KETUA PEGAWAI EKSEKUTIF/KETUA PENGARAH HASIL DALAM NEGERI
(CHIEF EXECUTIVE OFFICER/DIRECTOR GENERAL OF INLAND REVENUE)
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Tarikh : 24 Oktober 2013

Pengarah Eksekutif
Chartered Tax Institute Of Malaysia (CTIM)
Unit B-13-2, Block B, 13th Floor
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Tuan,

TECHNICAL DIALOGUE

Dengan hormatnya saya merujuk kepada surat tuan bertarikh 21 Ogos 2013 dan beberapa siri emel antara Encik Lim Kok Seng (CTIM) dengan pegawai Jabatan Dasar Percukaian, Lembaga Hasil Dalam Negeri Malaysia (LHDNM) berkenaan perkara di atas.

2. Memandangkan kekangan masa yang dihadapi oleh pegawai-pegawai LHDNM kerana terlibat dengan penggubalan Rang Undang-Undang Bajet 2014, tarikh perbincangan yang dicadangkan oleh CTIM tidak dapat dipenuhi oleh LHDNM. Walau bagaimanapun, maklum balas terhadap isu-isu yang dibangkitkan oleh CTIM diberi secara bertulis sepertimana yang dilampirkan bersama-sama surat ini.

3. Sekiranya pihak CTIM masih memerlukan penjelasan lanjut bagi isu-isu tertentu, LHDNM bersedia untuk memberi maklum balas semasa Dialog Teknikal Bajet 2014 atau pun mengadakan dialog secara berasingan.

Sekian, terima kasih.

"BERKHIDMAT UNTUK NEGARA"
"BERSAMA MEMBANGUN NEGARA"

(ABD. AZIZ BIN HASHIM)
Timbalan Ketua Pengarah (Dasar)
b.p. Ketua Pegawai Eksekutif/Ketua Pengarah Hasil Dalam Negeri
Lembaga Hasil Dalam Negeri Malaysia
umi/tech dialogue

1. (a) **Prohibition for deduction of an expense where withholding tax has not been paid**

Sections 39(1)(f), (i) and (j) of the ITA prohibit a deduction for an expense which is subject to withholding tax under Sections 109, 107A and 109B/109F respectively, where the tax has not been deducted in accordance with the said sections. These sections require tax to be deducted within one month of making or crediting the payments to the non-residents.

The proviso to the above sections was amended by Finance Act 2011 as follows:-

"Provided that–

(i) …; and

(ii) where such tax is deducted or such amount is paid after the due date for the furnishing of a return for a year of assessment that relates to such payment, the tax or amount so paid shall not prejudice the imposition of penalty under subsection 113(2) if a deduction on such payment is made in such return or is claimed in the information given to the Director General in arriving at the adjusted income of the payer;"

A taxpayer who has incurred an expense which is subject to withholding tax but has not paid nor credited the non-resident payee has technically not breached the provisions of Sections 109, 107A, 109B and 109F. Under such circumstances, sections 39(1)(f)(i) and (j) should not apply.

However, the IRB has indicated in the Technical dialogue on 8 April 2011 that in such a scenario, proviso (ii) to sections 39(1)(f), (i) and (j) would still apply and the penalty under Section 113(2) would be potentially applicable if a deduction for the expense is claimed and WHT is not paid. The IRB's application of the above sections is not consistent with the law and Public Ruling 4/2005.

Request

The IRB to reconsider its treatment.

Response

1(a)	**IRB maintains the stand as indicated in the Technical dialogue on 8.4.2011. Public Ruling 4/2005 will be amended to explain the proviso to subsections 39(1)(f), (i), (j) as introduced in Finance Act 2011.**

(b) **Effective Date**

Based on section 3(4) of the Finance Act 2011, the above amendments "have effect from 1 January 2011 for the year of assessment 2011 and subsequent years of assessment".

There has been some confusion as to whether an income tax return for a year of assessment ("YA") prior to YA 2011 which was furnished to IRB after 1 January 2011, is subject to the above amendments made pursuant to Finance Act 2011.

Example

Company X closes its accounts annually on 31 September. The company only submitted its tax return for YA 2009 on 1 March 2011 instead of the due date of 30 April 2010.

The company made a claim for deduction of technical fees paid to a non-resident company. However the company only deducted and remitted the withholding tax on the technical fees to the IRB on 28 February 2011.

Request

The IRB to confirm that Section 39(1)(j) should not apply to Company X, since the tax return is in respect of a YA that is prior to YA 2011 even though its submission is on or after 1 January 2011.

Response

1(b)	**Yes, IRB confirmed.**

(c) **Non-prohibition for deduction under Section 39(3)**

Section 39(3) provides that notwithstanding the fact that withholding tax has not been paid, the relevant expense should not be added back where the taxpayer "is exempt under paragraph 127(3) (b) or subsection 127(3A) or the Promotion of Investments Act, 1986, in respect of all income of that person from all sources not being exemption on income equal to capital expenditure incurred.

Request

It is extremely rare that the income of a person from ALL sources would be exempt. We wish to seek clarification if this is the intended application of this section.

Response

1(c)	**Subsection 39(3) is to be applied as follows:** **(i) For a payer who enjoys full exemption from all sources of income for a basis period for a YA under the PIA 1986, paragraph 127(3)(b) or subsection 127(3A) of the ITA 1967 and fails to remit withholding tax on the expenditure incurred and payable to a non-resident in respect of payments under section 109, 107A, 109B or 109F of the ITA 1967, the expenditure incurred and payable to the non-resident will not be added back in the tax computation.** **(ii) For a payer who enjoys a tax exemption on income equal to capital expenditure incurred for a basis period for a YA given under the PIA 1986, paragraph 127(3) (b) or subsection 127(3A) of the ITA 1967 and fails to remit withholding tax on the expenditure incurred and payable to a non-resident in respect of payments under section 109, 107A, 109B or 109F of the ITA 1967, the expenditure incurred and payable to the non-resident will be added back in the tax computation.** **(iii) For a payer who enjoys a tax exemption on income equal to capital expenditure incurred for a basis period for a YA under the PIA 1986, paragraph 127(3)(b) or subsection 127(3A) of the ITA 1967 and fails to remit withholding tax on the expenditure incurred and payable to a non-resident in respect of payments under section 109, 107A, 109B or 109F of the ITA 1967, and has no chargeable income (incurred loss) the expenditure incurred and payable to the non-resident will be added back in the tax computation.** **Note:** **Notwithstanding the above explanation, the withholding tax provisions are still applicable.**

2. **<u>IBA claim on hotel building by REIT which is not the operator of the hotel</u>**

Example 5 of Public Ruling 9/2012 - Taxation of Real Estate Investment Trusts/Property Trust Funds illustrates that industrial building allowance (IBA) on a hotel cannot be claimed by its owner, a REIT which lets out the building to a third party which operates

the hotel business. It appears from the example that the IRB takes the view that the owner of the hotel building must also operate the hotel business in order to qualify for IBA claim on the hotel.

However paragraph 7.2 of the same public ruling states that REITs that rent out their buildings will only qualify for IBA if the tenant uses the building as an industrial building.

Based on paragraph 60, Schedule 3 of the Income Tax Act, the REIT in Example 5 should qualify for IBA as the building is used as an industrial building.

Request

It is very common for REITs to lease their properties to others who will operate business in the properties (e.g. hotels, educational institutions and hospitals). A disallowance of the IBA claim on such buildings which is **permissible under the law** will adversely affect the growth of REITs and the capital market. CTIM requests that the IRB reconsiders its position.

Response

2	**Noted, meanwhile IRB's Legal Department is looking into the matter.**

3. **Apportionment of actual loss from a property development/construction project**

Paragraph 12 of the Income Tax (Property Development) Regulations 2007 provides that where there is an actual loss from a project, "the loss may be apportioned in accordance with the formula provided for in regulation 6 for the purposes of ascertaining the profit or loss of the project for that basis period and preceding basis periods, and any assessment that has been made or will be made under the Act for those periods may be revised ...".

The use of the word 'may' indicates clearly that it is a choice and not obligatory, in which case the word "shall" would have been used. However, paragraph 10.6.4 of Public Ruling 1/2009, states that where there is an actual loss, "the actual gross loss has to be apportioned ..."

Request

CTIM is of the view that the public ruling is not consistent with the wording of the law and request that the public ruling be amended to accord with the law

Response

3.	**IRBM is reviewing paragraph 10.6.4 of the Public Ruling No. 1/2009**

4. **Public Ruling 1/2013: Deductions for Promotion of Export**

(i) Paragraph 6.2.1 of the public ruling explains the types of expenditure which qualify for deduction under the Income Tax (Promotion of Exports) Rules 1986.

Paragraph 6.2.1(a) states:-

(a) Publicity and advertisement

(i) Cost of advertisement in any media outside Malaysia. Example of media are television web site, radio, newspapers, trade or general magazines, trade directories and guidebooks. For the purpose, media does not include advertising and publicity on billboards and vehicles and

Request

CTIM wishes to seek clarification on the reason for excluding advertising on billboards and vehicles as these are legitimate and commonly used forms of advertisement.

Response

4(i)	**It is a policy decision not to allow such expenses.**

(ii) Paragraph 6.2.1(c) states:-

(b) Export market research/ export market information

The expenses involved here are expenses directly related to carrying out export market research or obtaining export market information. Example of such expenses are:

(i) Expenses incurred in employing marketing consultants to carry put product market research and product testing overseas if they are related to the export market. If the appointed consultants are from abroad, payments made to the consultants are subject to withholding tax.

Request

CTIM is of the view that the last statement above may create confusion. Not all payment to foreign consultant are subject to withholding tax. Section 109B applies only in respect

of services performed in Malaysia and Section 109F applies only if the payment does not constitute business income of the recipient.

Response

4(ii)	**Noted. A review will be done.**

5. **Determination of the date that a company becomes an RPC**

Under paragraph 34A(6)(b), Schedule 2 of the Real Property Gains Tax 1976, "real property company"(RPC), means –

(a) a controlled company which, as at 21 October 1988, owns real property or shares or both, the defined value of which is not less than 75% of the value of its total tangible assets; or

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

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

The date on which a company becomes a RPC requires some clarification based on the illustration below.

A company became RPC after it purchased real property. The timeline as illustrated below.

|---|---|---|---|

2.1.2013	15.2.2013	15.3.2013	2.5.2013
Date of signing of SPA	Arranged banking facilities	Increase in paid up capital	Bank released facilities & paid for differential sum (date property actually OWNED)

The issue involves the determination of the date on which does the company become a RPC? 2 January 2013 or 2 May 2013? The date of acquisition for RPGT purposes is generally the SPA date. However, for paragraph 34A of Schedule 2, this is not

specified. On the basis that the definition of a RPC requires ownership of tangible real property assets, technically, this would only arise on 2 May 2013 in the example above. In practice, the Inland Revenue Board treats 2 January 2013, i.e the date of the signing of the agreement as the date the company would become a RPC. If this treatment is correct, and in the event the transaction is never completed, the shares will remain as RPC shares which would clearly create an illogical result.

Request

IRB to clarify its position.

Response

5	**The date of agreement for the purchase of real property is one fixed and facilities the determination of the date when the company becomes Real Property Company (RPC). The date of the agreement is objective and allows for only one date to be used. The interpretation of when a company become a RPC is clear and is not ambiguous, when the date of the agreement for the purchase of real property is used as the date when the company become a RPC. The date of agreement makes clear the law as to the date when the company becomes a RPC.**

6. **Public Ruling 4/2005 - Withholding Tax on Special Classes of Income**

CTIM wishes to clarify if the IRB will revise the Public Ruling 4/2005 on Withholding Tax on Special Classes of Income following the Court of Appeal's decision in LHDNM v Alam Maritim (M) Sdn Bhd [2012] 5 MLJ 749.

Response:

6	**The decision of this case is noted. Any decision regarding this case will be made known through Public Ruling if applicable.**

7. **Public Ruling 4/2013 - Accelerated Capital Allowances**

(a) In example 10, it is stated that double deduction for promotion of export and ACA are not mutually exclusive. However, in PU (A) 111/2009, it is stated that the ACA does

not apply to a company which has been granted any incentive under the Promotion of Investments Act 1986 ("PIA").

Request

Since the double deduction for Promotion of Exports ("POE") is given under the PIA, can a company which is claiming double deduction for POE be entitled to claim ACA?

Response:

7(a)	**A company is not eligible for ACA if it is still enjoying POE because both incentives are mutually exclusive.**

(b) **Non-application rules**

For example, the Income Tax (Accelerated Capital Allowance) (Security Control Equipment and Monitoring Equipment) Rules 2013 state that the Rules are not applicable to –

"(a) an individual or a company has been granted any incentive under the Promotion of Investments Act 1986 .....

(c) an individual or a company has been granted any exemption under section 127 of the Act....."

For incentives under the Promotion of Investments Act 1986, the Malaysian Investment Development Authority (MIDA) issues a letter of approval stating that the taxpayer has been granted the pioneer or investment tax allowance incentive. The actual incentive period would generally commence after the date of the approval letter as certain conditions would have to be fulfilled.

The same applies for tax exemption granted under section 127 of the Income Tax Act 1967.

Request

When does the non-application take effect, from the date of the approval letter of the incentive or the date the incentive period commences?

Response

7(b)	**Non-application takes place from the year of assessment the incentive**

	period commences.

8. **Public Ruling 6/2013 - Unit Trust Funds Part II - Taxation Of Unit Trusts**

Example 2

In the formula to calculate permitted expenses under both Sections 60F and 63B of the ITA 1967, item "C" refers to is the aggregate of the gross income consisting of dividend (whether exempt or not), **interest** and rent, and gains from realization of investments for a basis period.

However we note that in example 2 of the Public Ruling 6/2013, the IRB has included the tax exempt interest income of RM5,000 to arrive at the aggregate gross income of "C".

The meaning of item "C" in Sections 60F and 63B can be contrasted from that in Section 60H [Closed-end fund company] where "C" refers to "the aggregate of the gross income consisting of **dividend and interest (whether exempt or not)** and gains made from the realisation of investments (whether chargeable to tax or not) for that basis period.

Request

The IRB to clarify its position and make the necessary amendments to the law and/or public ruling prospectively.

Response

8	**The intention was to include all income whether exempt or not in the denominator (C) in the formula. The law will be amended accordingly.**

9. **Incidence of penalties in relation to technical disputes**

The IRB has indicated that penalties may be waived during a tax audit where there is a "technical dispute". It would be helpful if IRB could provide guidelines on circumstances under which they would waive penalties and include in the Tax Audit Framework and the Tax Investigation Framework.

Response

9	**To determine whether the offence is the technical disputes depend on the facts of each case. As such, it is difficult to provide guidelines on**

	circumstances under which penalties will be waived. **During an audit, a penalty will be imposed under subsection 113(2) or paragraph 44B (7) (b) of the ITA 1967 if it is discovered that there has been an understatement or omission of income. The penalty rate is equivalent to the amount of tax undercharged (100%). However, the DGIR in exercising his discretionary powers may consider a lower penalty to be imposed.** **The concessionary penalty rates may be imposed in cases where the taxpayer makes a voluntary disclosure. As such the taxpayer is encouraged to make a voluntary disclosure regarding the omitted income before the commencement of an audit. This disclosure must be made in writing to the relevant Branch Director of IRBM.** **Furthermore, the penalty under subsection 113(2), will be imposed although the audit finding is considered as a 'technical adjustment or dispute'. This is because there is no legal provision provided under the ITA 1967, to waive the penalty under subsection 113(2) if the issue is considered as a 'technical adjustment or dispute'.**

10. **Interest income of treasury company from loans to related companies**

Under Section 4B of ITA, interest income from loans is treated as business income if the company carries on the business of lending money and the business is one which is licensed under any written law.

A treasury company within a corporate group providing loans to the group carries on the business of lending money. The company would have been required to be licensed under the Moneylenders Act 1951[Act 400] if not for section 2A (2) of Act 400 which specifically exempts companies lending money to related companies from being licensed.

We are of the view that the interest income of group treasury company from lending to related companies should continue to be treated as section 4(a) business source income.

Request

IRB to reconsider its position.

Response:

10	**The law stands as it is now.**

11. **Tax incentives for abandoned projects**

The following gazette orders have been issued in respect of tax incentives for the revival of abandoned projects:

- P. U. (A) 89/2013 - Income Tax (Deduction for Expenses in relation to Interest and Incidental Cost in Acquiring Loan for Abandoned Projects) Rules 2013
- P. U. (A) 88/2013 - Income Tax (Exemption) (No. 9) Order 2013

The term "abandoned project" is defined in the gazette orders to mean "a project which is certified by the Minister of Housing and Local Government as an abandoned project pursuant to paragraph 11(1) (ca) of the Housing Development (Control and Licensing) Act 1966 [Act 118]".

Under section 3 of the Housing Development (Control and Licensing) Act 1966, "housing development" is defined to mean:

"*to develop or construct or cause to be constructed in any manner whatsoever* ***more than four units of housing accommodation*** *and includes the collection of moneys or the carrying on of any building operations for the purpose of erecting housing accommodation in, on, over or under any land; or the sale of more than four lots of land or building lots with the view of constructing more than four units of housing accommodation*"

Request

Are the tax incentives restricted to pure housing development projects (comprising residential units only) or also applicable to mixed development projects (comprising a combination of residential and commercial units) which are abandoned?

Response:

11	Tax incentives under the above Rules apply to any abandoned projects certified as such by the Ministry of Urban Wellbeing, Housing and Local Government (MUHLG) irrespective the project is purely housing or mixed development. The PR will be issued on the above matter.

12. **Tax treatment of late payment interest**

The term 'interest' is not defined in the ITA. The PR 2/2011 provides the IRB's interpretation of interest as "The return of compensation for the use or retention by a person of a sum of money belonging to or owed to another person". Broadly, this could include late payment interest. However, late payment interest on trade amounts should arguably be treated as incidental to business income as such amounts relate directly to sales made. Although this is not clear in the ITA, certain DTAs exclude late payment penalties from the definition of interest. For example, Paragraph 5 of Article 11 of Double Taxation Agreement between Malaysia and Germany stipulates that "..... *Penalty charges for late payment shall not be regarded as interest for the purpose of this Article.*"

CTIM would like to request that the IRB agree to the position that late payment penalties should not be regarded as interest.

Response

12	**Late payment interest on trade amounts has always been treated as incidental to business income. However, with effect from YA 2013, such late payment interest is treated as non-business income under section 4B.**

13. **Eligibility of Group Relief**

To qualify for group relief for losses, besides the ownership test, Section 44A(7) stipulates the following additional conditions:

"*Notwithstanding that a company to which subsection (3) applies, owns at least seventy per cent of the paid-up capital in the other company, it shall not be treated to have satisfied that subsection unless additionally in the year of assessment the first mentioned company is beneficially entitled to at least seventy per cent of—*

(a) any residual profits of the other company, available for distribution to that other company's equity holders; and

(b) any residual assets of the other company, available for distribution to that other company's equity holders on a winding up."

Section 44A(12 further defines

"**residual assets**" *means net assets of the claimant or surrendering company after distribution made to—*

(a) creditors of that company in respect of commercial loans; and

(b) holders of shares other than ordinary share,

and where that company has no residual asset, a notional amount of one hundred ringgit is deemed to be the residual assets of the company;

"**residual profits**" *means profits of the claimant or surrendering company after deducting any dividend which is of—*

(a) a fixed amount or at a fixed rate per cent of the nominal value of the shares of that company; or

(b a fixed rate per cent of the profits of that company,

but before deducting any return due to any non-commercial loan creditor which is not of—

(i) a fixed amount or at a fixed rate per cent of the amount of the borrowing; or

(ii) *a fixed rate per cent of the profits of that company,*

and where that company has no residual profit, a notional amount of one hundred ringgit is deemed to be the residual profits of that company.

In tax audits, the IRB has requested for the computation of "residual profits" and "residual assets" to justify the claim for group relief for losses.

Request

We request that the IRB issues guidelines on the computation of "**residual profits**" and "**residual assets**".

Response:

13	**A draft of the Public Ruling on Group Relief will be sent to the Joint Public Rulings Working Group (JPRWG) in due course.**

14. **Income Tax (Deduction for the Provision of Child Care Centre) Rules 2013**

Rule 3(1) states:-

"For the purpose of ascertaining the adjusted income of a person resident in Malaysia from his business for the basis period for a year of assessment, a deduction shall be allowed for any outgoings and expenses which were -

(a) expenses in respect of expenditure on the provision and maintenance of a child care centre; and

(b) expenses in respect of child care allowance to the persons employed by him in his business.

"**Person**" is defined in Rule 3(5) as "any person who, for the purpose of a business of his, provides a child care centre for the benefit of persons employed by him in his business."

With the definition of "person" above, it appears that the deduction given under this gazette order is only applicable to an employer who provides a child care centre for the benefit of its employees.

Request

CTIM requests that IRB clarifies if this is the intention of the incentive. Would the expenses incurred by the employer in the following scenarios qualify for the deduction under the above Rules?

Scenario 1

A Sdn Bhd incurs expenses on the provision and maintenance of a child care centre which is registered with the Department of Social Welfare under the Child Care Centre Act 1984, for the benefit of its employees. No child care allowance is provided to his employees.

Response

14	**Yes, A Sdn Bhd qualifies for the deduction under the above rules, even though no child care allowance is provided to his employees.**

Scenario 2

B Sdn Bhd pays child care allowance to its employees who place their children in child care centres. However B Sdn Bhd does not provide a child care centre for his employees. Must the child care centres be registered with the Department of Social Welfare?

Response:

14	**Yes, B Sdn Bhd qualifies for the deduction under the above rules, even though it does not provide a child care centre for his employees.** **Yes, the child care centres must be registered with the Department of Social Welfare**

CTIM MEMORANDUM ON TECHNICAL ISSUES

11 September 2013

Prepared by:
Technical Committee – Direct Tax (I) [TC-DT(I)], and
Technical Committee – Direct Tax (II) [TC-DT(II)]

CHARTERED TAX INSTITUTE OF MALAYSIA

CTIM Memorandum on Technical Issues

Contents

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The proviso to the above sections was amended by Finance Act 2011 as follows:-

"*Provided that–*

(i) …; and

(ii) *where such tax is deducted or such amount is paid after the due date for the furnishing of a return for a year of assessment that relates to such payment, the tax or amount so paid shall not prejudice the imposition of penalty under subsection 113(2) if a deduction on such payment is made in such return or is claimed in the information given to the Director General in arriving at the adjusted income of the payer;*"

A taxpayer who has incurred an expense which is subject to withholding tax but has not paid nor credited the non-resident payee has technically not breached the provisions of Sections 109, 107A, 109B and 109F. Under such circumstances, sections 39(1)(f)(i) and (j) should not apply.

However, the IRB has indicated in the Technical dialogue on 8 April 2011 that in such a scenario, proviso (ii) to sections 39(1)(f), (i) and (j) would still apply and the penalty under Section 113(2) would be potentially applicable if a deduction for the expense is claimed and WHT is not paid. The IRB's application of the above sections is not consistent with the law and Public Ruling 4/2005.

Request
The IRB to reconsider its treatment.

(b) Effective Date

Based on section 3(4) of the Finance Act 2011, the above amendments "*have effect from 1 January 2011 for the year of assessment 2011 and subsequent years of assessment*".

There has been some confusion as to whether an income tax return for a year of assessment ("YA") prior to YA 2011 which was furnished to IRB after 1 January 2011, is subject to the above amendments made pursuant to Finance Act 2011.

Example

Company X closes its accounts annually on 31 September. The company only submitted its tax return for YA 2009 on 1 March 2011 instead of the due date of 30 April 2010.

The company made a claim for deduction of technical fees paid to a non-resident company. However the company only deducted and remitted the withholding tax on the technical fees to the IRB on 28 February 2011.

Request

The IRB to confirm that Section 39(1)(j) should not apply to Company X, since the tax return is in respect of a YA that is prior to YA 2011 even though its submission is on or after 1 January 2011.

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(c) Non-prohibition for deduction under Section 39(3)

Section 39(3) provides that notwithstanding the fact that withholding tax has not been paid, the relevant expense should not be added back where the taxpayer *"is exempt under paragraph 127(3)(b) or subsection 127(3A) or the Promotion of Investments Act, 1986, in respect of all income of that person from all sources not being exemption on income equal to capital expenditure incurred.*

Request

It is extremely rare that the income of a person from ALL sources would be exempt. We wish to seek clarification if this is the intended application of this section.

2. IBA claim on hotel building by REIT which is not the operator of the hotel

Example 5 of Public Ruling 9/2012 - *Taxation of Real Estate Investment Trusts/Property Trust Funds* illustrates that industrial building allowance (IBA) on a hotel cannot be claimed by its owner, a REIT which lets out the building to a third party which operates the hotel business. It appears from the example that the IRB takes the view that the owner of the hotel building must also operate the hotel business in order to qualify for IBA claim on the hotel.

However paragraph 7.2 of the same public ruling states that REITs that rent out their buildings will only qualify for IBA if the tenant uses the building as an industrial building.

Based on paragraph 60, Schedule 3 of the Income Tax Act, the REIT in Example 5 should qualify for IBA as the building is used as an industrial building.

Request

It is very common for REITs to lease their properties to others who will operate business in the properties (e.g. hotels, educational institutions and hospitals). A disallowance of the IBA claim on such buildings which is permissible under the law will adversely affect the growth of REITs and the capital market. CTIM requests that the IRB reconsiders its position.

3. Apportionment of actual loss from a property development/construction project

Paragraph 12 of the Income Tax (Property Development) Regulations 2007 provides that where there is an actual loss from a project, *"the loss **may** be apportioned in accordance with the formula provided for in regulation 6 for the purposes of ascertaining the profit or loss of the project for that basis period and preceding basis periods, and any assessment that has been made or will be made under the Act for those periods **may** be revised …*".

The use of the word 'may' indicates clearly that it is a choice and not obligatory, in which case the word "shall" would have been used. However, paragraph 10.6.4 of Public Ruling 1/2009, states that where there is an actual loss, *"the actual gross loss **has to** be apportioned …".*

Request

CTIM is of the view that the public ruling is not consistent with the wording of the law and request that the public ruling be amended to accord with the law

4. Public Ruling 1/2013: Deductions for Promotion of Export

(i) Paragraph 6.2.1 of the public ruling explains the types of expenditure which qualify for deduction under the Income Tax (Promotion of Exports) Rules 1986.

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Paragraph 6.2.1(a) states:-

(a) Publicity and advertisement

(i) Cost of advertisement in any media outside Malaysia. Example of media are television, web site, radio, newspapers, trade or general magazines, trade directories and guidebooks. For this purpose, media does not include advertising and publicity on billboards and vehicles, and

Request
CTIM wishes to seek clarification on the reason for excluding advertising on billboards and vehicles as these are legitimate and commonly used forms of advertisement.

(ii) Paragraph 6.2.1(c) states:-

(c) Export market research / Export market information[1]

The expenses involved here are expenses directly related to carrying out export market research or obtaining export market information. Examples of such expenses are:

(i) Expenses incurred in employing marketing consultants to carry out product market research and product testing overseas if they are related to the export market. If the appointed consultants are from abroad, payments made to the consultants are subject to withholding tax

Request
CTIM is of the view that the last statement above may create confusion. Not all payment to foreign consultant are subject to withholding tax. Section 109B applies only in respect of services performed in Malaysia and Section 109F applies only if the payment does not constitute business income of the recipient.

5. Determination of the date that a company becomes an RPC

Under paragraph 34A(6)(b), Schedule 2 of the Real Property Gains Tax 1976, "real property company"(RPC), means –

(a) a controlled company which, as at 21 October 1988, owns real property or shares or both, the defined value of which is not less than 75% of the value of its total tangible assets; or

(b) a controlled company to which subsubparagraph (a) is not applicable, but which, at any date after 21 October 1988, acquires real property or shares or both whereby the defined value of real property or shares or both ***owned*** *at that date is not less than 75% of the value of its total tangible assets:*

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

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The date on which a company becomes a RPC requires some clarification based on the illustration below.

A company became RPC after it purchased real property. The timeline as illustrated below.

|---|---|---|---|

2.1.2013	15.2.2013	15.3.2013	2.5.2013
Date of signing of SPA	Arranged banking facilities	Increase in paid up capital	Bank released facilities and paid for differential sum (date property actually ***OWNED***)

The issue involves the determination of the date on which does the company become a RPC? 2 January 2013 or 2 May 2013? The date of acquisition for RPGT purposes is generally the SPA date. However, for para 34A of Schedule 2, this is not specificied. On the basis that the definition of a RPC requires ownership of **tangible** real property assets, technically, this would only arise on 2 May 2013 in the example above. In practice, the Inland Revenue Board treats 2 January 2013, i.e the date of the signing of the agreement as the date the company would become a RPC. If this treatment is correct, and in the event the transaction is never completed, the shares will remain as RPC shares which would clearly create an illogical result.

Request

IRB to clarify its position.

6. Public Ruling 4/2005 - Withholding Tax on Special Classes of Income

CTIM wishes to clarify if the IRB will revise the Public Ruling 4/2005 on Withholding Tax on Special Classes of Income following the Court of Appeal's decision in LHDNM v Alam Maritim (M) Sdn Bhd [2012] 5 MLJ 749.

7. Public Ruling 4/2013 - Accelerated Capital Allowances

(a) In example 10, it is stated that double deduction for promotion of export and ACA are not mutually exclusive. However, in PU (A) 111/2009, it is stated that the ACA does not apply to a company which has been granted any incentive under the Promotion of Investments Act 1986 ("PIA").

Request

Since the double deduction for Promotion of Exports ("POE") is given under the PIA, can a company which is claiming double deduction for POE be entitled to claim ACA?

(b) Non-application rules

For example, the Income Tax (Accelerated Capital Allowance) (Security Control Equipment and Monitoring Equipment) Rules 2013 state that the Rules are not applicable to –

"(a) an individual or a company has been granted any incentive under the Promotion of Investments Act 1986 .....

(c) an individual or a company has been granted any exemption under section 127 of the Act....."

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For incentives under the Promotion of Investments Act 1986, the Malaysian Investment Development Authority (MIDA) issues a letter of approval stating that the taxpayer has been granted the pioneer or investment tax allowance incentive. The actual incentive period would generally commence after the date of the approval letter as certain conditions would have to be fulfilled.

The same applies for tax exemption granted under section 127 of the Income Tax Act 1967.

Request
When does the non-application take effect, from the date of the approval letter of the incentive or the date the incentive period commences?

8. <u>Public Ruling 6/2013 - Unit Trust Funds Part II - Taxation Of Unit Trusts</u>

Example 2

[2]Note	
Permitted expenses (**A**):	
Manager's remuneration	24,000
Share registration expenses	20,000
Audit, accounting & secretarial fees	12,000
Telephone & stationery	6,000
Printing and postage	5,000
	67,000
Gross income consisting of dividend and interest chargeable to tax (**B**):	
Dividend (regross) - 300,000 X 100/75	400,000
Interest (tax exempt)	NIL
	400,000
Aggregate of the gross income (whether chargeable to tax or not)(**C**)	
Malaysian dividends (gross)	400,000
Dividends (pioneer company – tax exempt)	100,000
Dividends from overseas company	100,000
Interest (tax exempt)	5,000
Gains on disposal of investments	300,000
	905,000

In the formula to calculate permitted expenses under both Sections 60F and 63B of the ITA 1967, item "C" refers to is the aggregate of the gross income consisting of dividend (whether exempt or not), **<u>interest</u>** and rent, and gains from realization of investments for a basis period.

However we note that in example 2 of the Public Ruling 6/2013, the IRB has included the tax exempt interest income of RM5,000 to arrive at the aggregate gross income of "C".

The meaning of item "C" in Sections 60F and 63B can be contrasted from that in Section 60H [Closed-end fund company] where "C" refers to "the aggregate of the gross income

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consisting of **dividend and interest (whether exempt or not)** and gains made from the realisation of investments (whether chargeable to tax or not) for that basis period.

Request

The IRB to clarify its position and make the necessary amendments to the law and/or public ruling prospectively.

9. Incidence of penalties in relation to technical disputes

The IRB has indicated that penalties may be waived during a tax audit where there is a "technical dispute". It would be helpful if IRB could provide guidelines on circumstances under which they would waive penalties and include in the Tax Audit Framework and the Tax Investigation Framework.

10. Interest income of treasury company from loans to related companies

Under Section 4B of ITA, interest income from loans is treated as business income if the company carries on the business of lending money and the business is one which is licensed under any written law.

A treasury company within a corporate group providing loans to the group carries on the business of lending money. The company would have been required to be licensed under the Moneylenders Act 1951[*Act 400*] if not for section 2A(2) of *Act 400* which specifically exempts companies lending money to related companies from being licensed.

We are of the view that the interest income of group treasury company from lending to related companies should continue to be treated as section 4(a) business source income.

Request

IRB to reconsider its position.

11. Tax incentives for abandoned projects

The following gazette orders have been issued in respect of tax incentives for the revival of abandoned projects:

- P. U. (A) 89/2013 - Income Tax (Deduction for Expenses in relation to Interest and Incidental Cost in Acquiring Loan for Abandoned Projects) Rules 2013
- P. U. (A) 88/2013 - Income Tax (Exemption) (No. 9) Order 2013

The term "abandoned project" is defined in the gazette orders to mean "a project which is certified by the Minister of Housing and Local Government as an abandoned project pursuant to paragraph 11(1)*(ca)*of the Housing Development (Control and Licensing) Act 1966 [*Act 118*]".

Under section 3 of the Housing Development (Control and Licensing) Act 1966, "housing development" is defined to mean:

"to develop or construct or cause to be constructed in any manner whatsoever **more than four units of housing accommodation** and includes the collection of moneys or the carrying on of any building operations for the purpose of erecting housing accommodation in, on, over or under any land; or the sale of more than four lots of land or building lots with the view of constructing more than four units of housing accommodation"

Request

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Are the tax incentives restricted to pure housing development projects (comprising residential units only) or also applicable to mixed development projects (comprising a combination of residential and commercial units) which are abandoned?

12. Tax treatment of late payment interest

The term 'interest' is not defined in the ITA. The PR 2/2011 provides the IRB's interpretation of interest as "The return of compensation for the use or retention by a person of a sum of money belonging to or owed to another person". Broadly, this could include late payment interest. However, late payment interest on trade amounts should arguably be treated as incidental to business income as such amounts relate directly to sales made. Although this is not clear in the ITA, certain DTAs exclude late payment penalties from the definition of interest. For example, Paragraph 5 of Article 11 of Double Taxation Agreement between Malaysia and Germany stipulates that "…... Penalty charges for late payment shall not be regarded as interest for the purpose of this Article."

CTIM would like to request that the IRB agree to the position that late payment penalties should not be regarded as interest.

13. Eligibility of Group Relief

To qualify for group relief for losses, besides the ownership test, Section 44A(7) stipulates the following additional conditions:

"*Notwithstanding that a company to which subsection (3) applies, owns at least seventy per cent of the paidup capital in the other company, it shall not be treated to have satisfied that subsection unless additionally in the year of assessment the first mentioned company is beneficially entitled to at least seventy per cent of—*

(a) any residual profits of the other company, available for distribution to that other company's equity holders; and

(b) any residual assets of the other company, available for distribution to that other company's equity holders on a winding up."

Section 44A(12 further defines

"residual assets" *means net assets of the claimant or surrendering company after distribution made to—*

(a) creditors of that company in respect of commercial loans; and

(b) holders of shares other than ordinary share,

and where that company has no residual asset, a notional amount of one hundred ringgit is deemed to be the residual assets of the company;

"residual profits" *means profits of the claimant or surrendering company after deducting any dividend which is of—*

(a) a fixed amount or at a fixed rate per cent of the nominal value of the shares of that company; or

(b a fixed rate per cent of the profits of that company,

but before deducting any return due to any non-commercial loan creditor which is not of—

(i) a fixed amount or at a fixed rate per cent of the amount of the borrowing; or

(ii) a fixed rate per cent of the profits of that company,

and where that company has no residual profit, a notional amount of one hundred ringgit is deemed to be the residual profits of that company.

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In tax audits, the IRB has requested for the computation of "residual profits" and "residual assets" to justify the claim for group relief for losses

Request

We request that the IRB issues guidelines on the computation of “residual profits” and “residual assets”.

14. Income Tax (Deduction for the Provision of Child Care Centre) Rules 2013

Rule 3(1) states:-
“For the purpose of ascertaining the adjusted income of a person resident in Malaysia from his business for the basis period for a year of assessment, a deduction shall be allowed for any outgoings and expenses which were -

(a) expenses in respect of expenditure on the provision and maintenance of a child care centre; and
(b) expenses in respect of child care allowance to the persons employed by him in his business.

“Person” is defined in Rule 3(5) as “any person who, for the purpose of a business of his, provides a child care centre for the benefit of persons employed by him in his business.”

With the definition of “person” above, it appears that the deduction given under this gazette order is only applicable to an employer who provides a child care centre for the benefit of its employees.

Request
CTIM requests that IRB clarifies if this is the intention of the incentive. Would the expenses incurred by the employer in the following scenarios qualify for the deduction under the above Rules?

Scenario 1
A Sdn Bhd incurs expenses on the provision and maintenance of a child care centre which is registered with the Department of Social Welfare under the Child Care Centre Act 1984, for the benefit of its employees. No child care allowance is provided to his employees.

Scenario 2
B Sdn Bhd pays child care allowance to its employees who place their children in child care centres. However B Sdn Bhd does not provide a child care centre for his employees. Must the child care centres be registered with the Department of Social Welfare?

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CHARTERED TAX INSTITUTE OF MALAYSIA (225750-T)

21 August 2013

(By Mail)

Encik Abd Aziz B. Hashim
Deputy Chief Executive Officer (Policy)
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Dear Encik Abd Aziz

TECHNICAL DIALOGUE

In the course of providing tax advice to clients, our members have encountered some technical issues which require clarification, and certain difficulties in complying with requirements imposed by the law. The Technical Committees of the Chartered Tax Institute of Malaysia (CTIM) have compiled the issues in a *Memorandum for Technical Dialogue,* which will be sent to you shortly.

On behalf of the Technical Committees of CTIM, we would like to request for a Technical Dialogue with the Inland Revenue Board at a date convenient to you to discuss the technical issues compiled. In view of the IRB's involvement in the 2014 Budget preparation, we would suggest that the Technical Dialogue be held in the third week of September 2013.

Should you require any further clarification, please feel free to contact Mr K.S. Lim at CTIM's office (Tel. No. 2162 8989, samb. 103; email : kslim@ctim.org.my).

Thank you.

Yours sincerely,

CHARTERED TAX INSTITUTE OF MALAYSIA

P Thomas Simon
Executive Director

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