatments in respect of FRS to the relevant tax authorities.

The working group will initially focus on the following eight FRS, with the other FRS to be reviewed progressively:

- FRS 2 Share-based Payment
- FRS 5 Non-current Assets Held for Sale and Discontinued Operations
- FRS 102 Inventories
- FRS 116 Property, Plant and Equipment
- FRS 117 Leases
- FRS 121 The Effects of Changes in Foreign Exchange Rates
- FRS 139 Financial Instruments: Recognition and Measurement
- FRS 140 Investment Property

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