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Greetings from Deloitte Malaysia Tax Services

Public Rulings (PRs)

PR No. 1/2017: Income Tax Treatment of GST Part I – Expenses

The Inland Revenue Board (IRB) has issued PR No. 1/2017: Income Tax Treatment of GST Part I – Expenses on 8 June 2017. Among the issues covered are:

- Deductibility of input tax under the Income Tax Act 1967 (the ITA);
- Deductibility of output tax borne by registered person on deemed supplies;
- Reverse charge mechanism for imported services; and
- Bad debt relief

Quick links:

[Deloitte Malaysia](#)
[Inland Revenue Board](#)

Takeaways:

Public Rulings (PRs)

PR No. 1/2017: Income Tax Treatment of GST Part I – Expenses

PR No. 2/2017: Income Tax Treatment of GST Part II – Qualifying Expenditure for Purposes of Claiming Allowances

IRB's Practice Notes No. 1/2017 and No. 2/2017

New Tax Treaty /
Changes in Tax Treaty

Malaysia-Slovak
Republic Tax Treaty

The Third Protocol to
the Tax Treaty with
New Zealand

PR No. 2/2017: Income Tax Treatment of GST Part II – Qualifying Expenditure for Purposes of Claiming Allowances

The IRB released PR No. 2/2017 on 6 June 2017 to explain the income tax treatment of GST paid or to be paid on the purchase or acquisition of capital asset for the purpose of claiming allowances. Among the issues covered are:

- Income Tax Treatment of GST Incurred on the Acquisition of Capital Assets and Qualifying Expenditure
- Income Tax Adjustment in relation to Capital Goods Adjustment

Tax Cases

Ketua Pengarah Hasil Dalam Negeri (KPHDN) v United Malacca Berhad (High Court)

Insaf Tegas Sdn Bhd v KPHDN (High Court)

Upcoming events

[Real Estate Industry Taxation Workshop – Module 3](#)

Important deadlines:

Due date for 2018 tax estimates for companies with August year-end (1 August 2017)

6th month revision of tax estimates for companies with January year-end (31 July 2017)

9th month revision of tax estimates for companies with October year-end (31 July 2017)

Statutory filing of 2016 tax returns for companies with December year-end (31 July 2017)

IRB's Practice Notes No. 1/2017 and No. 2/2017

The IRB has issued the Practice Note No. 1/2017 as a guide to the newly amended Section 15A of the ITA with the deletion of the proviso by the Finance Act 2017. Essentially the effective date of 17 January 2017 for the amendment to the ITA refers to the date services are performed, except where payment for services has been made before this date, as shown below:

Service performed outside Malaysia	Payment made	Withholding tax
< 17 Jan 2017	< 17 Jan 2017	X
< 17 Jan 2017	≥ 17 Jan 2017	X
≥ 17 Jan 2017	< 17 Jan 2017	X
≥ 17 Jan 2017	≥ 17 Jan 2017	√

With the re-imposition of withholding tax on offshore services under the amended Section 15A, the IRB has also in a separate Practice Note No. 2/2017 confirmed that the Double Taxation Agreement with other countries will prevail as follows:

Contracting States	Implication
Singapore	Payment for services performed outside Malaysia are not subject to withholding tax.
Spain	
Australia	Payments for services are not subject to withholding tax.
Turkmenistan	

Please note that the Double Taxation Agreement is only applicable if the payee is a resident of the other contracting state.

New Tax Treaty / Changes in Tax Treaty

Malaysia-Slovak Republic Tax Treaty

The Double Taxation Avoidance Agreement (Tax Treaty) signed between Malaysia and the Slovak Republic entered into force on 14 March 2016 and is effective on 1 January 2017.

Snapshot

Nature of income	Normal Withholding Tax (Malaysia)	Treaty Rate
Dividends	Nil	0%* / 5%
Interest	15%	10%
Royalties	10%	10%
Technical Fees	10%	5%

*Only applicable where the beneficiary of the dividend payment is a company (other than partnership) that directly owns a minimum of 10 per cent of the capital of the paying company for 12 continuous months.

The Third Protocol to the Tax Treaty with New Zealand

The IRB has updated its "Double Taxation Agreement" webpage to reflect that the Third Protocol to the Tax Treaty between Malaysia and New Zealand had entered into force on 12 January 2016 and is effective on 1 January 2017. The Third Protocol serves to replace the information exchange clause contained in the Tax Treaty between Malaysia and New Zealand.

Tax Cases

Ketua Pengarah Hasil Dalam Negeri (KPHDN) v United Malacca Berhad (High Court)

Issues:

1. Whether the taxpayer is taxable on the receipts of late payment charges arising from a compulsory land acquisition; and

2. Whether the taxpayer is taxable on the reimbursement of staff retrenchment benefits paid to its employees who had then been working on the land.

Decision:

The High Court dismissed the appeal by the IRB on all issues with the following grounds of judgement [*The IRB has thereon agreed not to appeal to the Court of Appeal on the abovementioned issues*]:

1. Following a litigation in which the taxpayer had objected to and litigated against the compensated amount for the compulsory acquisition of the taxpayer's land awarded by the Land Administrator, the taxpayer was awarded with additional compensation and "late payment charges" in relation to the late payment of the additional compensation. In deciding as to whether those "late payment charges" were chargeable to income tax, the High Court held that the purpose of the "late payment charges" received by the taxpayer was to account for the accretion to capital of the value of the compulsorily acquired land between the time the land was acquired and the time additional compensation was paid. Thus the "late payment charges" would be capital in nature as the true character of the charges depends on the nature of the underlying debt, obligation or asset. The fact that the "late payment charges" were expressed or calculated as a percentage of the principal value does not mean that those charges were of income nature.
2. The reimbursement of retrenchment benefits by the Land Administrator was not in the nature of "income" as it was simply a payment for actual expenditure incurred to make the recipient whole, i.e., the taxpayer was merely being repaid the amount of an expenditure that had been incurred as a necessary consequence of the compulsory acquisition. Based on the true construction of Section 22(2) of the ITA, a reimbursement would only be taxable as income in the hands of a taxpayer if the amount reimbursed had been deducted when determining gross income. The taxpayer had not claimed the amount as a deduction in the year of assessment in which the retrenchment benefits were paid, hence the reimbursement thereof is not an income taxable on the taxpayer.

Insaf Tegas Sdn Bhd v KPHDN (High Court)

Issues:

1. Whether the taxpayer's disposal of land constituted a disposal of capital investment or stock in trade; and
2. Whether the IRB had correctly exercised its discretion to impose a penalty pursuant to Section 113(2) of the ITA.

The High Court dismissed the appeal by taxpayer on both the issues with the following grounds of judgement:

Issue 1

The High Court found that the transaction undertaken by the taxpayer, whose principal activity was property investment, was a disposal of its stock in trade and not capital investment. The taxpayer's intention at the time of purchase of the land was to develop the land for profit, not for permanent investment.

This was regardless of the fact that (1) the IRB had, further to the taxpayer's submission of the return form for Real Property Gains Tax (RPGT), issued an exemption certificate for RPGT; and (2) the taxpayer's contention that the disposal of land constituted an investment as the six badges of trade (i.e., namely subject matter of the transaction, period of ownership, frequency of transaction, alteration of property, methods and, circumstances of property disposal) were not present.

The High Court decided that the taxpayer's intention to develop the land for profit which existed since the acquisition of the land was evident because:

- a) The taxpayer's sale and purchase agreement (SPA) with Ligamas Sdn Bhd to acquire the 50-acre land was consistent with the commercial development of the land. The SPA contained specific conditions requiring the taxpayer's compliance, i.e., the taxpayer was required to submit the building plan within one year of the SPA's execution, indicating the taxpayer's intention to commercially develop the land within two years upon the building plan approval. The taxpayer's memorandum of association had described the taxpayer's business activity as property development allowing the taxpayer to enter into any contract to build buildings and other construction work.
- b) The taxpayer had passed two company resolutions prior and consequent to taxpayer's execution of SPA, i.e., the passing of a resolution for the purchase of the land in anticipation of the SPA and the appointment of a developer, Mixwell (Malaysia) Sdn Bhd consequent to taxpayer's execution of the SPA.

It was also established that the taxpayer's intention of development for profit had only changed following unfavourable market condition and the land was subsequently assigned to a third party due to the taxpayer's debt settlement exercise.

The High Court thereby concluded that the taxpayer, in its appeal, failed to meet the burden of proof test in proving that the IRB's assessment was excessive or erroneous according to Paragraph 13 of the Fifth Schedule of the ITA. The appellant had undisputedly disposed its stock in trade in the course of carrying on its business activity and pursuant to the Section 24(1) of the ITA, tax was chargeable on any gain or profit from taxpayer's disposal.

Issue 2

As the taxpayer was found to have made an incorrect return, it was clear from Section 113(2) of the ITA that the Director General (DG) was given the discretionary power to impose a penalty on an incorrect return filed by the taxpayer. It was regardless of whether the taxpayer's return was made negligently or in good faith, or with intent to deceive or evade tax. The DG, however, was not duty bound to require penalty payment but, to exercise the discretion after due consideration of all relevant facts and circumstances.

We invite you to explore other tax-related information at:

<http://www2.deloitte.com/my/en/services/tax.html>

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