



CHARTERED TAX INSTITUTE OF MALAYSIA (225750 T)
(Institut Percukaian Malaysia)

PROFESSIONAL EXAMINATIONS

FINAL LEVEL

REVENUE LAW

DECEMBER 2019

Student
Registration No.

Date

Desk No.

Examination Centre

Time allowed: 3 hours

INSTRUCTIONS TO CANDIDATES

1. You may answer this paper **EITHER** in English **OR** in Bahasa Malaysia. Only **ONE** language is to be used.
2. This paper consists of **SIX** questions. **Candidates are ONLY REQUIRED TO ANSWER FIVE (5) QUESTIONS.**
3. The Income Tax Act 1967 (as amended) is referred to as ITA.
4. Each answer should begin on a separate answer booklet.
5. Answers should be written in either black or blue ink.
6. No question paper or answer booklet is to be removed from the examination hall.

DO NOT TURN OVER THIS PAGE UNTIL INSTRUCTED BY THE INVIGILATOR

Question 1

- (a) Under section 3 of the ITA, '*a tax to be known as income tax shall be charged for each year of assessment upon the income of any person....*'

Required:

Discuss briefly what you understand by the word 'income' as used in the ITA distinguishing between revenue and capital and support your discussion with reference to the case of *CIT, Bengal v Shaw Wallace & Co* [(1932) 6 ITC 178].

(10 marks)

- (b) MT Overland Transport Sdn Bhd ('the company') is a locally incorporated company that operates a passenger bus transport business between Kuala Lumpur and Bangkok. The company has special permission from the Thai transport authorities to operate inside Thailand. Passengers who embark on the company's bus in Bangkok to Kuala Lumpur would purchase their tickets in Bangkok from a Thai agent representing the company there, using Thai currency. For the year ended 31 December 2018 the company's gross income from sale of tickets sold in Kuala Lumpur was RM98,000 while sale of tickets in Bangkok was equivalent to RM105,000.

Required:

With reference to section 3 of the ITA and relevant case law, discuss the taxability of the gross income derived from the sale of the tickets in Kuala Lumpur and Bangkok in the context of the law pertaining to '*accrued, derived or received in Malaysia from outside Malaysia*'.

(10 marks)

[Total: 20 marks]

Question 2

- (a) '*In order to decide whether a person carried on a business on his own account it is necessary to consider many different aspects of that person's work activity.*'

Mummery J.

In the context of the above dicta, and with reference to the ITA and relevant case laws, discuss briefly the following matters:

Required:

- (i) **Why is it important to make a distinction between income from a business source and that from an employment source?**

(2 marks)

- (ii) **In a litigation where one needs to determine whether the income derived is from an employment source or a business source, how do the courts go about reviewing the different aspects of the case on which a judgement has to be given?**

(3 marks)

- (iii) **How do the judges look at the issues generally faced by a court in comparing the decision in one case with the decision in a similar case, to arrive at a decision in the case in question?**

(3 marks)

- (b) Mr Menon ('Menon') is a qualified technician dealing with electrical works connected with air conditioners, television and water heaters ('electrical items'). He engages regularly with twelve different companies and some others, who will call on him to settle or to do work on matters connected with those electrical items for their customers. Some of these works are single day assignments or in some instances the job may take between two to three days to complete or fix. He sometimes refuses an assignment offered for various reasons (e.g. it is clashing with another accepted assignment).

The various companies pay Menon at the end of the month for the work done in the course of the preceding month based on bills he invoiced them.

For the year ended 31 December 2018 Menon received a total of RM185,000 for work done. He had incurred various expenses such as engaging odd job workers to assist him, travelling, telephone, repair and maintenance of tools and equipment used in the course of his work. He has claimed these expenses as deductions against his earnings.

Required:

Discuss whether Mr Menon was in employment, or was a self-employed person carrying on a business.

Note:

Support the answer with reference to the relevant provisions of the ITA and related case laws.

(9 marks)

- (c) Mr John Adams ('John') is a British national, and a human resource management expert dealing with employment litigation cases. He was offered an employment by a local management company, AB Sdn Bhd ('the company') on 1 September 2019 vide an offer letter. He arrived in Kuala Lumpur on 5 September 2019, signed and accepted on the offer and commenced work immediately. The company carries on the business of representing its clients in employment litigation cases. Due to a misunderstanding, he was not paid for 55 days into his employment. John was unhappy and wanted to resign. He also indicated in no uncertain terms that he may sue the company.

To avoid any bad publicity, the company agreed to compensate John and a settlement agreement was worked out. Under this settlement agreement dated 15 October 2019, the company will pay him RM800,000. A sum of RM250,000 was withheld from this sum under section 83(5). John had left for England on 15 October 2019.

Required:

With reference to the ITA and relevant case law, discuss whether the sum of RM800,000 received by Mr John Adams is exempted from income tax.

(3 marks)

[Total: 20 marks]

Question 3

Mr Alan carries on a poultry business and is helped in the business by his three grown up sons who are of legal age. The poultry business originally operated from a piece of land he owned in Ampang but it did poorly due to several factors including the location. Mr Alan then sold off his farm and the land in Ampang. He relocated to Kepong and continued operating his poultry business.

Mr Alan and his three sons executed a lease agreement as joint tenants of the land with the land proprietor in Kepong. Apart from the joint lease document, Mr Alan did not prepare any partnership agreement with his sons to carry on the poultry business either in Ampang or in Kepong.

The poultry operation in Kepong was all funded by Mr Alan including the acquisition of plant and machinery, tools, chicken feed and other related expenses for the farm. Mr Alan maintained a local bank account in his own name and all outgoings and incomings are accounted for by him from this account but otherwise there was no proper records to verify the transactions.

The three sons worked diligently on the farm to ensure its success this time, but did not involve themselves in the management of the farm. They were paid a fair sum for their efforts in addition to free food and lodging, with extra pocket money on festive occasions. However, their personal and business relationship soured in early 2017 and the three sons left the farm in late December 2017.

Sometime in the middle of 2018, Mr Alan's business was audited by the Malaysian Inland Revenue Board for the years of assessment 2015 to 2017. Based on the tax audit, the Inland Revenue Board raised additional assessments on Mr Alan as sole proprietor for the said years of assessment.

Mr Alan objected to the said assessments claiming that the poultry business was a partnership consisting of him and his three sons and therefore the profits must be divided equally between the four partners. The Inland Revenue Board dismissed his objection as being without basis.

Required:

- (a) **Based on the information provided with regards to the poultry business of Mr Alan, identify the salient facts in the scenario that are relevant for income tax purposes.**
(5 marks)
- (b) **Identify the tax issue or issues in this scenario with reference to the ITA.**
(3 marks)
- (c) **Discuss whether the claim by Mr Alan that the poultry business carried on as a partnership has any basis in law.**
(6 marks)
- (d) **Discuss the legal concept of a partnership and whether the stand taken by the Inland Revenue Board that there was no partnership, has any basis in law.**
(6 marks)

Note:

Support the answer with reference to the relevant provisions of the ITA and related case laws.

[Total: 20 marks]

Question 4

The International Trading Venture group of companies carry on various business activities including trading in edible goods, manufacturing and packing dry foodstuff for re-export. Malaysia Capital Venture (M) Sdn Bhd [MCV] is the ultimate holding company. It commenced business in 2014 and closes the accounts to 31 December each year. MCV has investments in two subsidiaries (one of which is overseas), financed by a bank loan on which interest expense amounts to RM30,000 per annum. These two subsidiaries commenced business in 2015. Between 60% and 70% of MCV's gross income is derived from its trading operations.

MCV provides treasury services, including sourcing funds, arranging loans and managing interest costs and foreign exchange rate fluctuations for companies in the group. The treasury activities are intercompany transactions to facilitate cash flow in the group and do not come under the purview of the Malaysian financial regulatory authorities.

MCV had extended a loan of RM5 million on 1 January 2017 to its Malaysian resident subsidiary company, Frozen Food (M) Sdn Bhd for its expansion purposes. The loan was for a period of three years with interest charged at the current market rate. Under the lending arrangement, the loan was due with accumulated interest on 31 December 2019.

Besides trading and treasury activities, MCV derives income from the following:

- Interest from fixed deposit

It has placed a deposit with a bank in Chennai, India, to facilitate the financing of the supply of dry foodstuff and spices from suppliers there. This placing of the deposit is one of the conditions for the supply of goods by the Indian suppliers. The fixed deposit earns interest and the amount would be added on to the deposit.

- Rent from vacant land

It has a piece of vacant land that is pending construction of a multi-storey building. Meanwhile it is rented out to an unrelated third party at a concessionary rental rate under terms that include the payment of the rent upfront under a 3-year lease agreement. The rental was received on 1 January 2019. The tenant uses it as an open car park and storage facility and provides its own security and maintenance.

- Rent from office building

A five-storey office building it owns was rented out since January 2017 to a foreign company which pays rent annually at the beginning of the year under a 3-year tenancy agreement. The agreement requires that MCV provide comprehensive maintenance and support services for the whole building (cleaning, security, maintenance of lighting and open spaces including the car park) for the period of the lease. MCV engaged a third party to provide these services.

- Dividend from subsidiary company

During the year MCV received a dividend from the Malaysian subsidiary it had invested in.

Required:

Discuss the tax treatment on the following income with respect to Malaysia Capital Venture (M) Sdn Bhd for the year of assessment 2019:

- (i) The interest income from the loan extended to Frozen Food (M) Sdn Bhd;** (4 marks)
- (ii) The interest income from the fixed deposit in the bank in Chennai, India;** (4 marks)
- (iii) The rental income from the vacant land;** (4 marks)
- (iv) The rental income from the five-storey office building; and** (4 marks)
- (v) The dividend income from the Malaysian subsidiary.** (4 marks)

Note:

You must make reference to the applicable provisions of the ITA, public rulings issued by the Inland Revenue Board and case laws where relevant, in your discussion of the tax treatment.

[Total: 20 marks]

Question 5

- (a) With reference to the ITA, explain briefly the meaning of ‘control’, in relation to a company and a partnership, in the context of disposals of certain assets in relation to which capital allowances has been previously made.**

Note:

You are NOT required to quote any case law for this part of the question.

(2 marks)

- (b) Sable Sdn Bhd (“the Company”) is in the business of growing coffee beans. In the year 2017, the Company transferred its coffee plantation in Sarawak to its wholly owned subsidiary (“the Subsidiary) and ceased its operations in Malaysia. The Company claimed agriculture allowance and capital allowance on qualifying assets used in the business before the transfer, and the Subsidiary is a non-resident that does not carry on business in Malaysia. Subsequently, the Subsidiary leased the plantation grounds to a third party.**

Required:

Discuss whether the provisions relating to disposals subject to control under the ITA would apply to the Company’s transfer of the coffee plantation to its subsidiary.

Note:

Support the answer with reference to the relevant provisions of the ITA and related case laws.

(4 marks)

- (c) Island Sdn Bhd (“the Company”) is in the business of growing, processing and retailing coffee beans. In the year 2017, the Company incurred capital expenditure on the construction of a building complex and other construction expenditures as in (i) and (ii) below.

Required:

Discuss briefly whether the expenditures incurred by the Company below would qualify for industrial building allowance.

- (i) **RM 200,000.00 on Building A which was to be used for the cleaning, servicing and repairing of the Company’s coffee grinding and roasting machines.**

(4 marks)

- (ii) **RM 300,000.00 on Building B where the coffee is cleaned and sorted. Here, sand, twigs, leaves and miscellaneous debris are removed from the coffee beans before being packed into bags.**

Note:

Support the answer with reference to the relevant provisions of the ITA and related case laws.

(4 marks)

- (d) Cherry Sdn Bhd (“the Company”) is in the business of manufacturing textiles and fabrics since 1992. In 2017 the Company decided to expand its business by constructing a new factory next to its existing factory. The taxpayer incurred construction expenditures totaling RM650,000 [RM400,000 + RM250,000] as in (i) and (ii) below.

Required:

Discuss briefly whether the expenditures incurred by the Company below would qualify for reinvestment allowance under Schedule 7A.

- (i) **RM 400,000.00 on the production area of the new factory which resulted in an increase in the production capacity of the Company;**

(3 marks)

- (ii) **RM 250,000.00 on the rest of the building consisting of a lobby area, meeting rooms, office space and staff lounge. Would the answer differ in the claim for reinvestment allowance on such expenditure had been made in 2011?**

(3 marks)

Note:

Support the answer with reference to the relevant provisions of the ITA and related case laws.

[Total: 20 marks]

Question 6

- (a) In 2018, the Inland Revenue Board ("IRB") conducted an audit on PSG Sdn Bhd ("PSG") for the years of assessment 2015 and 2016. Pursuant to the audit, the IRB found that PSG had claimed deductions for expenses in the year of assessment 2015 which were not wholly and exclusively incurred in the production of gross income. Accordingly, the IRB made an additional assessment in respect of PSG in the additional amount of tax of RM 300,000 for the year of assessment 2015, and a notice of additional assessment was duly served on PSG on 30 September 2018 ("Additional Tax").

PSG does *not* agree with the assessment as it believes that it should be deductible and therefore does not intend to pay the Additional Tax. PSG intends to appeal against the notice of additional assessment.

Required:

- (i) **Advise PSG on the payment of the Additional Tax and the consequences of failing to pay the Additional Tax within the prescribed time period.**

(2 marks)

Mr Charles is a director of PSG and owns 50% of the ordinary share capital of PSG. He often travels overseas and is planning to travel to Hawaii for a short holiday soon but is concerned about PSG not having paid the Additional Tax.

Required:

- (ii) **With reference to case law, advise Mr Charles on the possible actions that the IRB may take against him.**

(7 marks)

PSG had failed to pay the Additional Tax within the prescribed time period. Accordingly, the IRB has brought an action against PSG to recover the Additional Tax.

Required:

- (iii) **With reference to case law, advise PSG on how it can plead against the IRB's recovery action.**

(2 marks)

- (b) The Photobox group of companies is in the business of selling photo editing software. One of the companies in the group is Photobox Pte Ltd, a Singapore tax resident company incorporated in Singapore which does not have a permanent establishment in Malaysia. Another company in the group is Photobox Malaysia Sdn Bhd, a Malaysian tax resident company incorporated in Malaysia.

Photobox Pte Ltd is engaged in developing the Photobox photo editing software ("**Photobox Software**") and holds the rights to distribute the Photobox Software.

Photobox Pte Ltd is proposing to enter into a software distribution agreement with Photobox Malaysia Sdn Bhd ("**Distribution Agreement**"). Pursuant to the Distribution Agreement, Photobox Malaysia Sdn Bhd will be allowed to distribute the Photobox Software in the territory of Malaysia. The Distribution Agreement provides that Photobox Malaysia Sdn Bhd will not be granted any proprietary right in the Photobox Software.

In consideration, Photobox Malaysia Sdn Bhd will pay Photobox Pte Ltd a distribution fee.

Required:

With reference to the ITA, the Malaysia-Singapore Double Tax Agreement and case law authorities, discuss whether the distribution fee may be treated as 'royalty' and be liable for withholding tax in Malaysia.

Note:

Extract of the Malaysia-Singapore DTA is attached.

(9 marks)

DOUBLE TAXATION AGREEMENT (MALAYSIA – SINGAPORE)

Article 7

BUSINESS PROFITS

1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only on so much thereof as is attributable to that permanent establishment.

2. Subject to the provisions of paragraph 3, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment.

3. In determining the profits of a permanent establishment, there shall be allowed as deductions expenses including executive and general administrative expenses, which would be deductible if the permanent establishment were an independent enterprise, insofar as they are reasonably allocable to the permanent establishment, whether incurred in the State in which the permanent establishment is situated or elsewhere.

4. If the information available to the competent authority is inadequate to determine the profits to be attributed to the permanent establishment of an enterprise, nothing in this Article shall affect the application of any law of that State relating to the determination of the tax liability of a person by the exercise of a discretion or the making of an estimate by the

competent authority, provided that the law shall be applied, so far as the information available to the competent authority permits, in accordance with the principles of this Article.

5. No profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.

6. For the purposes of the preceding paragraphs, the profits to be attributed to the permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

7. Where profits include items of income which are dealt with separately in other Articles of this Agreement, then the provisions of those Articles shall not be affected by the provisions of this Article.

Article 12

ROYALTIES

1. Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the beneficial owner of the royalties is a resident of the other Contracting State, the tax so charged shall not exceed 8 per cent of the gross amount of the royalties.

3. The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work (including cinematograph films, and films or tapes for radio or television broadcasting), any patent, trade mark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment, or for information (know-how) concerning industrial, commercial or scientific experience.

4. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the royalties, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties arise, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the right or property in respect of which the royalties are paid is effectively connected with such permanent establishment or fixed base. In such case, the provisions of Article 7 or Article 14, as the case may be, shall apply.

5. Royalties shall be deemed to arise in a Contracting State when the payer is a resident of that State. Where, however, the person paying such royalties, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base in connection with which the obligation to pay the royalties was incurred, and such royalties are borne by such permanent establishment or fixed base, then such be deemed to arise in the State in which the permanent establishment or fixed base is situated.

6. Where, by reason of a special relationship between the payer and the beneficial owner both of them and some other person, the amount of the royalties paid, having regard to the use, right or information for which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such a case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Agreement.

Article 14

INDEPENDENT PERSONAL SERVICES

1. Subject to the provisions of Article 13, income derived by an individual who is a resident of a Contracting State in respect of professional services or other activities of an independent character shall be taxable only in that State unless he has a fixed base regularly available to him in the other Contracting State for the purpose of performing his activities. If he has such a fixed base, the income may be taxed in the other State but only so much of it as is attributable to that fixed base.

2. The term "professional services" includes especially independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants.

[Total: 20 marks]

(END OF QUESTION PAPER)