Minutes of the dialogue between Technical Department of IRBM and Association of Accountant on 17-06-2002

1. Interpretation of 'Crediting'

The term 'crediting' is used in various provisions of the Income Tax Act, 1967 (ITA) with regard to withholding tax. However, we note that there has been no guidance on the meaning or interpretation of this term. The term 'crediting' has been interpreted (in the Canadian case of *Compagnie Miniere Quebec Cartier v. MNR (84 DTC 1348),* to mean more than the making of an accounting entry, and it involves "making a sum of money available to" the creditor.

In view of the fact that the time frame within which withholding tax is payable rests on the meaning of this term, it is important to obtain the IRB's clarification and guidance on the interpretation of the term 'crediting', particularly under the current self assessment regime.

Jawapan.

LHDN mengesahkan bahawa perkataan "crediting" merujuk kepada sesuatu yang lebih daripada "book entry" semata-mata. Sesuatu amaun dianggap telah dikreditkan ke akaun seorang bukan-pemastautin sekiranya ianya telah sedia untuk digunakan oleh bukan pemastautin tersebut bagi manfaat dirinya. Oleh itu makna 'paying/crediting' bermaksud :-

(i) tarikh amaun tersebut dibayar; atau
(ii) tarikh amaun tersebut dikreditkan ke dalam akaun penerima ; atau
(iii) jika amaun itu digunakan untuk dikontra dengan amaun yang terhutang oleh penerima, tarikh yang perlu diambil kira ialah tarikh kontra dalam buku akaun pembayar.

Tindakan : Untuk makluman semua cawangan

2. Section 29 of the ITA - Basis Period to which 'Income Obtainable on Demand' is Related

Pursuant to Section 29 of the ITA (notwithstanding Sections 23 to 28), where a person is able to obtain the receipt of income on demand, that income shall be treated as received in the period when such a circumstance arises. Meanwhile, under Section 27 of the ITA, interest income is taxable on a received basis in the period in which the interest income first becomes receivable. Therefore, under Section 27 of the ITA, the charge to tax only arises when the interest income is received, although it could relate to an earlier period. However, under Section 29 of the ITA, if that interest income is 'obtainable on demand' in a particular period, the interest income would be taxable in that period, notwithstanding that it may not have been received in that period.

In view of the self assessment system, the professional bodies wish to seek the IRB's clarification on the following matters:

(i) the type of circumstances that would fall within the tax treatment governed by Section 29 of the ITA;

(ii) the distinction between 'income obtainable on demand' and 'income that is receivable'; and

(iii) the distinction between amounts due from related parties and amounts due from third parties, in the context of item (ii) above.

Jawapan.

LHDN mengesahkan bahawa maksud perkataan "income obtainable on demand" dan "receivable" boleh dibezakan seperti berikut :-

Perkataan "income obtainable on demand" merujuk kepada keadaan dimana amaun itu layak diterima dan penerima boleh menuntutnya pada bila-bila masa tanpa mengambil kira tarikh pembayaran sebenar. Sebagai contoh, faedah yang boleh diterima pada satu tarikh tertentu tetapi belum dibayar disebabkan oleh suatu persefahaman/persetujuan dengan siberhutang. Sipiutang mempunyai hak dibawah undang-undang untuk meminta dan menerima bayaran faedah tersebut, namun demikain sipiutang tidak menuntut bayaran atas sebab-sebab tersebut. Dalam keadaan ini faedah itu adalah "obtainable on demand" dan sipiutang dianggap telah menerima faedah itu pada tarikh ia layak diterima.

Perkataan "receivable" pula merujuk kepada keadaan dimana sesuatu amaun itu mungkin boleh diterima tetapi hanya boleh dibayar pada masa yang ditentukan oleh sesuatu perjanjian yang telah diadakan sebelumnya. Sebagai contoh, faedah yang terakru mungkin tidak boleh dituntut disebabkan wujudnya perjanjian yang menetapkan supaya bayaran dibuat pada tarikh yang terkemudian. Walaupun faedah tersebut terakru ia bukannya "obtainable on demand", ia hanya boleh dikenakan cukai pada tarikh ia diterima seperti yang ditetapkan di dalam perjanjian. Namun begitu faedah itu apabila diterima akan dikenakan cukai bagi tempoh ia terakru.

Penggunaan Seksyen 27 dan 29 tidak membezakan di antara transaksi dua pihak yang sama atau dengan pihak yang berlainan.

3. Paragraph 49, Schedule 3 of the ITA - 'Relevant Interest'

We understand that where a taxpayer rents and uses an industrial building and incurs renovation costs on the rented building, the taxpayer should be having a 'relevant interest', and should be entitled to claim industrial building allowances

(IBA) on the renovation costs. We also understand that it has been the practice of the IRB to grant IBA on the renovation costs under such circumstances. Nevertheless, the professional bodies would like the IRB to reaffirm that it is still the practice of the IRB to grant IBA on renovation costs incurred on an industrial building rented (and not owned) by the taxpayer.

Jawapan.

LHDN mengesahkan bahawa kos ubahsuai yang dilakukan oleh penyewa sebuah bangunan industri seperti keadaan yang disebut di atas layak mendapat Elaun Bangunan Industri.

4. Financial Institutions - Amortisation of Premiums/Accretion of Discounts

For accounting purposes, premiums/discounts will be amortised over the life of the security. For tax purposes, we understand that any deduction/taxability would arise upon maturity or realisation of the security. However, due to the volume of such transactions undertaken by financial institutions, it is difficult in practice to apply the 'realised' basis to each separate investment. We are of the opinion that the IRB should take a more practical and pragmatic approach by accepting the accounting basis and thus, adopting the accruals basis for the tax treatment of such items.

Jawapan.

LHDN mengesahkan bahawa asas akruan dari segi perakaunan bagi pelunasan premium (amortisation of premiums) atau pengumpulan (accreation) diskaun (untuk sepanjang tempoh sesuatu sekuriti/instrumen) boleh diterima bagi tujuan percukaian. Walau bagaimanapun, pembayar cukai perlu menggunakan kaedah penentuan yang konsisten ke atas sesuatu pendapatan/perbelanjaan.

5. Provision for Diminution in Value of Stocks/Shares

For banks, stockbrokers, share traders, etc., stocks/shares would be regarded as their 'stock in trande'. We understand that pursuant to Section 35 of the ITA, a deduction should be available for the diminution in value of such stocks. For practical purposes, it is often the case that a provision is made rather than an actual write-down to take into account of the fact that the value may fluctuate. As this would result in the stocks being stated at their carrying values, we are of the opinion that a deduction should be allowed for this type of provision. We understand that a draft ruling on this issue has been prepared and in the interim, the professional bodies would like the IRB to confirm that a deduction would be allowed on the said provision.

Jawapan.

Di mana peruntukan umum dibuat bagi penurunan nilai sesuatu stok/saham (sebagai contoh - 20% atau 30% dari nilai stok/saham), amaun peruntukan tersebut tidak dibenarkan sebagai potongan dari segi percukaian.

Sebaliknya, apabila peruntukan penurunan nilai stok/saham dibuat bagi menggambarkan nilai pasaran (i.e sebagai contoh, membandingkan kos sesuatu stok/saham dengan nilai pasaran pada suatu masa tertentu), peningkatan peruntukan boleh dibenarkan.

LHDN juga mengesahkan bahawa untuk menuntut potongan cukai bagi peruntukan penurunan nilai suatu stok/saham, pembayar cukai perlu menjelaskan asas bagaimana penilaian tersebut dibuat.

Di samping itu, apabila peruntukan penurunan nilai sesuatu stok/saham tidak lagi diperlukan, amaun berkaitan perlulah ditambah balik dan dikenakan cukai.

Stok/saham hendaklah ditunjukkan dalam akaun perdagangan pada nilai kos dan peruntukan penurunan/peningkatan nilai stok/saham dalam akaun untung rugi dan kunci kira-kira.

6. Withholding Tax

6.1 Regional Hubs

In recent years, a few large organisations have set up regional hubs to centralise their resources in respect of management and administrative services. This is often implemented with the view to minimising operating costs and maximising efficiency and productivity in order to achieve group synergy. The costs incurred by the regional centre for the shared services are normally recovered from the companies in the group by way of reimbursement of costs or charge of management fees.

The professional bodies are of the view that the aforesaid reimbursement of costs or management fee payments to non-residents should not fall within the ambit of Section 109B(1)(b). If the IRB takes the view that withholding tax is applicable to those payments and in the event that the non-residents are not able to claim the tax withheld as a credit in their home countries, the tax suffered would be a added cost to the group and may defeat the purpose of setting up the regional centre to undertake shared services. For multi-national conglomerates, the use of shared service centres for "backroom activities" is an essential part of the efforts to reduce costs and increase competitiveness of its businesses.

The professional bodies would like to confirm that the above would not attract withholding tax under Section 109B(1)(b) of the ITA.

Jawapan.

LHDN mengesahkan bahawa keputusan yang dibuatnya terdahulu iaitu kedua-dua perbelanjaan bayaran balik (reimbursements) dan bayaran yuran pengurusan termasuk di bawah Seksyen 4A dan tertakluk kepada cukai pegangan kecuali bayaran berkaitan urusan pentadbiran dan perkhidmatan harian biasa (day to day) syarikat.

6.2 Reimbursements of Out-of Pocket Expenses

A non-resident consultant comes to Malaysia to perform work for a short period of time (i.e. no PE arises and therefore Section 109B applies) for a local entity. The consultant incurs air fare, taxi fare, hotel accommodation and meal expenses, etc., and these expenses are reimbursed by the local entity. The IRB had stated in an earlier dialogue that reimbursements of out-of-pocket expenses made to a non-resident would be subject to withholding tax under Section 109B since it is concerned about the possibility of abuse and withholding tax evasion by taxpayers, by incorporating elements of a fee in the reimbursements.

The professional bodies had earlier expressed the view that withholding tax should not be applicable under the following circumstances:

(i) where the Malaysian taxpayer directly bears/pays the out-of-pocket expenses instead of the non-resident; or

(ii) where the non-resident bears/pays the out-of-pocket expenses (which are later reimbursed by the local entity), provided that such expenses can be substantiated by documentary evidence such as receipts, invoices, etc.

The professional bodies would like to seek the IRB's confirmation that withholding tax would not be applicable in the above circumstances.

Jawapan.

LHDN mengesahkan sekali lagi tentang keputusan yang dibuat sebelum ini (Dialog No. 2/2001) iaitu "reimbursement of out-of-pocket expenses" adalah sebahagian dari pendapatan kasar seorang bukan-pemastautin dan tertakluk kepada cukai pegangan.

LHDN juga sedia maklum komen yang dikemukakan oleh badan profesional tersebut, tetapi menegaskan bahawa LHDN keberatan untuk membenarkan "reimbursements" dikecualikan dari dikenakan cukai pegangan untuk mengelakan kemungkinan berlakunya penyelewengan.

6.3 Public Ruling on the Scope of Withholding Tax

Section 109B(1)(b) of the Act provides that withholding tax is required to be deducted from the payments made to non-residents in respect of the following:

- technical advice, assistance or services rendered in connection with technical management or administration of any specific, industrial or commercial undertaking, venture, project or scheme.

The scope of Section 109B(1)(b) has been a controversial issue. We note that in practice, the IRB has been taking a wide interpretation of this section. As a result, withholding tax is applicable on a wide range of payments made to non-residents. In practice, most taxpayers would deduct the withholding tax to avoid the imposition of a penalty by the IRB for non-compliance with the withholding tax provisions. This inevitably increases the costs of operations and may be seen as a disincentive to those businesses affected by such a withholding tax.

The professional bodies would like to suggest that the IRB issue a public ruling to set out clearly the scope of the withholding tax. It would be very useful if the types of payments which fall within the ambit of the above provision are clearly specified, particularly in respect of the reimbursement of costs or management fee payments by multinational conglomerates for the shared services to non-residents. This will facilitate tax compliance under the self assessment system.

Jawapan.

LHDN memaklumkan bahawa ia akan menyediakan ketetapan umum berkaitan cukai pegangan di bawah Seksyen 109B.

7. <u>Private Usage of Motor Vehicles in Controlled Companies</u>

We understand that it has been the practice of the IRB to disallow a deduction for the private usage of motor vehicles in the case of controlled companies. We are of the opinion that if this treatment is adopted, then it should not be necessary for the private usage of such vehicles to be reported as benefits in kind in the relevant employees' Forms EA. In other words, if the company has paid the tax on this private usage of motor vehicles, the employee should not be assessed on it as well. In light of the self assessment system, the professional bodies seek clarification from the IRB on this matter.

Jawapan.

LHDN memaklumkan bahawa kedua-dua isu yang dibangkitkan oleh persatuan akauntan tertakluk kepada dua prinsip percukaian yang berbeza. Sekiranya kenderaan tersebut digunakan bagi tujuan persendirian, perbelanjaan yang dituntut bukanlah "kesemuanya dan semata-mata dalam menghasilkan pendapatan kasar" dan oleh itu ia

bukanlah satu perbelanjaan yang dibenarkan sebagai potongan dalam mengira pendapatan bercukai syarikat tersebut. Sebaliknya, sekiranya seorang pengarah atau pekerja syarikat (termasuk syarikat terkawal) disediakan sebuah kereta bersama petrol yang digunakan bukan sahaja untuk perniagaan malahan juga bagi tujuan persendirian, maka kereta tersebut adalah suatu manfaat dan dikenakan cukai di bawah Seksyen 13(1)(b). Tiada peruntukan di dalam Akta yang mengatakan bahawa sekiranya syarikat telah membayar cukai ke atas kegunaan kereta persendirian, pekerjanya tidak boleh dikenakan cukai di atas jumlah yang sama.

8. <u>Paragraph 71, Schedule 3 of the ITA</u>

(i) Pursuant to Paragraph 71, Schedule 3 of the ITA, the Director General of Inland Revenue (DGIR) may withdraw any allowance and impose a balancing charge to an asset which was owned by a person for a period of less than two years. We understand that in a reply to an inquiry made to the then DGIR (Mr S Sundaram), he confirmed in his letter dated 14 July 1969 (reference no.:HQ/594/mss) as follows:

"I confirm that the paragraph will not be applied in the normal case of a bona fide sale to a third party of an asset which has been disposed off because it was unsuitable or no longer required for the purpose of the business.

On the other hand, paragraph 71 will be applied in a case such as prestige car owned by a company for use of a director or by a self-employed professional person where an attempt at tax avoidance is evident.

In view of the above, in the recent dialogue with the Operations Division of the IRB on 15 April 2002, it was confirmed that the stand taken by Mr S Sundaram was still in practice, and that Paragraph 71 would not be applicable to a bona fide disposal of assets. On the other hand, Paragraph 71 would only be applicable on the disposal of luxury assets.

The professional bodies would like the Technical Division of the IRB to reconfirm the views of the Operations Division of the IRB.

(ii) Paragraph 71 of Schedule 3 of the ITA states that "*where a person has incurred qualifying expenditure in relation to an asset which is owned by that person for a period of* ***less than two years..."***.

We understand that recently, members of the professional bodies had encountered situations whereby different interpretations on the term 'two years' were used by different IRB officers (i.e. some officers interpret 'two years' as being two years of assessment, while some officers interpret 'two years' as being two calendar years based on the exact number of days).

In view of the self assessment system, the professional bodies would appreciate it if the IRB could provide a clarification on this matter.

Jawapan.

(i) ***LHDN mengesahkan bahawa kedudukan tersebut masih tidak berubah.***

(ii) ***Perkataan "dua tahun" merujuk kepada dua tahun kalendar berasaskan kepada bilangan hari sebenar.***

9. Pioneer Status Incentive - Determination of Production Day

A company would normally assume a particular production day (for the purpose of the Pioneer Status Incentive) based on the relevant known criteria and subsequently prepares/submits its tax return on this basis while waiting for MIDA to notify the company of the actual production day. However, subsequent to the filing of the tax return, if MIDA specifies a later production day which results in a higher tax liability, we are of the opinion that penalties should not be imposed and that the company should be allowed to revise its tax return since at the time the tax return was filed, MIDA had yet to come out with a confirmation on the production day of the company.

The professional bodies would like the IRB to confirm that no penalty would be imposed and that the company would be allowed to revise its tax return under such circumstances.

Jawapan.

MITI akan menentukan "hari pengeluaran" apabila syarikat telah memenuhi kriteria yang ditentukan dan telah mengemukakan akaun beraudit mereka. Kriteria tersebut akan dimaklumkan kepada syarikat apabila permohonan berkaitan insentif telah diluluskan.

Sekiranya syarikat telah memenuhi semua syarat yang diperlukan, sijil taraf perintis akan dikeluarkan (yang menganduangi tarikh "hari pengeluaran") dalam tempoh kurang dari satu bulan.

Dimana syarikat telah menyediakan akaunnya berdasarkan "hari pengeluaran" yang telah ditentukan dan didapati tarikh "hari pengeluaran" yang ditentukan oleh MITI adalah satu tarikh yang terkemudian, tiada penalti akan dikenakan.

Walau bagaimanapun penalti akan dikenakan sekiranya syarikat membuat tuntutan palsu atau gagal mengemukakan sebarang bukti yang menyokong tuntutan mereka.

10. Insurance Companies - Actuarial Surplus Arising / Transferred

From years of assessment 1995 to 1998, any actuarial surplus arising to insurance companies was taxable on an 'arising' basis. However, with effect from year of assessment 1999, we understand that this treatment was changed and actuarial surpluses are only taxable as and when they are transferred. Since an actuarial surplus may have been taxed prior to year of assessment 1999 when it initially arose, and it may be taxed again subsequent to year of assessment 1999 when it is later transferred, this would result in the actuarial surplus being taxed twice. Please refer to the example set out below :

		Amount RM
YA 1995	Balance as at 1 January 1994	NIL
	Add : Actuarial surplus arising for YA 1995	6,803,201
YA 1996	Balance as at 1 January 1995	6,803,021
	Add : Actuarial surplus arising for YA 1996	6,846,401
YA 1997	Balance as at 1 January 1996	13,649,422
	Add : Actuarial surplus arising for YA 1997	4,513,065
YA 1998	Balance as at 1 January 1997	18,162,487
	Add : Actuarial surplus arising for YA 1998	22,594,771
		40,757,258
	Less : Actuarial surplus transferred	(4,000,000)
YA 1999	Balance as at 1 January 1998	36,757,258
	Less : Actuarial surplus transferred	(6,000,000)
YA 2000 (PYB)	Balance as at 1 January 1999	30,757,258
	Less : Actuarial surplus transferred	(4,000,000)

YA 2000 (CYB)	Balance as at 1 January 2000	26,757,258
	Less : Actuarial surplus transferred	(8,000,000)
YA 2001	Balance as at 1 January 2001	18,757,258

Total actuarial surplus that arose in YA 1995 to 1998 = RM40,757,258
Total actuarial surplus that was transferred in YA 1999 to 2001 = RM 18,000,000

The actuarial surplus transferred arose from the brought forward balance which has already been taxed in accordance with the legislative provision from YA 1995 to 1998. Therefore, to assess the amounts transferred of RM18,000,000 leads to double taxation.

The professional bodies would like the IRB to confirm that no double taxation would arise on actuarial surplus which was already taxed prior to year of assessment 1999.

Jawapan.

LHDN mengesahkan bahawa isu di atas adalah berkaitan dengan polisi dan telah dirujuk kepada Kementerian Kewangan untuk pertimbangan.

11. Paragraph 62, Schedule 3 of the ITA

Some companies write off their fixed assets in the following circumstances:

(i) although the assets may be usable, they have no resale value due to their condition.

(ii) the assets are obsolete or in disrepair, and are discarded as it is not cost effective to upgrade or repair the assets.

(iii) the assets are no longer in existence as they have been discarded due to wear and tear or cannibalized for the repair of other similar assets or are lost.

Normally, such assets have no market value or disposal value. However, we understand that some IRB officers have been applying the provisions of paragraph 62 of Schedule 3 of the ITA, to disallow claims for balancing allowance on the write off of these assets. Paragraph 62 states that where an asset is disposed off, its disposal value shall be taken to be its market value at the date of disposal. We understand that IRB officers have adopted the stand that the market values of these assets are deemed to be equal to their tax written down values.

The professional bodies would like to request the IRB to give due consideration to the circumstances in which an asset is written off in determining claims for balancing allowance. The professional bodies would also like to suggest that the IRB provide guidelines on the type of supporting documentation required when making the claims for balancing allowance.

Jawapan.

LHDN mengesahkan bahawa kaedah berikut boleh digunakan untuk menentukan nilai pasaran aset semasa ianya dilupuskan/dihapuskira bagi tujuan tuntutan elaun imbangan/kenaan imbangan :-

- ***i	tuntutan insuran; atau***
- ***Ii.	penilaian oleh badan penilai bebas.***

Kaedah di atas boleh digunakan bagi menentukan nilai pasaran aset yang besar seperti mesin kilang dan sebagainya.

Walau bagaimanapun bagi aset yang bernilai rendah (seperti kerusi, meja dsb.) kaedah di atas tidak perlu.

***Catatan :	Sebarang hapuskira bagi aset-aset yang bernilai rendah boleh diterima. Oleh itu elaun imbangan yang dituntut boleh dibenarkan.***

12. Capital Expenditure of Nominal Value

Pursuant to Public Ruling 2/2001, expenditure on assets that have an expected life span of not more than 2 years (implements, utensils and articles) is to be dealt with on a replacement basis in which the cost of replacing such assets is to be allowed as deductible expenditure under Section 33(1)(c) in determining the adjusted income of the business.

However, it is noted that some companies have a policy of writing off of capital expenditure incurred below a certain nominal amount (depending on the policy adopted) to the profit and loss accounts. These items may have an expected life span of more than 2 years and hence, do not fall under the criteria stipulated in the Public Ruling 2/2001. However, in light of the self assessment regime, we are of the opinion that, in administering the law, the IRB should take into consideration the ways in which businesses are being operated and that there should be some form of harmonisation between accounting treatment and tax treatment.

Since the issue here merely involves the deferment of income rather than the loss of income to the IRB, we are of the opinion that the IRB should allow companies to claim an outright deduction of this type of capital expenditure based on the accounting policy adopted by the companies. This will also make it easier to prepare tax computations and thus, assist in lowering compliance costs.

Jawapan.

LHDN memaklumkan bahawa pada masa ini ia tidak bersetuju dengan layanan sedemikian dan meminta badan profesional untuk membuat pengemukaan ke Kementerian Kewangan.

13. <u>Reinvestment Allowance (RA)</u>

We would like the IRB to confirm that if a company wishes to revise its tax payable by claiming RA on capital expenditure incurred in prior years, the company may do so by revising its tax returns submitted earlier pursuant to Section 131 of the ITA (i.e. for relief in respect of error or mistake) without any penalty being imposed.

Jawapan.

Persatuan akauntan dimaklumkan bahawa tiada penalti akan dikenakan dalam keadaan tersebut.

14. <u>Section 113(2) of the ITA</u>

We are of the opinion that, as a matter of principle, penalties should not be imposed on technical adjustments made on tax computations prior to YA 2001 (i.e. prior to the implementation of the self assessment system). However, some members had encountered situations whereby a tax deduction which was initially claimed on repairs and maintenance was later reclassified as capital expenditure by the IRB subsequent to a field audit. We understand that a penalty under Section 113(2) was imposed by the IRB in such a situation.

Prior to the implementation of the self assessment system (i.e. prior to YA 2001), as the onus of determining the taxpayer's tax liability lies with the IRB, it has been the practice of the IRB in the past not to impose penalties on technical adjustments made subsequent to a field audit by the IRB.

However, we understand that some IRB officers have recently deviated from this past practice by imposing penalties on technical adjustments made subsequent to a field audit by the IRB on tax computations prior to YA 2001. We are of the opinion that penalties should not be imposed on technical adjustments made on tax computations prior to YA 2001 and we are also of the view that there should be some guidance given to all IRB officers on how tax audits should be conducted with regard to tax computations prior to YA 2001.

Jawapan.

Pelarasan teknikal biasanya timbul disebabkan perbezaan interpretasi perundangan percukaian oleh pembayar cukai. Ianya berlaku disebabkan oleh sesuatu peruntukan yang tidak jelas atau disebabkan wujudnya undang-undang yang berbeza.

Persatuan akauntan dimaklumkan bahawa penalti tidak akan dikenakan dalam keadaan pelarasan teknikal sebenar yang bukan bertujuan untuk pelarian cukai.

Walau bagaimanapun, samada sesuatu transaksi itu adalah pelarasan teknikal sebenar ataupun percubaan pelarian cukai adalah bergantung kepada fakta sesuatu kes.

Mesyuarat mencadangkan supaya dialog diadakan secara berasingan dengan Bahagian Audit Cukai bagi membincangkan masalah ini.

Tindakan : Bahagian Audit Cukai

15. Interest Income Assessable Either Under S.4(a) or S.4(c) of the ITA

Some companies are required to place funds in fixed deposits as a guarantee in order to obtain banking facilities used for **business purposes** (and not for investment purposes). We are of the opinion that the interest income form the fixed deposits derived therefrom should be assessable as part of the business source under S.4(a) instead of as a non-business source under S.4(c) of the ITA. However, we understand that different IRB officers have been taking different views on the treatment of this particular income.

The professional bodies wish to seek confirmation from the IRB that the interest income derived from funds placed in fixed deposits as a guarantee in order to obtain banking facilities used for **business purposes** (and not for investment purposes) should be assessable as business source under S.4(a) instead of non-business source under S.4(c) of the ITA. In considering this issue, the IRB should take into consideration the fact that nowadays, there are various circumstances where companies are required by certain authorities to place funds in fixed deposits that generate interest income in order to obtain facilities (or even contracts for contractors) for business purposes (and not investment purposes).

Jawapan.

LHDN mengambil maklum tentang pandangan badan profesional bahawa amalan perniagaan pada masa ini menyebabkan institusi kewangan mewajibkan sesebuah syarikat mengadakan simpanan tetap yang akan digunakan sebagai deposit sekuriti (kolateral) sebelum sesuatu pinjaman boleh diluluskan dan pinjaman ini digunakan bagi tujuan modal kerja

perniagaannya. Oleh itu faedah yang diterima sepatutnya tidak dianggap sebagai pendapatan bukan perniagaan.

Walau bagaimanapun, LHDN masih berpendapat bahawa faedah yang timbul dari simpanan tetap ini adalah merupakan pendapatan bukan perniagaan dan oleh itu tertakluk kepada cukai di bawah Seksyen 4(c).

16. Definition of Entertainment to Exclude Advertising and Promotion

Pursuant to Section 39 of the ITA, entertainment is defined to include:

(a) the provision of food, drink, recreation or hospitality of any kind; and

(b) the provision of accommodation or travel in connection with or for the purpose of facilitating entertainment of the kind mentioned in (a) above.

Since the introduction of the non-deductibility of entertainment expenses, we note that the IRB has adopted a wide interpretation of entertainment, with the result that certain advertising or promotion expenses incurred for the purposes of business have been regarded as entertainment, and not allowed as a tax deduction. With effect from year of assessment 1995, the Act was amended to exclude from the definition of entertainment, promotional gifts consisting of articles incorporating the conspicuous advertisement or logo of the company. (However, the Act is silent on the tax deductibility of advertising and promotion expenses.)

Non-deductibility of certain advertising and promotion expenses has increased the cost of operating a business for companies, as these expenses are usually incurred to increase the sales of products or services, for example:

(i) provision of incentives (e.g. local/overseas trips) to dealers/salesmen who meet sales targets;

(ii) promotional events at public venues to launch or provide new products or services.

We are of the opinion that the expenses incurred on advertising and promotion with the intention to improve the company’s profile and promote its products and services should not be regarded as entertainment.

The professional bodies would also like to suggest that the IRB issue a public ruling to specify the scope of entertainment expenses and examples of the types of entertainment expenses that are not allowable.

Jawapan.

Persatuan akauntan dimaklumkan bahawa perbelanjaan “promosi dan pengiklanan” biasanya dilakukan bagi tujuan mempromosikan sesebuah

perniagaan boleh dibenarkan di bawah Seksyen 33(1) Akta Cukai Pendapatan 1967.

Berkaitan isu "keraian" pula, LHDN mempersoalkan tentang beberapa perbelanjaan "promosi" yang dilakukan oleh pembayar cukai (seperti insentif perjalanan, produk percuma yang tidak berkaitan, dsb.) yang lebih merupakan perbelanjaan keraian.

Selaras dengan Sistem Taksiran Sendiri dan keperluan untuk memperjelaskan isu ini, LHDN memaklumkan bahawa ia akan mengeluarkan satu ketetapan umum berkaitan isu ini.

LHDN selanjutnya meminta kerjasama badan profesional untuk membantu menyenaraikan jenis perbelanjaan promosi yang biasanya di lakukan oleh pembayar cukai.

17. Draft Public Rulings

The IRB had in November 2000 issued draft public rulings on the following subjects for comment:

(i) allowable pre-operational and pre-commencement of business expenses for companies; and

(ii) rent from letting of real properties.

The professional bodies would appreciate it if the IRB could advise on the status of these public rulings.

Jawapan.

LHDN memaklumkan bahawa ketetapan umum bagi item (i) telah dikeluarkan manakala ketetapan umum bagi item (ii) masih dalam peringkat akhir penyediaan.

18. Tax Incentives to Increase Export of Services

In the previous dialogue held with the Technical Division of the IRB on 13 November 2001, the IRB had clarified that qualifying services which relate to the above incentive are:

(i) private health care and education services that are undertaken within Malaysia, (i.e. the patients and students would be coming to Malaysia from outside Malaysia); and

(ii) as for other services (i.e. legal, accounting, etc.) the incentive will apply if such services are performed outside Malaysia.

Subsequent to the dialogue, the Income Tax (Exemption) (No. 9) Order 2002 (the Order) was issued in January 2002. The Order defines qualifying services as services which are provided to foreign clients, from Malaysia, and in relation to the provision of private health care and private education, the services to be provided to foreign clients are to be provided either in Malaysia, or provided from Malaysia.

The professional bodies would like to seek clarification on the following matters:

(i) With regard to private health care and education services, the Order defines qualifying private health care and education services as services provided to foreign clients which are to be provided either in Malaysia, or provided from Malaysia. In this regard, the professional bodies would like to seek clarification on the distinction between the term "in Malaysia" and the term "from Malaysia";

(ii) With regard to services other than private health care and education services (i.e. legal, accounting, etc.), contrary to the stand taken by the IRB during the previous dialogue (i.e. Services must be performed *outside* Malaysia), the Order defines qualifying services as services which are provided to foreign clients *from* Malaysia. In this regard, the professional bodies would like to seek clarification on this discrepancy;

Jawapan.

Persatuan akauntan dimaklumkan maksud perkataan :-

(a) "dalam Malaysia" bermaksud perkhidmatan tersebut dilakukan di Malaysia. Sebagai contoh, seorang pelanggan luar negara mendapatkan rawatan perubatan dan telah dimasukkan di hospital swasta di Malaysia atau seorang pelajar luar negara sedang mengikuti kursus di institusi pendidikan swasta di Malaysia;

(b) "dari Malaysia" pula bermaksud, perkhidmatan tersebut dilakukan di Malaysia oleh seseorang di Malaysia kepada pelanggan diluar Malaysia melalui internet/pelajaran jarak jauh atau surat-menyurat dan sebagainya.

(c) "perkhidmatan dilakukan di luar Malaysia" mestilah berkaitan dengan sebarang kontrak untuk mengeksport perkhidmatan dari seseorang di Malaysia kepada pelangan luar negara sekiranya kontrak tersebut memerlukan perkhidmatan tersebut dilakukan di luar negara.

(iii) Would there be a prescribed form to be issued by the IRB?

The professional bodies would also like to suggest that the IRB issue a guideline to assist taxpayers in the application of the above incentive.

LHDN memaklumkan bahawa borang khas (Borang BT/PET/2002) telah dikeluarkan.

19. Approved Operational Headquarters Company

Income tax is charged at the rate of 10% on the chargeable income of an approved operational headquarters company in relation to the source consisting of the provision of qualifying services. The professional bodies would like to seek the IRB's confirmation that the tax charged for the years of assessment prior to YA 2001, as well as the tax paid in YA 2001 and subsequent years, can be included as part of the Section 108 credit (compared aggregate).

Jawapan

LHDN memaklumkan bahawa cukai yang telah dibayar tersebut boleh diambil kira dalam pengiraan kredit Seksyen 108.

20. Segregation of Expenses for Business and Non-Business Purposes

We understand that under the self assessment regime, taxpayers are required to identify and segregate expenses incurred for business and non-business purposes. However, we note practical problems have been encountered by small businesses in complying with this requirement.

Illustration

A single mother rents a shop floor for the purpose of carrying on a business and she also lives at the premises with her children. She has a car which is used for both business and domestic purposes.

Practical difficulty is encountered in segregating the expenses incurred for business and non-business purposes, such as the following :

(i) Utility Bills and Rental

Should the allocation of the expenses incurred be based on floor area utilisation or the duration of usage (i.e. business hours vs non-business hours)?

(ii) Car Expenses

Should the allocation of the expenses be based on mileage or hours of usage of the car? It is quite normal that the taxpayer may drop off her children at school on the way to a business appointment.

The professional bodies would like to propose that for practical reasons, the allocation of expenses for business and non-business purposes be based on a justifiable ratio rather than a detailed computation for each item.

Jawapan

Persatuan akauntan dimaklumkan bahawa LHDN bersedia menerima sebarang jumlah yang berasaskan kepada asas pembahagian yang munasabah dan konsisten.

Sebagai contoh dalam kes di mana separuh masa dari penggunaan kereta digunakan bagi tujuan perniagaan dan sebahagian lagi untuk persendirian, maka asas pembahagian yang munasabah berkaitan perbelanjaan (seperti minyak, penyelangaraan dsb.) adalah 50%.

21. **<u>Basis Period for Unit Trust Entities</u>**

The professional bodies are of the opinion that for practical purposes, it may be more sensible if the tax computations prepared prior to year 2004 are prepared based on the financial year as the basis period for a particular year of assessment, so that it is in line with the basis stipulated in the Income Tax (Amendment) Bill 2001 (i.e. preparation of tax computations based on financial year). Please refer to item 9 of “Our Comments on the Income Tax (Amendment) Bill 2001” for our detailed comment on this matter.

Jawapan.

Persatuan akauntan dimaklumkan bahawa sebagai satu konsessi, LHDN bersetuju supaya pengiraan cukai bagi unit amanah dibenarkan mengikut tahun kewangan sebagai tahun asasnya dengan syarat ianya digunakan secara konsisten.

OUTSTANDING ISSUES

The following issues were raised in the earlier dialogues with the Technical Division of the IRB which have not been resolved:

1. **Investment Holding Companies**

   (25 August 2000 Dialogue refers)

   Pursuant to Section 60F of the ITA, a company whose activities consist **wholly** of making and deriving income from investments, is an investment holding company (IHC).

   Nonetheless, recently there have been situations whereby the IRB have treated a company having both management services and investment holding activities as an IHC under Section 60F. The IRB have instead allowed a deduction of expenses up to the amount of management fee income earned.

   The professional bodies wish to clarify with the IRB that in the event that a company is having both management activities and investment holding activities (i.e. the company is not one whose activities consist **wholly** of making investments), the company is not an IHC under Section 60F but is carrying on a business activity as per Section 4(a) of the ITA instead, and therefore deduction of expenses should not be restricted up to the amount of management fee income earned.

   The professional bodies are still awaiting clarification from the IRB on the above matter.

   Jawapan.

   LHDN telah memaklumkan bahawa penentuan layanan cukai adalah berasaskan kepada fakta sesuatu kes.

2. **Deduction on Cost for Developing Websites**

   (13 November 2001 Dialogue refers)

   As an effort to encourage the usage of information and communication technology, an annual deduction of 20% is allowed on the cost of developing websites.

   The professional bodies would like to seek clarification on the type of costs that would qualify for such deduction as currently the cost of developing a website would include expenditure on computer hardware and software, which would normally be eligible for capital allowances of 40%.

Alternatively, the professional bodies would like to recommend that instead of identifying the expenditure incurred on the development of a website (other than computer hardware and software) and allowing a 20% annual deduction, the IRB should consider the total development cost of a website as being eligible for the same capital allowance rate as that for computer hardware and software.

The professional bodies are still awaiting clarification from the IRB on the above matter.

Jawapan.

LHDN memaklumkan bahawa pada masa ini kos perkakasan dan perisian layak mendapat elaun modal dipercepatkan. Kos untuk membangunkan laman web selain dari kos ke atas perkakasan dan perisian akan dipertimbangkan di dalam kaedah yang akan dikeluarkan kelak iaitu pada kadar 20% potongan tahunan.