INLAND REVENUE BOARD MALAYSIA

TAXATION OF REAL ESTATE INVESTMENT TRUSTS / PROPERTY TRUST FUNDS

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DIRECTOR GENERAL'S PUBLIC RULING

A Public Ruling as provided for under section 138A of the Income Tax Act 1967 is issued for the purpose of providing guidance for the public and officers of the Inland Revenue Board Malaysia. It sets out the interpretation of the Director General of Inland Revenue in respect of the particular tax law, and the policy and procedure that are to be applied.

A Public Ruling may be withdrawn, either wholly or in part, by notice of withdrawal or by publication of a new ruling.

Director General of Inland Revenue,
Inland Revenue Board Malaysia.

1. **Objective**

The objective of this Ruling is to explain the tax treatment accorded to approved real estate investment trusts / property trust funds in Malaysia.

2. **Related Provisions**

The provisions of the Income Tax Act 1967 (ITA 1967) related to this Ruling are sections 33, 43, 44, 61, 61A, 63C, 63D, 109D, 110, paragraphs 4*(a),* 4*(d),* Schedule 1 and paragraphs 2, 38A and 63 of Schedule 3.

3. **Interpretation**

The words used in this Ruling have the following meaning:

3.1 “Real estate investment trust” or “property trust fund” means a unit trust scheme that invests or proposes to invest primarily in income generating real estate.

3.2 “Islamic real estate investment trust” is a real estate investment trust that is managed and operated based on Syariah principles.

3.3 “Total income” in relation to a person and a year of assessment means total income ascertained in accordance with the ITA 1967.

3.4 “Distribution” refers to the distribution of income by a real estate investment trust or Islamic real estate investment trust to its unit holders.

3.5 “Securities Commission” means the Securities Commission established under the Securities Commission Act 1993.

3.6 “Fund” means a real estate investment trust or Islamic real estate investment trust.

4. **Basis Of Assessment Of Real Estate Investment Trusts / Property Trust Funds (REITs/PTF)**

The basis year for a year of assessment or the financial accounting period which ends on a day other 31 December is the basis period of REITs/PTF for that year of assessment and this is determined in accordance with the provisions of section 21A of the ITA 1967. All the subsections of section 21A are applicable except for subsection 21A (5) of the ITA 1967.

Example 1

Highand REIT commenced operations on 1.11.2007 and made up its accounts to 30.6.2008. The Highand REIT makes up its subsequent accounts to 30 June annually.

The basis periods for the following years of assessment are:

Year Of Assessment	Basis Period
2007	1.11.2007 to 31.12.2007
2008	1.01.2008 to 31.12.2008
2009	1.07.2008 to 30.06.2009
2010	1.07.2009 to 30.06.2010

5. Rental Income Of REITs/PTF - Special Tax Treatment

The tax treatment of PTF changed with effect from the year of assessment 2005 when the Government introduced new tax incentives to promote the growth of REITs/PTFs in Malaysia.

5.1 Prior to year of assessment 2005, there was no specific provision for the taxation of REITs/PTF. The tax treatment was in accordance with the provisions of the ITA 1967 applicable to unit trusts i.e. subsection 61(1), sections 63A and 63B.

Pursuant to section 63C of the ITA 1967, with effect from the year of assessment 2005, rental income received by REITs/PTF from its investments in real properties is treated as business income. Notwithstanding this special tax treatment, the ascertainment of the adjusted income from rental in the basis period for a year of assessment, the following restrictions are applicable:

(a) The amount of deductible expenses incurred in that year of assessment is restricted to the gross income from the rental source in that year of assessment. Any excess of expenditure is disregarded, i.e not allowable as a deduction against other sources of income of REITs/PTF or to be carried forward to the following years of assessment, and

(b) If the source does not produce any income, no deduction for expenses is allowed.

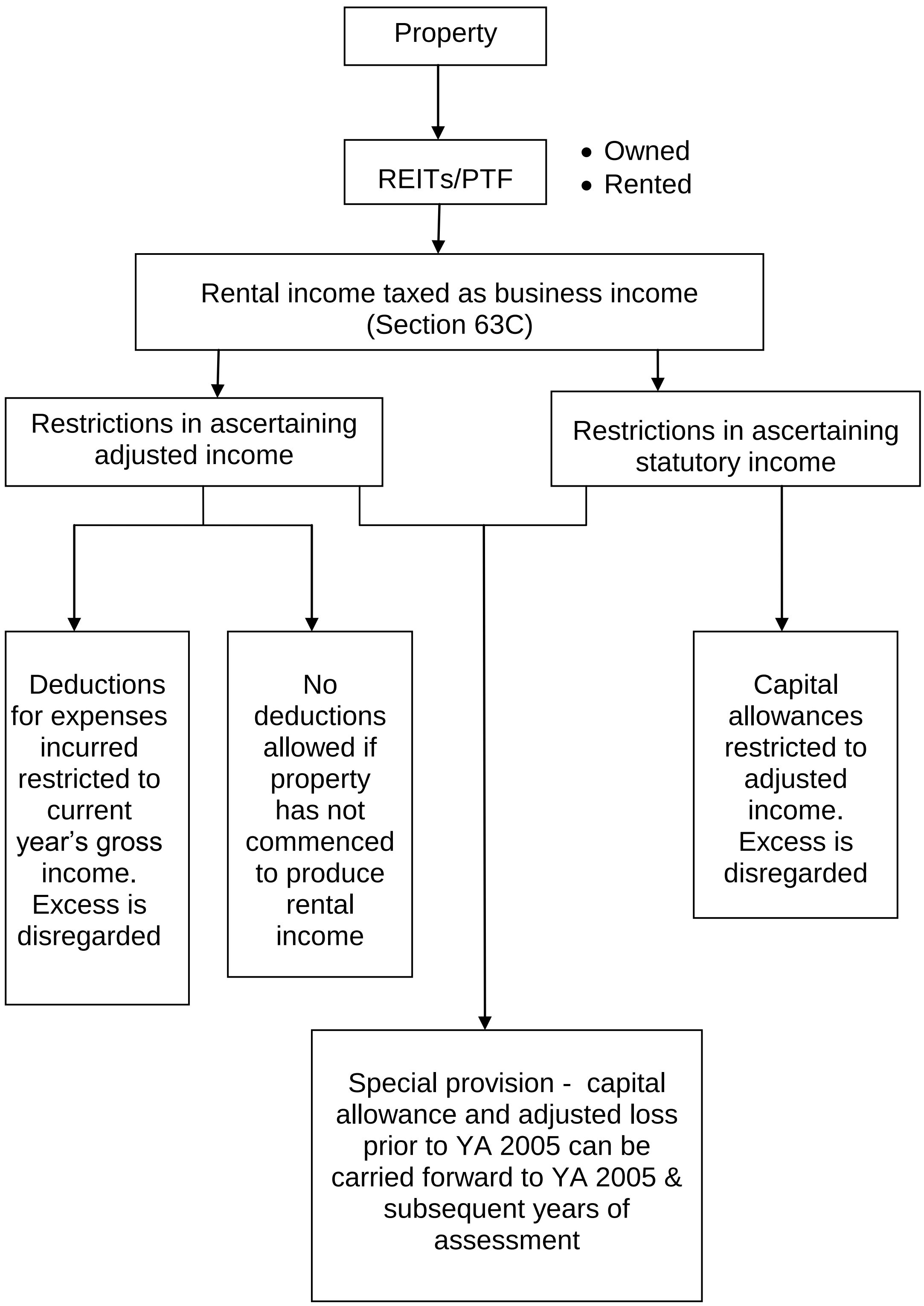
5.2 In ascertaining the statutory income from rental in the basis period for a year of assessment, capital allowance is allowable pursuant to Schedule 3 of the ITA 1967 but subject to the following restrictions:

(a) The amount of capital allowance is restricted to the adjusted income of the rental source for the year of assessment, and

(b) If there is no adjusted income or insufficient adjusted income to absorb the capital allowance, any excess capital allowances is not allowed to be carried forward to the following years of assessment.

5.3 The following diagram illustrates the special tax treatment accorded to REITs/PTF:

Special Tax Treatment Accorded To REITs/PTF



6. Deductibility Of Expenses

Rental income received by REITs/PTF from the letting of property is taxable under paragraph 4*(a)* of the ITA 1967. Rental income received from all of the rental properties constitutes a single source of income. The deductibility of expenses are as follows:

6.1 Pursuant to subsection 33(1) of the ITA 1967, expenses wholly and exclusively incurred in the production of the rental income are allowable against that rental income.

6.2 Since rental income is treated as a business source in accordance with section 63C of the ITA 1967, REITs/PTF manager's remuneration is deductible. However, trustee's fee is not allowable under subsection 33(1) of the ITA 1967.

6.3 Pursuant to the Income Tax (Deduction for Establishment Expenditure of Real Estate Investment Trust or Property Trust Fund) Rules 2006 [P.U.(A) 135/2006], with effect from year of assessment 2006, fees for legal, valuation and consultancy for establishing REITs/PTF prior to an approval by the Securities Commission (SC) are allowed as a deduction in ascertaining the adjusted business income of REITs/PTF from the rental source. REITs/PTF are deemed to have incurred the establishment expenditure in the basis period for a year of assessment in which the business commenced.

Example 2

Jaya Bhd and its group of companies own several commercial properties which are rented out. Since the rental returns have been lucrative and consistent over the years, Jaya Bhd decided to pool the properties and form a unit trust in order to enjoy the tax incentives offered by the Government. Jaya REIT was established on 1.6.2010 and the establishment expenses incurred amounted to RM1.3 million. Jaya Bhd made a submission to the SC for Jaya REIT to be approved as a REIT. Approval was obtained and Jaya REIT invited subscriptions from the public on 2.1.2011. Jaya REIT made up its first set of accounts to 31.12.2011.

The establishment expenses of RM1.3 million can be allowed as a deduction against Jaya REIT's gross income from rental source in ascertaining the adjusted income of its business in the basis period for year of assessment 2011.

7. Capital Allowance And Industrial Building Allowance

REITs/PTF are allowed to claim capital allowance and industrial building allowance as follows:

7.1 Capital allowance

REITs/PTF qualify for capital allowance pursuant to Schedule 3 of the ITA 1967. The capital allowance is deductible against the adjusted business income from the rental source of REITs/PTF.

7.2 Industrial building allowance

REITs/PTF deriving rental income from an industrial building may be granted industrial building allowance (IBA) under Schedule 3 of the ITA 1967, deductible against the adjusted business income from the rental source. REITs/PTF that rent out their buildings will only qualify for IBA if the tenant uses the building as an industrial building. Pursuant to paragraphs 63 and 64 of Schedule 3 of the ITA 1967, an industrial building is a building that is used for specified purposes. These purposes are limited to the certain types or groups of trades and the building must be used for any one of the qualifying ways stated.

7.3 Disposal of industrial building

Prior to year of assessment 2008 if companies dispose industrial buildings to REITs/PTF, the company is subject to a balancing charge if the disposal value is more than the residual expenditure or balancing allowance if the disposal value is less than the residual expenditure.

With effect from year of assessment 2008, pursuant to paragraph 38A of Schedule 3 of the ITA 1967, companies which have or should have claimed IBA and subsequently disposes the industrial building to REITs/PTF are deemed to have disposed the industrial building for a sum equal to its residual expenditure on the first day of the company's final period. As such, the company would not be subject to a balancing charge or balancing allowance. REITs/PTF are eligible to claim IBA on the remaining balance of the unclaimed tax written down value of the building.

Example 3

Company Y disposed of a factory (which had been granted IBA) on 30.6.2010 for RM5 million to Smart REITs (SR), a unit trust approved by the SC as a REIT. Company Y closes its accounts on 30 June and SR on 30 September. Company Y is deemed to have disposed of the building on 1.7.2009, the first day of Company Y's final period i.e.1.7.2009 to 30.6.2010. Residual expenditure of the factory at 1.7.2009 is RM120,000. SR rents out the factory to a tenant that uses the building as an industrial building.

As Company Y disposed an industrial building to a REIT, the selling price of RM5 million is disregarded. The qualifying expenditure for SR is the residual expenditure of the industrial building at 1.7.2009 i.e. RM120,000. No balancing allowance or charge arises to Company Y.

7.4 Disposal of industrial building together with plant and machinery

Paragraph 38A,of Schedule 3 of the ITA 1967 is applicable to industrial buildings only. When an industrial building is disposed of together with the plant and machinery, balancing charge or balancing allowance of the plant and machinery has to be computed separately.

Example 4

An Islamic REIT acquired a factory together with the plant and machinery from Company Z on 30.12.2009 for a sum of RM10 million (including RM1 million for the plant and machinery). Company Z closes its accounts on 31 December whereas the Islamic REIT on 30 September.

The factory building is an industrial building and Company Z is deemed to have disposed the factory building on the first day (1.1.2009) of Company Z's final period, i.e. 1.1.2009 to 31.12.2009. The residual expenditure of the factory building on 1.1.2009 was RM500,000 and the residual expenditure of the plant and machinery on 31.12.2009 was RM200,000. The Islamic REIT rents out the factory to a tenant that uses the building as an industrial building.

As Company Z disposed the factory building which is an industrial building to a REIT, the sale proceeds are disregarded. The Islamic REIT would be eligible to claim IBA on the balance of the unclaimed tax written down value of the factory building(RM500,000).

However, Company Z will be subject to balancing charge or balancing allowance on the disposal of the plant and machinery to the Islamic REIT. The disposal value of the plant and machinery is equal to the market value of the plant and machinery at the date of disposal or the net proceeds from the sale, whichever is greater.

7.5 IBA for building used in a hotel business

Where a person carrying on certain types or groups of trades has incurred in the basis period for a year of assessment expenditure on the construction or purchase of a building used for specified purposes for that business, that building is treated as an industrial building for the purposes of that business. In other words, where a person has for the purposes of a business of his incurred expenditure in the basis period for a year of assessment on the construction or purchase of a building used for specified purposes, that building is treated as an industrial building for the purposes of that business [paragraphs 12, 16, 42, 42A, 42B, 63 and 64 of Schedule 3 of the ITA 1967].

In the case where a person carrying on a hotel business has incurred expenditure on the construction or purchase of a building for the purpose of that hotel business, that hotel building is treated as an industrial building for the purpose of that hotel business. Where a person has incurred expenditure on the construction or purchase of a building for the purpose of a hotel business in the basis period for a year of assessment and if that building or part thereof is used by the person solely for the purpose of a hotel and that hotel is registered with the Ministry of Tourism, that person is eligible for IBA [paragraph 37F of Schedule 3 of the ITA 1967].

Example 5

Company A owned a hotel building in Kota Kinabalu and operated the hotel business since 2008. Company A has been eligible for IBA since the year of assessment 2008. On 1.4.2011, KK REIT purchased the hotel building (excluding the furniture and fixtures) from Company A for RM30 million. Company A rented the same hotel building from KK REIT and continued operating the hotel business. Both Company A and KK REIT close their accounts on 31.12 each year. Company A is deemed to have disposed of the hotel building to KK REIT on 1.1.2011, the first day of Company A's final period i.e. 1.1.2011 to 31.12.2011. Residual expenditure on 1.1.2011 was RM10 million.

For years of assessment 2008 to 2010, Company A had qualified for IBA as the company being the owner of the building, had operated the hotel business. Since KK REIT, the new owner, did not operate the hotel business, KK REIT does not qualify for IBA for year of assessment 2011 and subsequent years.

8. Transitional Provision - Section 63C ITA 1967

This transitional provison provides that -

(a) sections 43 and 44 of the ITA 1967 in respect of any adjusted loss, and

(b) paragraph 75 of Schedule 3 of the ITA 1967 in respect of capital allowance

of a unit trust which was ascertained prior to the coming into operation of section 63C of the ITA 1967 is allowable against the income for the year of assessment 2005 and subsequent years of assessment.

8.1 Unabsorbed losses and capital allowances ascertained prior to year of assessment 2005

Example 6

Amanah Pelaburan Kay (APK), an approved REIT since 1.1.2005 closes its accounts on 31 December every year. APK has been in operation since 2004 and derives rental income from 2 hospital buildings that are in Kuala Lumpur and Petaling Jaya.

The unabsorbed adjusted loss and capital allowance of APK for the year of assessment 2004 are as follows:

Property	Adjusted Loss(RM)	Capital Allowance(RM)
Hospital in Kuala Lumpur	Nil	Nil
Hospital in Petaling Jaya	300,000	100,000

For the year ended 31.12.2005, APK's income and expenditure statement and claims for capital allowance or industrial building allowance are as follows:

Year Ended 31.12.2005

Rented Building	RM
Hospital in Kuala Lumpur	
Rental	600,000
Allowable expenses	300,000
Industrial building allowance	25,000
Capital allowance	100,000
Hospital in Petaling Jaya	
Rental	400,000
Allowable expenses	300,000
Industrial building allowance	25,000
Capital allowance	100,000

Computation Of Total Income For Year Of Assessment 2005

Rented Building	RM	RM
Rental		
(a) Hospital in Kuala Lumpur	600,000	
(b) Hospital in Petaling Jaya	400,000	1,000,000
Less: Allowable expenses		
(a) Hospital in Kuala Lumpur	300,000	
(b) Hospital in Petaling Jaya	300,000	600,000
		400,000
Less: IBA		
(a) Hospital in Kuala Lumpur	25,000	
(b) Hospital in Petaling Jaya	25,000	50,000
		350,000
Less: Capital allowance		
(a) Hospital in Kuala Lumpur	100,000	
(b) Hospital in Petaling Jaya	100,000	
Current year capital allowance	200,000	
Capital allowance b/f[1]	100,000	300,000
Statutory income		50,000
Less: Loss b/f[2]	300,000	
(restricted)	50,000	50,000
Loss c/f	250,000	
Total income		NIL

Observation

[1]The unabsorbed capital allowance from the year(s) of assessment prior to the introduction of section 63C of the ITA1967 is carried forward to be deducted against the adjusted income in the year of assessment 2005 and subsequent years until it is fully absorbed.

[2] The unabsorbed loss of RM300,000 from the year(s) of assessment prior to the introduction of section 63C of the ITA1967 is carried forward to be deducted against the statutory income in the year of assessment 2005 and subsequent years until it is fully absorbed. Since only RM50,000 of the carried forward loss is absorbed in year of assessment 2005, the balance of RM250,000 is carried forward to the subsequent year(s) of assessment.

8.2 Unabsorbed capital allowances ascertained from year of assessment 2005

Example 7

The facts are the same as in Example 6 except that the income and expenses and claims for capital allowance/IBA of APK for the years ended 31.12.2006 and 31.12.2007 are as follows:

Rented Building	Year Ended 31.12.2006 (RM)	Year Ended 31.12.2007 (RM)
Hospital in Kuala Lumpur		
Rental	Nil	200,000
Allowable expenses	600,000	400,000
Industrial building allowance	50,000	50,000
Capital allowance	50,000	50,000
Hospital in Petaling Jaya		
Rental	1,200,000	1,300,000
Allowable expenses	300,000	300,000
Industrial building allowance	50,000	50,000
Capital allowance	350,000	300,000

In 2006 and 2007, the hospital building in Kuala Lumpur was under renovation.

Computation Of Total Income For Year Of Assessment 2006

Rented Building	RM	RM
Rental		
(a) Hospital in Kuala Lumpur	Nil	
(b) Hospital in Petaling Jaya	1,200,000	1,200,000
Less: Allowable expenses		
(a) Hospital in Kuala Lumpur	600,000	
(b) Hospital in Petaling Jaya	300,000	900,000
Adjusted income		300,000
Less: IBA		
(a) Hospital in Kuala Lumpur	50,000	
(b) Hospital in Petaling Jaya	50,000	100,000
		200,000
Less: Capital allowance		
(a) Hospital in Kuala Lumpur	50,000	
(b) Hospital in Petaling Jaya	350,000	
	400,000	
(restricted)	200,000	200,000
(disregarded[3])	200,000	
Statutory income / Total income		Nil

Loss (prior to YA2005) b/f 250,000[2]
Loss c/f 250,000[4]

Observation

[3]The capital allowance for year of assessment 2006 is restricted to the amount of adjusted income of RM200,000. The unabsorbed capital allowance of RM200,000 cannot be carried forward to the following year of assessment and is to be disregarded.

[4]The adjusted loss brought forward from the year of assessment prior to the introduction of section 63C of the ITA 1967 could not be fully absorbed in the year of assessment 2006. The balance of the unabsorbed loss can be carried forward to the subsequent year(s) of assessment until the amount is fully absorbed.

Computation Of Total Income For Year Of Assessment 2007

Rented Building	RM	RM
Rental		
(a) Hospital in Kuala Lumpur	200,000	
(b) Hospital in Petaling Jaya	1,300,000	1,500,000
Less: Allowable expenses		
(a) Hospital in Kuala Lumpur	400,000	
(b) Hospital in Petaling Jaya	400,000	800,000
Adjusted income		700,000
Less: IBA		
(a) Hospital in Kuala Lumpur	50,000	
(b) Hospital in Petaling Jaya	50,000	100,000
		600,000
Less: Capital allowance		
(a) Hospital in Kuala Lumpur	50,000	
(b) Hospital in Petaling Jaya	300,000	350,000
		250,000
Less: Loss b/f (refer to [4]Observation)	250,000	
Fully absorbed	250,000	250,000
Loss c/f	Nil	
Total income		Nil

8.3 Deductions for expenses and IBA restricted from year of assessment 2005

With effect from the year of assessment 2005, allowable expenses are restricted to gross income and IBA is restricted to the adjusted income from the business source of the REIT.

Example 8

A REIT owns 2 factory buildings in Shah Alam and Klang which were let out to 2 manufacturing companies since 2006. The factory located in Klang was not rented out in 2009 after the tenants vacated the premise on 31.12.2008. The accounting period of the REIT is 31.12. each year.

The Income and expenditure account and claims for capital allowance/IBA of the REIT for the year ended 31.12.2009 are as follows:

Year Ended 31.12.2009

Rented Building	RM
Factory (Shah Alam)	
Rental	300,000
Allowable expenses	350,000
Industrial building allowance	30,000
Factory (Klang) (vacant)	
Rental	Nil
Allowable expenses	50,000
Industrial building allowance	20,000
Dividends (exempted)	200,000

Computation Of Total Income For Year Of Assessment 2009

Rented Building	RM	RM
Rental		
(a) Factory (Shah Alam)		300,000
(b) Factory (Klang) (vacant)		Nil
		300,000
Less: Allowable expenses		
(a) Factory (Shah Alam)	350,000	
(b) Factory (Klang) (vacant)	50,000	
	400,000	
(restricted)	300,000	300,000
(disregarded[5])	100,000	
Adjusted income		Nil
Less: Industrial building allowance		
(a) Factory (Shah Alam)	30,000	
(b) Factory (Klang) (vacant)	20,000	
(disregarded[6])	50,000	Nil
Total income		Nil

Observation

[5,6]The excess expenditure of RM100,000 and IBA of RM50,000 that cannot be fully absorbed in the year of assessment 2009 cannot be carried forward to the following year of assessment and is to be disregarded.

8.4 Rental source that has not commenced as a source of income

If a building has not been rented out, a rental source is not considered as having been commenced. As such, any related expenses incurred prior to the commencement of that source of income are not deductible against other existing rental income.

Example 9

The facts are the same as in Example 8 except that the REIT purchased a new factory building in Petaling Jaya in 2010 which did not produce any income in 2010.

The income and expenditure account for the year ended 31.12.2010 is as follows:

Rented Building	RM
Factory (Shah Alam)	
Rental	500,000
Allowable expenses	350,000
Industrial building allowance	30,000
Factory (Klang)	
Rental	150,000
Allowable expenses	50,000
Industrial building allowance	20,000
Factory - new (Petaling Jaya)	
Rental	Nil
Allowable expenses	50,000
Dividend (single tier)	200,000

Computation Of Total Income For Year Of Assessment 2010

Rented Building	RM	RM
Rental		
(a) Factory (Shah Alam)		500,000
(b) Factory (Klang)		150,000
(c) Factory - new (Petaling Jaya)[7]		Nil
		650,000
Less: Allowable expenses		
(a) Factory (Shah Alam)	350,000	
(b) Factory (Klang)	50,000	
(c) Factory (Petaling Jaya)[8]	Nil	400,000
Adjusted income		250,000
Less: Industrial building allowance		
(a) Factory (Shah Alam)	30,000	
(b) Factory (Klang)	20,000	50,000
Statutory income / Total income		200,000
Dividends		200,000
Chargeable income		400,000

Observation

[7,8]The source of income from the factory in Petaling Jaya has not commenced as no rental income has been produced. Therefore no deduction for the expense is allowable for this factory.

9. Tax Treatment On Income Of REITs/PTF

REITs/PTF receive exempt income and this income continues to be an exempt income when distributed to the unit holders. REITs/PTF that comply with the provisions of section 61A of the ITA 1967 are tax-exempt.

9.1 Tax treatment of REITs prior to year of assessment 2007

With the introduction of section 61A of the ITA 1967 which took effect from year of assessment 2005, a tax flow through treatment was accorded to REITs/PTF. Under this treatment, REITs/PTF are tax-exempt on their total income for a year of assessment equivalent to the amount of income distributed to unit holders in the basis period for a year of assessment. The amount of income not distributed in that year of assessment would be subject to tax at the prevailing corporate tax rate at the REITs/PTF level.

Example 10

Luxury Property Investment Trust (LPIT), an approved REIT had a net income before tax amounting to RM1,500,000 and a total income of RM1,000,000 in the basis period for the year of assessment 2006. LPIT distributed RM900,000 of its total income to its unit holders in the year of assessment 2006. LPIT retained the balance in its account to carry forward to the following year of assessment.

As LPIT distributed RM900,000 of its total income of RM1 million, LPIT is exempted from tax on the total sum of RM900,000 distributed for the year of assessment 2006. The balance of total income not distributed amounting to RM100,000 is chargeable to tax at the tax rate of 28%.

9.2 Tax treatment on REITs from year of assessment 2007

With effect from year of assessment 2007, subsection 61A(1) of the ITA 1967 was amended and REITs/PTF are fully exempt from tax for a year of assessment if they distribute to their unit holders 90% or more of their total income in the basis period for that year of assessment.

9.2.1 Distribution is 90% or more of total income

Example 11

A REIT has the following total income for year of assessment 2009.

			RM
(a)	Business (rental)		200,000
	Less: Section 33(1) expenses		25,000
	Adjusted income		175,000
	Less: Capital allowance	15,000	
	IBA	60,000	75,000
	Statutory business income		100,000
(b)	Interest		10,000
	Aggregate income / Total Income		110,000

Distribution to unit holders: RM100,000

$$\% \text{ of distribution} = \frac{100{,}000}{110{,}000} \times 100 = 91\%$$

Chargeable income: Nil

Tax charged: Nil

9.2.2 Distribution is less than 90% of total income

Where distribution made by REITs to its unit holders is less than 90% of the total income, the whole chargeable income will be subjected to tax at the prevailing corporate tax rate.

Example 12

A REIT has the following total income for year of assessment 2009.

			RM
(a)	Business (rental)		200,000
	Less: Section 33(1) expenses		25,000
	Adjusted income		175,000
	Less: CA	15,000	
	IBA	60,000	75,000
	Statutory business income		100,000
(b)	Interest		10,000
	Aggregate income / Total income		110,000

Distribution to unit holders: RM90,000

$$\% \text{ of distribution} = \frac{90{,}000}{110{,}000} \times 100 = 81.81\%$$

Chargeable income: RM110,000

Tax charged: 110,000 @ 25% = 27,500

9.2.3 Audit adjustment resulting in a distribution of less than 90% of total income

Example 13

The facts are the same as in Example 11 except that an audit was carried out by the Inland Revenue Board Malaysia (IRBM) where adjustments made resulted in total income being increased to RM112,500 for the year of assessment 2009. As a result, the distribution of RM100,000 by the REIT was less than 90% of its total income.

Distribution to unit holders: RM100,000

$$\text{\% of distribution} = \frac{100,000}{112,500} \times 100 = 88.88\ \%$$

Chargeable income: RM112,500

Tax charged: 112,500 @ 25% = 28,125

As the REIT only distributed 88.88% of its total income of RM112,500, the Fund is taxed on the total sum of RM112,500 for the year of assessment 2009. The undistributed balance of RM12,500 that has been subject to tax will be retained in the REIT's account for future distribution.

It is to be noted that prior to an audit by IRBM, the REIT had distributed RM100,000 to the unit holders and the distribution was subjected to withholding tax. Subsection 110(9A) ITA 1967 will not be applicable to the unit holders who have been subjected to withholding tax.

9.3 Tax treatment on interest income received by REITs/PTF

Interest income earned by REITs/PTF from the following is exempt from tax:

(a) Any savings certificates issued by the government.

(b) Securities or bonds issued or guaranteed by the government.

(c) Debentures, other than convertible loan stock, approved by the Securities Commission.

(d) Bon Simpanan Malaysia issued by Bank Negara Malaysia.

(e) A bank or financial institution licensed under the Banking and Financial Institutions Act 1989 or Islamic Banking Act 1983.

(f) Bonds and securities issued by Pengurusan Danaharta Nasional Berhad, and

(g) Interest income received from a foreign source and remitted to the REIT in Malaysia.

9.4 Tax treatment on dividend income received by REITs/PTF

Taxable dividend income forms part of the total income of REITs/PTF and tax credits attached to taxable dividends are given to the REITs/PTF. When the total income of REITs/PTF are distributed to the unit holder, the distribution is subject to tax at the unit holder level. In other words, taxable dividend income of REITs/PTF no longer remains as a taxable dividend income when REITs/PTF distributes its total income to the unit holder.

9.5 Tax treatment on exempt income received by REITs/PTF

The tax exempt income received by REITs/PTF e.g. capital gains and certain interest income is not included in computing the total income of REITs/PTF.

9.6 Illustrations to show the tax treatment on the various types of income received by REITs/PTF

9.6.1 Rental and interest (tax exempt) - Distribution is more than 90%

Example 14

Sunnyland REIT, an approved REIT received rental from the letting of a hotel. For the year ended 31.3.2010, Sunnyland REIT claimed capital allowances of RM15,000 and had the following Income and Expenditure Statement:

Income Statement

			RM
Rent (hotel building)			2,000,000
Interest from Goverment Bonds (tax exempt)			275,000
			2,275,000
Less: Bad debts			
Specific provision	25,000		
Specific provision	30,000	55,000	
Property operating expenses:			
Property manager's fee	60,000		
Maintenance cost	60,000		
Insurance, assessment and quit rent	20,000	140,000	
Expenses of the REIT:			
Trustee's fee	30,000		
REIT manager's fee	60,000		
Administration expenses	20,000		
Depreciation	5,000		
Loan interest[9]	100,000	215,000	410,000
Net income before tax			1,865,000

[9] RM100,000 related to purchase of government bonds

Sunnyland REIT made the following distributions in the basis period for the year of assessment 2010:

Current year income	RM1,570,000
Interest from Goverment Bonds (tax exempt)	RM 275,000
Total	RM1,845,000

Computation Of Total Income For Year Of Assessment 2010

		RM
Net income before tax		1,865,000
Less: Interest from Government Bonds		275,000
		1,590,000
Add:		
Bad debts (general provision)	30,000	
Loan interest (Government Bonds)	100,000	
Depreciation	5,000	
Trustee fee	30,000	165,000
Adjusted income		1,755,000
Less:		
Capital allowances		15,000
Statutory income/ Total income		1,740,000

Distribution to unit holders: RM1,570,000

$$\% \text{ of distribution} = \frac{1,570,000}{1,740,000} \times 100 = 90.22\%$$

Chargeable income: Nil

Tax charged: Nil

The special tax flow through treatment can be summarised as follows:

		RM
Net income before tax		1,865,000
Less:		
Tax payable		Nil
Net income after tax (distributable income for the year)		1,865,000
Less:		
Income distributed (not subjected to tax)	1,570,000	
Exempt Government Bond interest	275,000	1,845,000
Undistributed income c/f (not subjected to tax)		20,000

9.6.2 Rental and interest income - Distribution is less than 90% and more than 90%

Example 15

Jaya REIT receives income and makes distribution for 2 years of assessment as follows:

Income	**YA 2009 (RM)**	**YA 2010 (RM)**
Statutory income - rental	10,000	9,000
Statutory income - Interest	2,000	5,000
Total income	12,000	14,000
Distribution	10,000 (83%)	14,000 (100%)
Net income before tax	15,000	16,000

Computation Of Chargeable Income And Tax Payable

Income	**YA 2009 (RM)**	**YA 2010 (RM)**
Total income of Jaya REIT	12,000	14,000
Chargeable income	12,000	NIL
Tax payable @ 25%	3,000	NIL

The special tax flow through treatment for the year of assessment 2009 can be summarised as follows:

	RM
Net income before tax	15,000
Less:	
Tax payable	3,000
Net income after tax (distributable income for the year)	12,000
Less:	
Income distributed (subjected to tax)	10,000
Undistributed income c/f (subjected to tax)	2,000

The special tax flow through treatment for the year of assessment 2010 can be summarised as follows:

		RM
Net income before tax		16,000
Less:		
Tax payable		Nil
Net income after tax (distributable income for the year)		16,000
Add:		
Undistributed income b/f (subjected to tax)		2,000
		18,000
Less:		
Distribution:		
Income distributed (not subjected to tax)	14,000	
Undistributed income b/f (subjected to tax)	2,000	16,000
Undistributed income c/f (not subjected to tax)		2,000

9.6.3 REITs derives rental and dividend income

Example 16

Condo REIT received income and makes the following distribution for year of assessment 2010.

Income	**YA 2010 (RM)**
Statutory business income (rental)	10,000
Dividend[10] (@ 25% = RM5,000)	20,000
Total income	30,000
Distribution (90%)	27,000
Net income before tax	50,000

Computation Of Chargeable Income And Tax Payable

	RM
Total income of REIT	30,000
Chargeable income	Nil

	RM
Tax payable	Nil
Less:	
Section 110 set off	5,000
Tax repayable	5,000

Observation

[10]From year of assessment 2008, single-tier dividend income is exempted from tax and any expenses related to the derivation of the dividend are to be disregarded. Also, with effect from year of assessment 2008, the statutory income from dividend (franked dividend) received by REITs/PTF is deemed to be the total income or part of the total income of REITs/PTF. REITs/PTF are given a set-off for the tax credit attached to dividends.

The special tax flow through treatment can be summarised as follows:

	RM
Net income before tax	50,000
Add:	
Tax repayment	5,000
Net income after tax (distributable income for the year)	55,000
Less:	
Income distributed (not subjected to tax)	27,000
Undistributed income c/f (not subjected to tax)	28,000

Example 17

The facts are the same as in Example 16 except that Condo REIT makes an income distribution of less than 90% of total income for year of assessment 2010.

Income	YA 2010 (RM)
Statutory business income (rental)	10,000
Dividend (@ 25% = RM5,000)	20,000
Total income	30,000
Distribution (66.66%)	20,000
Net income before tax	50,000

Computation Of Chargeable Income And Tax Payable

	RM
Total income of REIT	30,000
Chargeable income	30,000

	RM
Tax payable - 30,000 @ 25%	7,500
Less:	
Section 110 set off	5,000
Tax payable	2,500

The special tax flow through treatment can be summarised as follows:

	RM
Net income before tax	50,000
Less:	
Tax payable	2,500
Net income after tax (distributable income for the year)	47,500
Less:	
Income distributed (not subjected to tax)	20,000
Undistributed income c/f (not subjected to tax)	27,500

10. Rental Income Of A Unit Trust (Other Than REITs/PTF)

To ensure that REITs/PTF enjoy the special tax treatment where rental income from the letting of property is treated as a business source, a new provision under section 63D was introduced to exclude unit trusts other than REITs/PTF from this special treatment. Other property trusts that do not qualify as REITs/PTF under SC's REITs Guidelines will continue to have their rental income treated as a source under paragraph 4*(d)* of the ITA 1967 and special deductions will be available to these unit trusts under sections 63A and 63B of the ITA 1967.

11. Distribution Of REITs/PTF Income To Unit Holders

REITs/PTF may make any number of distributions to its unit holders anytime in the basis period for a year of assessment.

11.1 Grace period allowed to distribute income to qualify for tax exemption

If REITs/PTF intend to distribute 90% or more of its total income but has fallen short of 90% at the end of the basis period, REITs/PTF are given a grace period of two months from the closing of its accounts to distribute the balance so as to qualify for tax exemption at the REITs/PTF level.

11.2 Deduction of withholding tax

Pursuant to section109D of the ITA 1967, where REITs/PTF (payer) that are tax-exempt under section 61A of the ITA 1967 distribute income which is deemed derived from Malaysia to a unit holder, the payer is required to deduct the tax at the rate applicable to such income. Withholding tax under section 109D of the ITA 1967 is a final tax.

11.3 Determining the residence status of unit holders

For purposes of facilitating deduction of withholding tax, REITs/PTF may use the information available in the Central Depository System (CDS) account to determine the residence status of the unit holder i.e. based on the nationality of the unit holder. In cases where the unit holders are able to confirm their tax residence status directly to the payer, such confirmation may also be relied upon for purposes of deducting withholding tax.

11.4 Withholding tax rates

A summary of the withholding tax rate is as follows:

(a) resident and non-resident individual unit holders as well as other resident entities are subject to a final withholding tax of 10% for the period from 1.1.2009 to 31.12.2016.

(b) foreign institutional investors are subject to a final withholding tax of 10% for the period from 1.1.2009 to 31.12.2016, and

(c) foreign corporate unit holders are subject to a final withholding tax at the prevailing corporate tax rate in accordance with Part 1 of Schedule 1 of the ITA 1967.

11.5 Accumulated income of REITs/PTF

11.5.1 The undistributed accumulated income of REITs/PTF from prior years could fall under any one of the following categories:

(a) A previous year's undistributed income (tax exempt), or

(b) A previous year's undistributed income which has already been subjected to tax at the REITs/PTF level.

11.5.2 The undistributed accumulated income of REITs/PTF from prior years which has been subjected to tax at the REITs/PTF level would carry with it a tax credit[11]. The distribution of such income will not be subject to any further taxes upon distribution in subsequent years. The tax credit indicated on the distribution voucher would be at the actual tax rate suffered by the REITs in the year of assessment in which the income was assessed.

[11]Pursuant to subsection 110(9A) of the ITA 1967 this tax credit

can be utilised as a set-off against the tax payable by the unit holders for the year of assessment in which the accumulated income (subjected to tax at the REITs/PTF level) is distributed.

11.6 Distribution voucher

REITs/PTF shall prepare distribution vouchers for the unit holders based on the share of each unit holder at the time of distribution. A typical distribution voucher should contain the following details:

(a) Payment date.

(b) Accounting period.

(c) Number of units held.

(d) Taxable income.

(e) Malaysian tax.

(f) Non-allowable expenses.

(g) Non-taxable income, and

(h) Net amount payable.

(Refer to Appendix 1 for a specimen sample of a distribution voucher).

11.7 Information on unit holders

REITs/PTF shall furnish to the Inland Revenue Board of Malaysia (IRBM) the following information when making distributions to both resident and non-resident unit holders:

(a) Name of unit holder.

(b) Identity card number / company registration number.

(c) Taxable income

(i) Exempt at REITs/PTF level

(ii) Undistributed income from previous years, and

(d) Tax suffered at REITs/PTF level on undistributed income.

REITs/PTF may forward the above information using a diskette or compact disc (CD) to:

Lembaga Hasil Dalam Negeri Malaysia
Cawangan Tidak Bermastautin
Unit Cukai Pegangan
Tingkat 7 Kanan, Blok 8
Kompleks Pejabat Kerajaan
Jalan Duta, Kuala Lumpur
Karung Berkunci 11061
50990 Kuala Lumpur.

12. **Payment Of Withholding Tax**

When REITs/PTF distributes income to a unit holder which is not a resident company, the REITs/PTF being the payer has to deduct withholding tax at the applicable tax rates. The payment of withholding tax would have to be made as follows:

12.1 The payer must remit the amount withheld to the Director General Of Inland Revenue (DGIR) within one month after distributing the income to the unit holder other than a unit holder which is a resident company. However the DGIR may -

(a) give notice in writing to the payer requiring him to deduct and pay tax at any other rates or to distribute the income without deduction of tax, or

(b) under special circumstances, the DGIR has allowed extension of time for the tax deducted to be paid.

12.2 The payer must pay withholding tax on the gross income distributed (global basis) in respect of all its unit holders without having to provide detailed information on the recipients when making payment.

12.3 Since the payment is on a global basis, registration of files will be for the payers only and not for each unit holder. IRBM will record the payment of withholding tax as a whole without details for each recipient of distribution. However, the payer must make details of the payment available upon the request of IRBM.

12.4 The payer has to submit Form CP37E and furnish the following particulars when making payment:

(a) Name, address and income tax reference number of the payer, and

(b) Particulars of deductions such as the period for which distribution is made, date of distribution, gross distributed income, amount of deduction and net amount distributed.

Form CP37E is available for download from IRBM's website at http://www.hasil.gov.my.

12.5 Form CP37E together with the payment must be submitted to the relevant branches at the following addresses according to the location of the branch that is handling the income tax file of the payer.

STATES	ADDRESS
Peninsula Malaysia	Lembaga Hasil Dalam Negeri Malaysia Cawangan Pungutan Tingkat 15, Blok 8A Kompleks Pejabat Kerajaan Jalan Duta, Karung Berkunci 11061 50990 Kuala Lumpur
Sabah & WP Labuan	Lembaga Hasil Dalam Negeri Malaysia Unit Pungutan Tingkat Bawah, 3 & 4, Wisma Hasil Jalan Tuanku Abdul Rahman 88600 Kota Kinabalu Sabah
Sarawak	Lembaga Hasil Dalam Negeri Malaysia Unit Pungutan, Aras 1, Wisma Hasil No 1, Jalan Padungan 93100 Kuching Sarawak

13. Failure To Deduct And Remit Tax

Where the payer fails to pay any amount of withholding tax due from him to the DGIR under subsection 109D(2) of the ITA 1967, the amount which he fails to pay shall be increased by 10% of the amount. The amount which he fails to pay and the increased sum shall be a debt due from him to the Government and shall be payable immediately to the DGIR pursuant to subsection 109D(3) of the ITA 1967.

14. Debt Due To Payer

Where the payer who makes payments to the unit holder has not deducted withholding tax but paid the withholding tax himself to the DGIR, the payer may recover that amount of withholding tax from that unit holder as a debt due to the payer.

Director General of Inland Revenue,
Inland Revenue Board Malaysia.

Appendix 1

Specimen sample of a REITs/PTF distribution voucher

ABC REIT

VOUCHER NO.	DISTRIBUTION NO.	UNIT HOLDINGS	DISTRIBUTION INTERIM / FINAL	PERIOD ENDING	PAYMENT DATE

Distribution from the income which is tax exempt at REITs/PTF level under Section 61A of the Income Tax Act 1967

TAXABLE INCOME	MALAYSIAN TAX WITHHELD	NON-TAXABLE INCOME / NON-DEDUCTIBLE EXPENSE	NET PAYABLE

Distribution of income which has been subject to tax at REITs/PTF level

TAXABLE INCOME	MALAYSIAN TAX PAID BY REITs/PTF	NON-TAXABLE INCOME / NON-DEDUCTIBLE EXPENSE	NET PAYABLE

We hereby certify that Malaysian income tax deducted as above has been or will be accounted for by us to the Director General of Inland Revenue Malaysia. Please retain this voucher for submission to the tax authorities.

Details of Unit Holder

Yours Faithfully

ABC REIT