An Analysis of the 2014 Budget

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Introduction

The 2014 Budget was tabled on October 25, 2013 with the main objective of gearing the country to becoming a high-income and developed nation by 2020. Themed as "Strengthening Economic Resilience, Accelerating Transformation and Fulfilling Promises", the Budget emphasises five main thrusts i.e.

- Invigorating economic activity
- Strengthening fiscal management
- Inculcating excellence in human capital
- Intensifying urban and rural development
- Ensuring the well-being of the rakyat

Malaysia's economy has demonstrated its underlying resilience by growing at an expected rate of between 4.5% to 5.0% in 2013 and it is anticipated that a 5.0% to 5.5% growth rate will be achieved in 2014. Growth is expected to come through increase in foreign direct investment, private investment and private and public consumption. However, the level of Government deficit and the recent downgrade by Fitch Ratings have prompted initiatives towards enhanced fiscal management in the near term and fiscal sustainability measures over the longer term. In this respect, the deficit is projected to come down from 4.0% in 2013 to 3.5% in 2014, due to an expected increase in revenue collection by RM4 billion to RM224.1 billion.

Thus, it did not come as a great surprise when the Minister of Finance finally announced the implementation of the Goods & Services Tax ("GST") regime, come April 1, 2015. It is anticipated that GST will contribute significantly towards the revenue tax collection target for 2014 and subsequent years.

Public sector transformation programmes will continue at an increased pace to enhance the effectiveness and efficiency of the public service delivery system. However, the implementation of projects with high import content and low value spin-offs will "be sequenced" in light of declining levels of surplus in the balance of payments current account.

The Services sector has been given greater focus, particularly the logistics, aviation and tourism sectors. Efforts are also being undertaken to promote Malaysia as a centre for origination as well making it a major regional player in Islamic finance.

Apart from those tax reductions, which will be in tandem with the implementation of GST i.e. the reduction in personal and corporate tax rates, the budget proposals contain relatively few tax changes.

Set out below are the highlights of the 2014 Budget announcements covering personal tax, corporate tax, investment incentives, stamp duty, Labuan, petroleum income tax, real property gains tax and GST.

A. PERSONAL TAXATION

REDUCTION IN INCOME TAX RATES AND CHANGE IN INCOME TAX STRUCTURE

Presently, resident individuals are taxed at scale rates ranging from 0% to 26%, with the maximum rate of 26% being applicable to the chargeable income band of RM100,000 and above.

In line with the implementation of the GST regime, it has been 1967.The term derives its meaning from judicial pronouncements An illustration of the corresponding tax savings are tabulated below:

Chargeable income (RM)	Existing rates (%)	Proposed rates (%)	Reduction (%)
1 – 5,000	0	0	-
5,001 – 20,000	2	1	1
20,001 – 35,000	6	5	1
35,001 – 50,000	11	10	1
50,001 – 70,000	19	16	3
70,001 – 100,000	24	21	3
100,001 – 250,000	26	24	2
250,001 – 400,000	26	24.5	1.5
Above 400,000	26	25	1

Chargeable income brackets (RM)		Present tax rate (%)	Proposed tax rate (%)	Present tax payable (RM)	Proposed tax payable (RM)	Tax savings (RM)	Tax savings (%)
On the first	5,000	0	0	0	0	0	0
On the next	5,000	2	1	100	50	50	50.0
On the first	10,000			100	50	50	50.0
On the next	10,000	2	1	200	100	100	50.0
On the first	20,000			300	150	150	50.0
On the next	15,000	6	5	900	750	150	16.7
On the first	35,000			1,200	900	300	25.0
On the next	15,000	11	10	1,650	1,500	150	9.1
On the first	50,000			2,850	2,400	450	15.8
On the next	20,000	19	16	3,800	3,200	600	15.8
On the first	70,000			6,650	5,600	1,050	15.8
On the next	30,000	24	21	7,200	6,300	900	12.5
On the first	100,000			13,850	11,900	1,950	14.1
On the next	150,000	26	24	39,000	36,000	3,000	7.7
On the first	250,000			52,850	47,900	4,950	9.4
On the next	150,000	26	24.5	39,000	36,750	2,250	5.8
On the first	400,000			91,850	84,650	7,200	7.8
Exceeding	400,000	26	25				

It is also proposed that non-resident individuals' income tax rate be reduced by 1% from 26% to 25%.

These proposals shall take effect from the year of assessment 2015.

MONTHLY TAX DEDUCTION AS FINAL TAX

Monthly Tax Deduction (MTD) is a mechanism to deduct monthly tax payments on employment income received by employees in the current year. Employers are responsible to remit MTD to the Inland Revenue Board (IRB) every month as provided under the Income Tax (Deduction from Remuneration) Rules 1994.

The amount of MTD is based on the prescribed Rules and takes into account a deduction for the following: -

- Personal relief
- Relief for spouse with no income
- Child relief
- Contributions to the Employees Provident Fund (EPF)
- Other approved schemes e.g. zakat

Nevertheless, the employees may make an irrevocable election to request their employers to deduct other optional deductions allowable under the Income Tax Act 1967 (“the Act”), in ensuring that the MTD payments are equal to the total final tax payable.

Employees are required to submit tax returns to the IRB on or before 30 April in the following year and any balance of tax payable needs to be paid by the due date.

For ease of administration, it is proposed that employees whose total income tax is equivalent to the amount of MTD deducted throughout the year need not submit the annual income tax returns. This will render the amount of MTD as the final tax paid. The exemption from filing a tax return is only applicable to:

(i) employees who receive employment income prescribed under Sections 13(1)(a), (d) and (e) of the Act;
(ii) employees whose MTD are made under Section 107(2) of the Act and the Income Tax (Deduction from Remuneration) Rules 1994;
(iii) employees serving under the same employer for a period of 12 months in that year of assessment;
(iv) employees whose MTD are not borne by the employer for that year of assessment; and
(v) employees who have not elected for joint assessment under Section 45 of the Act.

Where an employee meets the above conditions and no return for that year of assessment has been furnished by that employee, it is proposed that:

(i) the employee is deemed to have made an election not to file a return;
(ii) the total amount of MTD deducted shall be deemed to be the tax payable of the employee for that year of assessment; and
(iii) Director General shall not make an assessment in respect of the employee for that year of assessment.

However, the Director General retains the power to raise a deemed assessment or an additional assessment and in such a case, the total amount of MTD deducted deemed as the final tax payable for that year of assessment shall be disregarded.

The above proposal takes effect from the year of assessment 2014.

SPECIAL TAX RELIEF FOR MIDDLE INCOME TAXPAYERS

Presently, the following rebates are given to resident taxpayers: -

- RM400 for taxpayers with chargeable income up to RM35,000 and an additional RM400 for the spouse; and
- The amount equivalent to zakat contributions by Muslim taxpayers

In an effort to alleviate the financial burden of middle income taxpayers, it is proposed that a special once-off tax relief of RM2,000 be given to resident middle income taxpayers earning up to RM8,000 a month (aggregate income of up to RM96,000 per annum). This would translate into tax savings of up to RM480 after deduction of this special relief from the aggregate income.

The proposal is effective for the year of assessment 2013 only.

1MALAYSIA PENSION SCHEME (SP1M)

In 2010, the Government established the 1Malaysia Pension Scheme (SP1M) for the self-employed without fixed income to contribute voluntarily to the Employees Provident Fund (EPF). Under SP1M, the Government makes a contribution of 5% of the amount contributed by the self-employed, subject to a maximum of RM60 per year.

To encourage more self-employed individuals to participate in the scheme to save for their retirement, it is proposed that the Government increases its contribution from 5% to 10% (i.e. from a maximum of RM60 to RM120 per year).

The proposal is effective from January 1, 2014 to December 31, 2017.

INCENTIVE ON PRIVATE RETIREMENT SCHEME

Presently, a maximum relief of RM3,000 is given for contributions made to a Private Retirement Scheme (PRS) or deferred annuity scheme. The PRS is required to be approved by the Securities Commission.

It is proposed that individuals be given a one-off incentive of RM500 if the individual participating in the PRS meets the following criteria:

(a) has a minimum cumulative investment of RM1,000 within a year; and
(b) is between 20 to 30 years old.

This proposal takes effect from January 1, 2014 to December 31, 2018 and is aimed at encouraging youths within the age group to save for their retirement.

TAXABILITY OF WITHDRAWAL FROM A DEFERRED ANNUITY SCHEME

Presently, any withdrawal from a deferred annuity scheme is not subject to tax. In an effort to encourage contributors to retain their savings for retirement, it has been proposed that withdrawal from a deferred annuity scheme before the contributor attains the age of 55 (other than reasons of permanent total disablement, serious disease, mental disability, death or permanent departure from Malaysia), will be taxed at a rate of 8%. In this context, deferred annuity refers to schemes contracted on or after 1 January 2014 and such schemes must be issued by:

(i) insurers licensed under the Financial Services Act 2013; or
(ii) takaful operators registered under the Islamic Financial Services Act 2013 and contain the Retirement Saving Standards approved by Bank Negara Malaysia.

The same tax treatment will apply for withdrawals made from Private Retirement Schemes.

This proposal shall be effective from January 1, 2014.

B. CORPORATE TAXATION

GAINS OR PROFITS FROM A BUSINESS ARISING FROM STOCK IN TRADE PARTED WITH BY ANY ELEMENT OF COMPULSION

Section 24(1)(a) provides that any stock in trade sold (or parted with on requisition or compulsory acquisition or in a similar manner) would be treated as business income subject to tax.

However, the Courts have ruled in several tax cases that income received pursuant to a compulsory acquisition should not be subject to income case. In the case of *Penang Realty Sdn Bhd v KPHDN (2006) MSTC 4206*, the Court of Appeal ruled that the compulsory acquisition of a taxpayer's land by the Government could not constitute a sale and the compensation received was not subject to income tax as the element of compulsion essentially vitiated the intention to trade as established in the Supreme Court decision of *Lower Perak Cooperative Housing Society Bhd v KPHDN (1994) 2 MSTC 3,406*. In another case of *Metacorp Development Sdn Bhd v KPHDN (2011) MSTC 30-024*, the High Court in a judicial review application by Metacorp on a similar point ruled that the failure of the DGIR to follow the decision of the superior courts rendered its decision defective as the two cases were binding on the DGIR.

It is proposed that a new Section 4C be introduced to clarify that any amounts that are receivable by a person from the disposal of its stock in trade including such amounts arising from any element of compulsion such as a compulsory acquisition or forced sale are to be treated as gains or profits from a business.

In conjunction with the introduction of the new Section 4C, the amended Section 24(1)(a) and new Section 24(1)(aa) provide that any debt owing to a person arising in respect of stock in trade parted with by any element of compulsion including on requisition or compulsory acquisition or in a similar manner shall be treated as gross business income for the relevant period.

These proposals take effect from the year of assessment 2014.

DEEMED INTEREST INCOME FROM LOAN OR ADVANCES TO DIRECTOR

Presently, a company (other than an exempt private company) is prohibited from making a loan to a director of the company or of a related company under Section 133 of the Companies Act 1965, unless the said loan is made:

(a) to provide such a director with funds to meet expenditure incurred or to be incurred by him/her for the purposes of the company or for the purpose of enabling him/her properly to perform his/her duties as an officer of the company; or
(b) to provide such a director who is engaged in the full-time employment of the company or its holding company with funds to meet expenditure incurred or to be incurred by him/her in purchasing or otherwise acquiring a home; or
(c) to such a director who is engaged in the full-time employment of the company or its holding company, where the company has at a general meeting approved of a scheme for the making of loans to employees of the company, and the loan is in accordance with that scheme.

Loan or advances may be made by a company to its directors from either its internal funds or from external borrowings. In the instance where the loan or advances are made from the company's internal funds, it would generally be interest-free as there is no additional financing cost incurred by the company. There is currently no specific provision in the Act to impute a deemed interest income on the company in respect of the loans or advances given by the company.

Effective from the year of assessment 2014, it is proposed that where a company provides any loans or advances from its internal funds to its directors, the company shall be deemed to derive interest income from such loans or advances. The interest income for the basis period for a year of assessment shall be the aggregate sum of monthly interest in the basis period, computed in accordance with the following formula:

$$\frac{1}{2} \times A \times B$$

Where A is the total amount of loan of advances outstanding at the end of the calendar month; and
B is the average lending rate of commercial banks published by the Central Bank at the end of the calendar month, or, where there is no such average lending rate, such other reference lending rate as may be prescribed by the Director General.

Where interest is charged by the company and the total interest charged and payable by the director is more than the aggregate sum of interest as determined based on the above formula, this provision of deemed interest income shall not apply. On the other hand, if the interest charged by the company is less than the aggregate sum of interest as determined based on the above formula, the actual interest charged shall be disregarded.

DEFINITION OF DIRECTOR

Presently, a director who is liable for the payment of tax due and payable by the company means a director who:

(i) occupies the position of director by whatever name called, or is concerned in the management of the company's business; and
(ii) either on his/her own or with one or more associates, the owner of, or able to directly or through the medium of other companies by any other indirect means to control, more than 50% of the ordinary share capital of the company.

It is proposed that the percentage of the ordinary share capital that is to be owned or controlled by a person who is regarded as a director be reduced from more than 50% to not less than 20%. This proposal shall take effect upon the coming into operation of the Finance (No. 2) Act 2013.

With this proposal, a director who owns not less than 20% of the ordinary share capital of the company would be put under an onerous burden as he would be jointly and severally liable for the company's tax liabilities. This proposal is seen as grossly unfair as such directors are not in the position to exercise control over the management or affairs of the company by virtue of their shareholding.

APPEAL TO THE SPECIAL COMMISSIONERS OF INCOME TAX (SCIT)

Presently, the Director General shall forward an appeal against an assessment to the SCIT within 12 months from the date of receipt of a notice of appeal or within the extended period granted by the Minister of Finance if the Director General is of the opinion that there is no reasonable prospect of coming into an agreement with the appellant.

It is proposed that under the new Section 102(1A), in the case where the person has applied to invoke a mutual agreement procedure as provided for under a double taxation arrangement based on the same or similar grounds as per the appeal made under Section 99, the appeal filed by a person will not be forwarded to the SCIT until finalisation of the mutual agreement procedure. The person may then within 30 days from the determination of the mutual agreement procedure, submit a written request to the Director General to forward the appeal to the SCIT and such appeal must be forwarded to the SCIT by the Director General within 3 months from the receipt of such request.

This proposal takes effect upon coming into operation of the Finance (No. 2) Act 2013.

REVIEW OF CORPORATE INCOME TAX RATES

The current corporate tax rate of 25% is imposed on the following entities:

- a company
- a trust body
- an executor of an estate of an individual who was domiciled outside Malaysia at the time of his/her death
- a receiver appointed by the court; and
- a limited liability partnership

in line with the implementation of Goods and Services Tax (GST), it is proposed that the corporate income tax rate for the above entities be reduced to 24%.

Presently, a company with a paid-up capital of up to RM2.5 million and a limited liability partnership with total contribution of capital of up to RM2.5 million are subject to the following tax rates:

(i) 20% on chargeable income up to RM500,000; and

(ii) 25% on the remaining chargeable income.

In this regard, it is proposed that the rates be reduced by 1% for a company with a paid-up capital of up to RM2.5 million, as follows:

(i) 19% on chargeable income up to RM500,000; and

(ii) 24% on the remaining chargeable income.

It is noted that the Appendix 11 to the 2014 Budget Speech is silent on the applicability of the above reduced tax rates to a limited liability partnership with total contribution of capital of up to RM2.5 million.

The above proposals are effective from the year of assessment 2016.

REVIEW OF INCOME TAX RATES FOR CO-OPERATIVE SOCIETIES

Presently, the progressive income tax rates for co-operative societies range from 0% to 25% with the maximum rate of 25% applicable to chargeable income exceeding RM750,000.

It is proposed that effective from the year of assessment 2015, the income tax rates be reduced as follows in view of the implementation of GST:

Chargeable income (RM)	Current		Proposed		Tax savings	
	Tax Rate (%)	Tax Payable (RM)	Tax Rate (%)	Tax Payable (RM)	(RM)	(%)
First 30,000 Next 30,000	5	0 1,500	5	0 1,500		
On 60,000 Next 40,000	10	1,500 4,000	10	1,500 4,000		
On 100,000 Next 50,000	15	5,500 7,500	15	5,500 7,500		
On 150,000 Next 100,000	20	13,000 20,000	18	13,000 18,000		
On 250,000 Next 250,000	22	33,000 55,000	21	31,000 52,500	2,000	6.1
On 500,000 Next 250,000	24	88,000 60,000	23	83,500 57,500	4,500	5.1
On 750,000 750,000 and above	25	148,000	24	141,000	7,000 **	4.7

** Tax savings for chargeable income exceeding RM750,000 = RM7,000 + [1% × (chargeable income – RM750,000)]

TRAINING EXPENSES IN LINE WITH GST IMPLEMENTATION

It is proposed that expenses incurred for GST related training in accounting and ICT be given double tax deductions, effective for the y ears of assessment 2014 to 2015. This proposal is to support the smooth implementation of GST, to ensure that tax compliance is enhanced and to reduce the cost of GST implementation for taxpayers.

TAX INCENTIVE FOR FLEXIBLE WORK ARRANGEMENTS

Presently, there are no tax incentives available to encourage employers to implement flexible work arrangements (FWA) for employees.

As a means of encouraging employers to implement FWA for their employees to help boost motivation and increase the productivity of employees, it is proposed that expenses incurred by an employer in training of employees, supervisors and managers as well as consultancy fees incurred to design an appropriate FWA be given double deductions. This incentive is only given to companies that have obtained FWA status from Talent Corporation Malaysia Berhad and applies to applications for FWA status received by Talent Corporation Malaysia Berhad between January 1, 2014 to December 31, 2016.

The eligible expenses include costs for training in:

(a) optimising a work-life balance;
(b) technology orientation;
(c) managing a flexible workforce; and
(d) helping managers embrace flexible work alternatives.

TAX INCENTIVE FOR IMPLEMENTATION OF MINIMUM WAGES

Under the Minimum Wage Policy, all enterprises including professional firms are required to pay a minimum wage of RM900 per month in Peninsular Malaysia, and RM800 per month in Sabah, Sarawak and Labuan to their local and foreign employees, except employees classified as domestic workers. The wages paid by the employer are eligible for tax deduction.

It is proposed that the difference between the original salary and the minimum wages paid by small and medium enterprises (i.e. companies which have a paid-up capital in respect of ordinary shares of not more than RM2.5 million), co-operatives, associations and organisations (trust bodies and societies) be given double deductions.

This proposal is effective from January 1, 2014 to December 31, 2014 and is aimed at reducing the cost of complying with the provisions in the Minimum Wages Order 2012.

DOUBLE DEDUCTION FOR ANCHOR COMPANIES UNDER VENDOR DEVELOPMENT PROGRAMME

The Vendor Development Programme (VDP) has been introduced with the objective of creating vendors that are competitive and of world standard. Under the VDP, government-linked companies and multinational companies are regarded as anchors whereas local companies and small and medium enterprises (SMEs) are vendors.

Presently, operating and development expenses incurred by anchor companies in implementing VDP are not eligible for a tax deduction.

It is proposed that double deductions be given on qualifying expenses incurred by anchor companies to encourage more participation to develop local vendors. The qualifying operating expenses include:

(a) Cost of product development, research and development, innovation and quality improvement;
(b) Cost of obtaining ISO / Kaizen / 5S certifications, evaluation programmes and business process reengineering exercises for the purpose of increasing vendor capabilities; and
(c) Cost of vendor skills training, capacity building, lean management systems and financial management systems.

The qualifying criteria for the double deduction are as follows:

(a) Anchor companies are required to sign a Memorandum of Understanding (MOU) with the Ministry of International Trade and Industry (MITI) under VDP;
(b) Qualifying operating expenses must be certified by MITI before the anchor companies can claim the deduction;
(c) Qualifying operating expenses are capped at RM300,000 per year; and
(d) Double deduction is given for 3 years of assessment.

This proposal is effective for MOUs signed by anchor companies and MITI from January 1, 2014 to December 31, 2016.

TAX DEDUCTION FOR SECRETARIAL AND TAX FILING FEES

Presently, secretarial and tax filing fees incurred by taxpayers are not allowed as tax deductible expenses on the basis that such expenses are not wholly and exclusively incurred directly in the production of gross income.

Proposed Legislation

Effective from the year of assessment 2015, it is proposed that the following deductions be given per year:

- secretarial fee — up to RM5,000
- tax filing fee — up to RM10,000

The deduction given to secretarial and filing fees is welcomed as these expenses are necessarily incurred to comply with the relevant statutory requirements. However, the limitation imposed on the deductible amount is unjustified and should be removed.

EXTENSION OF ACCELERATED CAPITAL ALLOWANCE ON INFORMATION TECHNOLOGY AND COMMUNICATION EQUIPMENT

Presently, the Income Tax (Accelerated Capital Allowance) (Information and Communication Technology Equipment) Rules 2008 provide for accelerated capital allowance (initial allowance of 20% and an annual allowance of 80%) on capital expenditure incurred in relation to the purchase of the following information and communication technology equipment:

(a) Access control system;
(b) Banking systems;
(c) Barcode equipment;
(d) Bursters / decollators;
(e) Cables and connectors;
(f) Computer assisted design (CAD);
(g) Computer assisted manufacturing (CAM);
(h) Computer assisted engineering (CAE);
(i) Card readers;
(j) Computers and components;
(k) Central processing unit;
(l) Storage;
(m) Screen;
(n) Printers;
(o) Scanner / reader;
(p) Accessories;
(q) Communications and network; and
(r) Software system or software package.

The above incentive is set to expire in the year of assessment 2013. To ensure the smooth implementation of GST by businesses by encouraging them to invest in the information and communication technology equipment, it is proposed that the accelerated capital allowance be extended for another 3 years i.e. from year of assessment 2014 to year of assessment 2016.

EXTENSION OF INCENTIVES UNDER THE GREEN LANE POLICY PROGRAMME

Presently, small and medium companies are eligible for the following incentives under the Green Lane Policy programme:

1. Financial assistance:
   Interest subsidy of 2% per year subject to a maximum of RM200,000 per year or accumulated amount of RM1,000,000 for a period of 5 years.

2. Fiscal incentives:
   (a) Stamp duty exemption on loan agreement;
   (b) Deduction for expenses incurred in obtaining the first 1-InnoCERT certification.

3. Government procurement incentives:
   (a) Registration of approved-manufacturer status company without site visit;
   (b) Additional 5 bonus marks will be given in technical evaluation for the purpose of evaluating technical tender / price quotation;
   (c) Due consideration will be given for appointment as receiver of the Transfer of Technology (TOT) Programme in the related industry;
   (d) Priority in participating in procurement exercise by Ministry of Finance (Incorporation) Companies.

The above incentives are given for applications submitted to the Ministry of Finance (MOF) on or before December 31, 2014. It is proposed that the incentives be extended to applications received by the MOF on or before December 31, 2017.

APPEAL ON DEEMED ASSESSMENT

Presently, a taxpayer who is aggrieved by an assessment is given the right to file an appeal to the SCIT via the submission of Form Q to the Director General as provided for under Section 99(1) of the Act. The appeal can be made against the following assessments:

(a) Deemed assessment under Section 90(1) of the Act upon filing of a return by a taxpayer in accordance with Section 77 or 77A of the Act;
(b) Assessment issued under Section 90(3) of the Act according to the best judgment of the Director General in determining the amount of the chargeable income of that taxpayer;
(c) Assessment or additional assessment under Section 91(1) of the Act where it appears to the Director General that no or no sufficient assessment has been made on a person chargeable to tax;

(d) Assessment under Section 91(2) of the Act where tax has been repaid to a person by mistake;
(e) Assessment under Section 91(3) of the Act for the purpose of making good the loss of tax attributable to the fraud, wilful default or negligence;
(f) Assessment under Section 91(4) of the Act for the purpose of giving effect to the revocation, withdrawal or cancellation of any exemption, relief, remission or allowance granted to a person;
(g) Deemed assessment or additional assessment under Section 91(A) of the Act where a taxpayer has furnished an amended return in accordance with Section 77B of the Act;
(h) Advance assessment under Section 92 of the Act; and
(i) Notice of non-chargeability deemed a notice of assessment under Section 97A of the Act.

It is proposed that the right of a taxpayer to appeal to the SCIT will not be applicable to the deemed assessment under items (a) and (g) above, except where the taxpayer is aggrieved by such deemed assessments as a result of complying with a public ruling issued by the Director General. This will be effective upon the coming into operation of the Finance (No. 2) Act 2013.

The above proposal is seen as an infringement of the taxpayer's rights to appeal against an assessment, particularly in a self-assessment system. Public rulings are not law and merely represent the IRB's interpretation of specific provisions in the Act and hence, the avenue to appeal which rests solely on a disagreement with the IRB's view on a subject matter seems unfair and regressive.

AMENDMENT OF DEFINITION OF ENTERTAINMENT UNDER SECTION 18 OF THE ACT

Presently, "entertainment" as defined under Section 18 of the Act , includes:
(a) the provision of food, drink, recreation or hospitality of any kind; or
(b) the provision of accommodation or travel in connection with or for the purpose of facilitating entertainment of the kind mentioned in paragraph (a),

by a person or an employee of his in connection with a trade or business carried on by that person.

It is proposed that the definition of "entertainment" be amended such that expenses incurred by a person or employee of his with or *without consideration paid, whether in cash or in kind*, in promoting the business carried on by that person, shall fall within the definition of "entertainment".

This proposal takes effect from the year of assessment 2014.

The widening of the definition of "entertainment" to include "with or without consideration paid" is clearly a reaction to the court decision in the Aspac Lubricant case. The other amendment to treat "*the provision of accommodation or travel for the purpose of promoting business*" as "entertainment" has far reaching consequences, as expenses relating to the promotion of business are currently deductible under Section 33(1) of the Act. However, if such expenses are classified as "entertainment", the deductibility of such expenses will be limited to 50% and this will increase of the cost of doing business.

TAX DEDUCTION FOR TAKAFUL BUSINESSES

Presently, Section 60AA of the Act does not provide any tax deduction for management expenses incurred by General Takaful business and commission expenses incurred in respect of the Shareholders' Fund.

Hence, it has been proposed that effective from the year of assessment 2014: -
(a) a deduction be given on management expenses incurred by General Takaful business; and
(b) a deduction be given on commission expenses incurred in respect of the Shareholders' Fund in connection with the general business.

However, the proposed amendment does not address the commission expenses incurred in respect of the Shareholders' Fund in connection with family business. This will result in Takaful Operators not being on par with conventional insurers.

SECTION 109E WITHHOLDING TAX ON PROFIT DISTRIBUTED OR CREDITED TO PARTICIPANTS FOR TAKAFUL FUNDS

Under Section 109E of the Act, any profits distributed or credited out of a family fund, family re-*takafu*l fund or general fund under Section 60AA would be subject to withholding tax. Income tax deduction is claimed on the profits distributed from the family fund, family re-*takaful* fund or general fund to participants.

It is proposed that withholding tax will apply only where a tax deduction has been claimed on the profits distributed or credited to the participants out of the operator's family fund, family re-*takaful* fund or general fund. This proposed amendment (which will be effective from the year of assessment 2014) provides flexibility to the *Takaful* Operators and to reduce the administrative issues in respect of complying with the withholding tax requirements.

EXTENDING THE DEDUCTIBILITY OF CONTRIBUTIONS TO CHARITABLE ORGANISATIONS

Presently, a person who makes contributions to an approved institution or organisation under Section 44(6) is given a tax deduction from the aggregate income in the relevant year for any gift of money, and the amount shall not exceed:

(a) 7% of the aggregate income in the case of a person other than a company; or
(b) 10% of the aggregate income in the case of a company.

A charitable organisation is defined as an organisation that is established and maintained to administer a public fund, which is meant to be held solely for the purpose of religious worship or the advancement of religion. The fund is to be used for the construction, improvement or maintenance of a building or buildings in Malaysia.

It is proposed that the abovementioned fund shall also include funds utilised to purchase buildings used as places of worship. This proposal takes effect from the year of assessment 2014.

TAX TREATMENT OF LIMITED LIABILITY PARTNERSHIPS

Presently, provisions in the Act specifically governing a limited liability partnership (LLP) are as follows:

1. A LLP is excluded from the definition of "partnership" under Section 2 of the Act. Instead, it is a taxable person for the purpose of the Act.
2. The tax residence of a LLP in Malaysia is determined based on the management and control of its business or affairs exercised by its partners.
3. In arriving at the adjusted income of a LLP, no deduction is allowed in respect of any remuneration or any similar payment paid to the partners of the LLP where such remuneration or payment is not specified or provided in the agreement made in accordance with Section 9 of the Limited Liability Partnerships Act 2012.
4. A partnership or company, which converts into a LLP is allowed to carry forward its unabsorbed business losses and unabsorbed capital allowances to be utilised against the future income of the LLP.
5. A compliance officer who is appointed by the partners of the LLP under the Limited Liability Partnerships Act 2012 shall be responsible for doing all acts and things required under the Income Tax Act 1967 on behalf of the LLP. Where no compliance officer is appointed, the partners of the LLP are jointly and severally liable.
6. The following tax treatments for a LLP are similar to that of a company, trust body or co-operative society:
   (a) Determination of basis period;
   (b) Due date for filing of tax return and payment of balance of tax payable;
   (c) Furnishing of estimate of tax payable and payment of tax instalments;
   (d) Tax rate including preferential tax rate on the first RM500,000 of the chargeable income;
   (e) Profits paid, credited or distributed by a LLP to its partners are exempted from tax; and
   (f) Controlled transfer provisions would apply.

For the purposes of streamlining the tax treatment of LLPs to be in line with that of companies, it is proposed that:

I. Controlled transfer provisions shall apply in respect of the assets transferred by the converting partnership or company to the newly formed LLP; and
II. A LLP is not entitled to make a claim for capital allowances in respect of the assets transferred for the year of assessment in which the conversion occurred unless a claim has not been made by the converting company or partners of the converting partnership in that year of assessment.

These proposals will take effect upon the coming into operation of the Finance (No. 2) Act 2013.

TAXATION OF WITHDRAWALS OF CONTRIBUTIONS MADE TO A DEFERRED ANNUITY OR A PRIVATE RETIREMENT SCHEME ("PRS")

Currently, where a person (the payer) makes a payment to an individual in relation to a withdrawal of contribution before reaching the age of 55 (other than by reason of death or permanently leaving Malaysia) from a fund administered by that payer under a PRS, the payer is required to deduct tax at the rate of 8%. The tax withheld has to be paid to the Director General within one month after making the payment to the individual.

In the event that the payer fails to remit the tax within the stipulated deadline, a penalty of 10% of the sum owing will be levied and this shall be a debt due to the Government.

It is proposed that the taxability of the withdrawals of contributions by an individual be extended to a deferred annuity. Deferred annuity means a deferred annuity contracted on or after 1 January 2014 issued by insurers licensed under the Financial Services Act 2013 or takaful operators registered under the Islamic Financial Services Act 2013, and contains the Retirement Saving Standards approved by the Central Bank.

In addition to the above, the withdrawals of contributions made to a deferred annuity or a PRS by an individual before reaching the age of 55 (which is subject to the withholding tax of 8%) would exclude withdrawals due to the reason of permanent total disablement, serious disease, mental disability, death or permanently leaving Malaysia.

This proposal (which takes effect upon the coming into operation of the Finance (No. 2) Act 2013) is aimed at aligning the tax treatment on deferred annuity with PRS and to extend the exception rules by including the reason for withdrawal due to the individual's permanent total disablement, serious decease and mental disability.

However, with the new definition of "deferred annuity" under Section 2 of Act, the issue that remains unclear is whether an individual can continue to claim the relief of up to RM3,000, which is given for contributions made for any deferred annuity and PRS under Section 49(1D) of the Act.

MUTUAL ADMINISTRATIVE ASSISTANCE IN TAX MATTERS

Presently, Section 132A of the Act provides that the government is empowered to enter into tax information exchange arrangements with a foreign government with a view to exchanging information that is seen to be relevant in order to administer, assess, collect or to enforce the taxes under this Act or other taxes under any written law.

It is proposed that the Government of Malaysia and a foreign government may enter into a mutual administrative assistance arrangement on tax matters that include simultaneous tax examination, automatic exchange of information or tax administrations abroad. This proposal, takes effect upon the coming into operation of the Finance (No. 2) Act 2013, will enable a closer working relationship with foreign governments on matters pertaining to exchange of information and administration of taxes in order to enhance greater transparency on a cross border basis.

BASIS PERIOD OF A COMPANY, LIMITED LIABILITY PARTNERSHIP, TRUST BODY OR CO-OPERATIVE SOCIETY FOLLOWING CHANGE OF FINANCIAL YEAR END

Currently, under Section 21A(3) of the Act, where a company, limited liability partnership, trust body or co-operative society has made up the accounts of its operations for a period of 12 months ending on a day other than 31 December and there is a failure to make up the accounts ending on the corresponding day in the following basis year, the Director General may direct that the basis period for the year of assessment in which the failure occurs, or the basis periods for that year and the following year of assessment, shall consist of a period or periods (which may be of any length) as specified in the direction.

However, there is no provision in the Act (apart from the public rulings issued by the Inland Revenue Board) governing the direction of basis periods for the relevant years of assessment for the same failure which applies to a company, limited liability partnership, trust body or co-operative society that normally makes up the accounts for a period of 12 months ending on December 31.

It is proposed that with effect from the year of assessment 2014 the words "*other than December 31*" in Section 21A(3) of the Act be replaced by the words "*in a basis year*". This amendment enables the Director General to direct the basis periods of all companies, limited liability partnerships, trust bodies or co-operative societies that change their accounting year end and will take effect from the year of assessment 2014.

BASIS PERIOD OF A COMPANY, LIMITED LIABILITY PARTNERSHIP, TRUST BODY OR CO-OPERATIVE SOCIETY FOR FIRST YEAR OF ASSESSMENT

Currently, as provided under Section 21A(4) of the Act, where a company, limited liability partnership, trust body or co-operative society commences operations on a day in a basis year and makes up its accounts for a period of 12 months ending on a day other than December 31, there shall be no basis period in relation to any of its sources of income for the first year. However, the provision is silent on the determination of the basis periods for those cases where the accounts are made up for a period of less than or more than 12 months. As a result, references are sought to the relevant public rulings issued by the Inland Revenue Board.

Effective from the year of assessment 2014, it is proposed that, where a company, limited liability partnership, trust body or co-operative society commences operations on a day in a basis year for a year of assessment (hereinafter referred to as "first year of assessment") and makes up its account:

(a) for a period of less than 12 months ending on a day in that basis year, that period shall constitute the basis period for the first year of assessment;
(b) for any period of months ending on a day in the immediately following basis year, that period (hereinafter referred to as "second year of assessment") shall constitute the basis period for the year of assessment immediately following the first year of assessment. There shall be no basis period in relation to any of its sources of income for the first year of assessment; or
(c) for a period of more than 12 months ending on a day in the basis year immediately following the second basis year, that period shall constitute the basis period for the year of assessment

immediately following the second year of assessment. There shall be no basis period in relation to any of its sources of income for the first year of assessment and the second year of assessment.

The following examples illustrate the determination of basis period following the above proposed amendments:

Example 1 [illustrating scenario (a)]:
A company commences operations on March 1, 2013 and accounts are made up to September 30, 2013 (less than 12 months) and thereafter to September 30 of each year.

The basis period for the year of assessment 2013 is March 1, 2013 to September 30, 2013.

Example 2 [illustrating scenario (b)]:
A company commences operations on March 1, 2013 and accounts are made up to June 30, 2014 and thereafter to 30 June of each year.

The basis period for the year of assessment 2014 is March 1, 2013 to June 30, 2014

Example 3 [illustrating scenario (c)]:
A company commences operations on December 1, 2013 and accounts are made up to March 31, 2015 (more than 12 months) and thereafter to March 31, of each year.

The basis period for the year of assessment 2015 is December 1, 2013 to March 31, 2015.

With the above proposal, the issues of overlapping basis periods, apportionment of adjusted business income or loss, and submission deadlines of tax returns and estimates of tax payable can be mitigated. This is a positive measure to simplify the direction of basis periods and provides clarity to taxpayers in a self-assessment environment.

DEDUCTION NOT ALLOWED FOR FAILURE TO FURNISH INFORMATION REQUESTED UNDER SECTION 81 OF ACT

Presently, there is no provision under the Act to disallow the claim for deduction in arriving at a person's adjusted income if that person fails to furnish any information as requested by the Director General under Section 81 of the Act.

It has been proposed that where a person fails to furnish any information as requested by the Director General in accordance with Section 81 to justify the person's claim for deduction in arriving at his/her adjusted income within the time specified in the notice or such other period as may be allowed by the Director General, such claim for deduction made by that person be disallowed. It is hoped that Director General would give adequate notice for taxpayers to furnish the required information due to the serious consequences of failure to provide such information within the given time frame. This proposal takes effect from the year of assessment 2014.

This proposal is seen as another measure which curbs the taxpayer's rights to a proper channel of appeal in the event of a tax audit. It is hoped that the IRB would allow a reasonable time frame for the requested information to be furnished if there are valid reasons for this. However, in extenuating circumstances such as loss of records due to a fire or other natural disaster, this proposal will clearly deny the taxpayer the right to make a bona fide claim for a deduction due to circumstances beyond his control.

PAYMENT OF WITHHOLDING TAX DUE

Currently, there is no legislation to empower the Director General to direct a person to remit withholding tax, which should be deducted within a specific timeframe.

Proposed Legislation

In an effort to expedite the collection of outstanding withholding tax, it is proposed that the Director General be empowered to issue a notice to require a person to remit withholding tax that should be deducted and payable to the IIRB within a specific timeframe. This proposal takes effect upon the coming into operation of the Finance (No. 2) Act 2013.

TAX TREATMENT ON INTEREST INCOME FROM LOAN TRANSACTIONS BETWEEN RELATED PARTIES

Currently, interest income that is accruing in or derived from Malaysia shall, when it has been received, be treated as gross income in the basis period when it was first receivable. Interest is deemed received when it is obtainable on demand.

With effect from the year of assessment 2014, it is proposed that interest on loan transactions between related parties will be deemed obtainable on demand when the interest is due to be paid.

FURNISHING OF TAX RETURN BY A COMPANY

Presently, a company can submit its tax return either by way of manual filing or electronic filing to the Director General.

Furthermore, there is no specific provision that states that the return furnished by a company has to be based on accounts audited by a professional accountant.

It is proposed that, with effect from the year of assessment 2014:-

(i) A company is required to file its tax return to the Director General in the prescribed form in an electronic medium or by way of electronic transmission in accordance with Section 152A of the Act; and

(ii) A company's return furnished to the Director General has to be based on accounts audited by a professional accountant, together with a report made by the said professional accountant in accordance with subsections 174(1) and 174(2) of the Companies Act 1965.

The imposition of e-filing on companies is a positive measure to enhance the efficiency of the tax filing system. However, the mandatory requirement for all companies to prepare audited accounts on which their tax returns are based will increase the administrative burden and costs for certain categories of taxpayers who are not required to prepare audited accounts under the Companies Act 1965 such as private exempt companies, companies under liquidation or permanent establishments of non-residents. Also, there may be instances where a company is unable to produce its audited accounts on time due to various reasons such as loss of records, change in key accounting personnel, etc. Failure to submit a tax return without the audited accounts would render the filing as incomplete and would consequently be subject to penalties. Thus, this proposal will place a heavy burden on companies to ensure the timely preparation of their audited accounts under any circumstances.

ESTIMATE OF TAX PAYABLE FOR SMALL AND MEDIUM ENTERPRISE

Presently, a small and medium enterprise (SME) which has commenced operations in a year of assessment is not required to furnish an estimate of tax payable or make instalment payments for a period of two years beginning from the year of assessment in which the SME commences operations.

A SME is defined as a company with a paid-up capital in respect of ordinary shares of RM2.5 million and below at the beginning of the basis period for the relevant year of assessment, and not more than:

(a) 50% of the paid-up capital in respect of ordinary shares of the company is directly or indirectly owned by a related company;

(b) 50% of the paid-up capital in respect of ordinary shares of the related company is directly or indirectly owned by the first mentioned company; or

(c) 50% of the paid-up capital in respect of ordinary shares of the first mentioned company and the related company is directly or indirectly owned by another company.

"Related company" is defined as a company, which has a paid-up capital in respect of the ordinary shares of more than RM2.5 million at the beginning of the basis period for a year of assessment.

It is proposed that where a SME first commences operations in a year of assessment and the SME has no basis period for that year of assessment and for the immediate following year of assessment, the SME is not required to furnished an estimate of tax payable for that year of assessment and for the immediate two following years of assessment. This proposal takes effect from the year of assessment 2014.

Example:

A SME commences operations on November 1, 2014 and closes its first set of accounts on January 31, 2016 (15 months accounts).

Year of assessment	2014	2015	2016	2017	Legislation
Basis period	No	No	Yes	Yes	Section 21A(4)(c)
Estimate of tax payable	Not required	Not required	Not required	Required	New Section 107C(4A)(c)

Likely Tax Effects and Implications

The above amendment is a consequence of the proposed amendment made to Section 21A(4) of the Income Tax Act 1967.

AMENDMENT TO SECTIONS 60F, 60H AND 63B

The current law allows a deduction of permitted expenses for investment holding companies, closed-end fund companies and unit trusts. The deduction of permitted expenses is determined in accordance with the formula below:

$$A \quad X \quad \frac{B}{4C}$$

(i) where, for investment holding companies:

A is the total of the permitted expenses incurred for that basis period reduced by any receipt of a similar kind;

B is the gross income consisting of dividend, interest and rent chargeable to tax for that basis period; and

C is the aggregate of the gross income consisting of dividend (*whether exempt or not*), interest and rent, and gains made from the realisation of investments for that basis period.

(ii) where, for closed-end fund companies:

A is the total of the permitted expenses incurred for that basis period;

B is the gross income consisting of dividend and interest chargeable to tax for that basis period; and

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

(iii) where, for unit trusts:

A is the total of the permitted expenses incurred for that basis period;

B is the gross income consisting of dividend, interest and rent chargeable to tax for that basis period; and

C is the aggregate of the gross income consisting of dividend (*whether exempt or not*), interest and rent, and gains made from the realisation of investments (whether chargeable to tax or not) for that basis period.

To standardise the definition of C in the above formula, it is proposed that the words in the existing legislation be substituted with "dividend and interest (whether such dividend or interest is exempt or not)".

The proposal, which takes effect from the year of assessment 2014, will effectively reduce the deduction of permitted expenses that can be claimed in arriving at the total income and this will result in a higher chargeable income for the investment holding companies, closed-end fund companies and unit trusts.

DEDUCTION FOR INTEREST ON MONEY BORROWED

Presently, subject to interest restriction provision, any sum of interest payable in the basis period for a year of assessment on money borrowed and employed in the production of gross business income or being laid out on assets used or held for the production of gross business income is allowed a deduction in arriving at the adjusted business income for that basis period even if the interest is not paid or due to be paid in that basis period.

Based on the proposed new Section 33(4) which takes effect from the year of assessment 2014, a taxpayer is only eligible to claim a deduction in respect of interest on borrowings when such interest is due to be paid. However, the deduction would be given in the year the interest is payable.

Example:
ABC Sdn Bhd borrowed RM1 million from XYZ Sdn Bhd in the year of assessment 2014. Based on the loan agreement, interest accrues yearly from year of assessment 2014 but the loan principal together with the accrued interest will only be due to be paid in the year of assessment 2018.

Tax Treatment	
Existing Legislation	***Proposed Legislation***
Interest payable is allowed a deduction in the year it is accrued and payable (i.e. incurred) for each year of assessment starting from years of assessment 2014 until 2018.	The interest is only allowed in the year of assessment 2018 when the interest is due to be paid. The deduction however, is to be given in the respective years of assessment when the interest is accrued and payable. This would require a revised tax return to be submitted for the earlier years of assessment.

This proposal together with the new Section 29(3) of the Act, aims to align the timing of taxing of interest income on the lender and deduction of interest expense by the borrower.

C. INVESTMENT INCENTIVES

EXTENSION OF TAX INCENTIVES FOR NEW FOUR AND FIVE-STAR HOTELS

Presently, hotel operators undertaking new investments in four and five-star hotels are given the following tax incentives:

Peninsular Malaysia

(a) Pioneer status with tax exemption of 70% of statutory income for a period of five years; or

(b) Investment tax allowance (ITA) of 60% on qualifying capital expenditure incurred within a period of five years, which can be set-off against 70% of statutory income for each year of assessment.

These incentives are valid for applications received by the Malaysian Investment Development Authority (MIDA) from October 8, 2011 to December 31, 2013.

Sabah and Sarawak

(a) Pioneer status with income tax exemption of 100% of statutory income for a period of five years; or

(b) ITA of 100% on qualifying capital expenditure incurred within a period of five years, which can be set-off against 100% of statutory income for each year of assessment.

These incentives are for applications received by MIDA from August 30, 2008 to December 31, 2013.

It is proposed that the pioneer status or ITA for hotel operators undertaking new investments in four and five-star hotels in Peninsular Malaysia, Sabah and Sarawak be extended for another 3 years. This will apply to applications received by the MIDA from January 1, 2014 until December 31, 2016. This measure is in conjunction with the Visit Malaysia Year 2014 and is aimed at promoting an adequate supply of international standard accommodation, as well as to increase the facilities for meeting, incentive, convention and exhibition (MICE) activities.

TAX INCENTIVE FOR USE OF GREEN TECHNOLOGY

Presently, the following tax incentives are available for companies carrying out activities relating to environmental management:

- Pioneer status or investment tax allowance to companies generating energy from renewable sources, expenditure on energy conservation and recycling of agricultural waste into value added products;
- Import duty and sales tax exemption for equipment used for the generation of energy from renewable resources and energy conservation;
- Tax exemption equivalent to 100% of the additional capital expenditure incurred to obtain the Green Building Index (GBI) certificate given to the owners of buildings;
- Stamp duty exemption on instruments of transfer of ownership for buyers of buildings and residential properties awarded with the GBI certificate; and
- Accelerated capital allowance for environmental protection equipment.

It is proposed that the following incentives be given:

(i) Investment tax allowance for purchase of green technology equipment; and
(ii) Tax exemption on the use of green technology services and systems.

The effective date for the above incentives is yet to be determined.

TAX INCENTIVE FOR RESEARCH AND DEVELOPMENT OF BIOECONOMY

Currently, the following tax incentives are given for companies undertaking biotechnology activities that had been granted with the bionexus status by the Malaysian Biotechnology Corporation Sdn Bhd (BiotechCorp):

- Pioneer status with tax exemption of 100% of statutory income for a period of ten years, or investment tax allowance of 100% on qualifying capital expenditure incurred within a period of five years.
- Upon the expiry of the tax exemption period, a bionexus status company is given a concessionary tax rate of 20% on income from qualifying activities for 10 years.
- Industrial building allowance of 10% over a period of 10 years on building used solely for the purpose of biotechnology research activities.
- Exemption of import duty and sales tax on importation of raw materials / components and machinery and equipment.
- Tax deduction equivalent to the total investment made in seed capital and early stage financing for a company or an individual investing in a bionexus status company.

It is proposed that the following incentives be given for projects which are viewed as viable by BiotechCorp:

1. Tax deduction for companies that invest to acquire technology platform in bio-based industry;
2. Exemption on import duty on R&D equipment for companies that invest in pilot plants for the purpose of pre-commercialisation in Malaysia; and
3. Special incentive to companies to partially cover the operational cost of human capital development in respect of their Centre of Excellence for R&D.

The above incentives are applicable to applications received by BiotechCorp from January 1, 2014 to December 31, 2018.

D. STAMP DUTY

EXEMPTION FOR LOAN AGREEMENTS UNDER THE SOFT LOAN INCENTIVE SCHEME FOR SMALL AND MEDIUM ENTERPRISES

Please refer to Section B above relating to incentives under the Green Lane Policy Programme.

AMENDMENT TO SECTION 9 OF STAMP ACT 1949

At present, for the purpose of subsection 9(6) of the Stamp Act 1949, the person mentioned in subsection 9(1) shall keep and retain the books, records and documents in connection with the issue of such Articles of Association and Memorandum of Association for a period of seven years from the year in which such Articles of Association and Memorandum of Association are issued.

It is proposed that for the purpose of subsection 9(6), the person mentioned in subsection 9(1) shall keep and retain the books, records and documents in connection with the issue of such instruments referred to in paragraph 1(a), (b) or (c) under

Section 9 for a period of seven years from the year in which such instruments are issued. The instruments concerned include unstamped cheques, contract notes or policies of insurance drawn or drawn up and issued on forms to be supplied or adopted by the banker, dealer or insurer; unstamped Articles of Association and Memorandum of Association lodged with the Registrar of Companies; and unstamped TNB Electricity Supply Form issued and supplied by Tenaga Nasional Berhad.

With the proposed amendment, the books, records and documents in connection with instruments referred to in paragraph 1(a), (b) or (c) under Section 9 of the Stamp Act 1949 shall be kept and retained for a period of seven years from the year in which such instruments are issued. The instruments include unstamped cheques, contract notes or policies of insurance drawn or draw up and issued on forms to be supplied or adopted by the banker, dealer or insurer; unstamped Articles of Association and Memorandum of Association lodged with the Registrar of Companies; and unstamped TNB Electricity Supply Form issued and supplied by Tenaga Nasional Berhad.

This proposal takes effect upon the coming into operation of the Finance (No. 2) Act 2013.

AMENDMENT TO SECTION 47A OF STAMP ACT 1949

At present, an instrument which is not stamped within the period specified in or under Section 40 or 47 of the Stamp Act 1949 may be stamped on payment of the unpaid duty and a penalty as prescribed under subsection 47A(1). Pursuant to subsection 47A(2), the Collector may, if he thinks fit, reduce or remit such penalty or the further amount payable for the payment of duty on unstamped TNB Electricity Supply Form issued and supplied by Tenaga Nasional Berhad under paragraph 9(1)(c).

It is proposed that subsection 47A(2) be amended to provide that the Collector may, if he thinks fit, reduce or remit such penalty or the further amount payable where there is a failure by the authorised person to remit the duties collected under subsection 9(1) on unstamped cheques, contract notes or policies of insurance drawn or drawn up and issued on forms to be supplied or adopted by the banker, dealer or insurer; unstamped Articles of Association and Memorandum of Association lodged with the Registrar of Companies; and unstamped TNB Electricity Supply Form issued and supplied by Tenaga Nasional Berhad in accordance with subsection 9(3).

This proposal takes effect upon the coming into operation of the Finance (No. 2) Act 2013.

E. INDIRECT TAXES

IMPORT DUTY EXEMPTION ON R&D EQUIPMENT FOR COMPANIES INVESTING IN PILOT PLANTS FOR THE PURPOSE OF PRE-COMMERCIALISATION

Please refer to Section C above.

F. LABUAN

NEW SECTION 21A FOR PRESCRIBED FORM

Presently, under Section 21 Labuan Business Activity Tax Act, 1990 (LBATA), the Minister may make regulations generally for the purpose of carrying out, or giving effect to, the provisions of LBATA and in particular, but without prejudice to the foregoing, for prescribing such forms as are required by LBATA to be prescribed or as he may deem necessary.

It is proposed that this section be substituted with the provision that the Minister may make regulations generally for the purpose of carrying out, or giving effect to, the provisions of LBATA. A new Section 21A will also be enacted to empower the Director General to prescribe such forms as are required by LBATA and such other forms as he considers that are ought to be prescribed in connection with the operation of LBATA.

The proposed amendment effectively segregates the roles of the Minister of Finance and the Director General of Inland Revenue. The Minister's role is confined to making regulations and the Director General is now empowered to prescribe forms as required by Labuan Business Activity Tax Act. The proposal shall take effect upon coming into operation of LBATA.

G. PETROLEUM INCOME TAX

AMENDMENT TO SECTION 2 OF THE PETROLEUM (INCOME TAX) ACT 1967 (PITA)

Presently, the definition of "entertainment" in Section 2 of the PITA is as follows:

"includes –

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

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

by a chargeable person or an employee of his in connection with petroleum operations carried on by that chargeable person"

It is proposed that the definition of "entertainment" be amended, by inserting after the words "employee of his" the words "with or without any consideration paid whether in cash or in kind, in promoting or". With these additional words, the definition of entertainment will now read as follows:

"includes –

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

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

by a chargeable person or an employee of his with or without any consideration paid whether in cash or in

This proposal is to align the definition of "entertainment" as provided in Section 18 of the Income Tax Act 1967 and shall take effect from the year of assessment 2014.

RETURN OF INCOME

Section 34A(3) of PITA currently requires every chargeable person to make up accounts of his expenditure or profits or losses arising from his petroleum operations. Those accounts shall be audited by a professional accountant and, together with a report made by the accountant, shall contain, in so far as they are relevant, the matters set out in subsections 174(1) and (2) of the Companies Act 1965. However, there is no explicit requirement for the chargeable person to furnish his return based on the accounts, which have been audited by a professional accountant.

It is proposed that the return furnished by the chargeable person shall be based on accounts audited by a professional accountant, together with a report made by that accountant which shall contain, in so far as they are relevant, the matters set out in subsections 174(1) and (2) of the Companies Act 1965. This proposal shall take effect from the year of assessment 2014 and is made to be aligned with the similar proposal to the Income Tax Act 1967.

DISPOSAL OF APPEALS

Presently, if the Director General is of the opinion that there is no reasonable prospect of coming to an agreement with a taxpayer in relation to the taxpayer's appeal against an assessment, the Director General may forward the appeal to the SCIT at any time within the twelve-month period (or such extended period granted by the Minister) from the date of receipt of the notice of appeal.

It is proposed that where a person has made an application to invoke a mutual agreement procedure ("MAP") under Section 65A of the PITA and the grounds of such application are similar to an appeal filed under the PITA, then the appeal shall not be forwarded to the SCIT until the MAP has been determined. The person may within 30 days from the date of the determination of the MAP request the Director General to forward such appeal to the SCIT and the Director General shall forward the appeal to the Special Commissioners within three months of receiving such a request.

This proposal is made in order to be aligned with a similar proposal in respect of the Income Tax Act 1967 and will take effect upon coming into operation of the Finance (No. 2) Act 2013.

IMPLEMENTATION OF ADVANCE PRICING ARRANGEMENT (APA)

An APA is a mechanism to obtain up-front agreement from the tax authorities on the prices of goods and services to be transacted in a specified future period between a taxpayer and its related persons. Presently, there is no specific legislation governing APAs for upstream petroleum operations in Malaysia. However, Section 138C (governing APA), was inserted in the Income Tax Act 1967 with effect from 1 January 2009.

To enable chargeable persons engaged in upstream petroleum operations to pro-actively manage transfer-pricing risk, it is proposed that chargeable persons be allowed to apply to the Director General for APAs. The parties to an APA will be:

I. The IRB and a chargeable person (Unilateral APA); or

II. Where relevant tax treaties are in place under Section 65A of the PITA, an APA can be between the IRB, the chargeable person and the tax authority of the relevant foreign jurisdiction (Bilateral APA) or the IRB, the chargeable person and the tax authorities of more than one foreign jurisdiction (Multilateral APA).

APAs can only be entered into in respect of cross-border transactions. The meaning of "transactions" in this context is construed as a transaction between:

(a) companies one of which has control over the other; or
(b) companies both of which are controlled by some other person.

The "chargeable person" in the proposed new APA Section i.e. Section 71A, refers to the person in a petroleum agreement that enters into a controlled transaction with another company. The application for an APA shall be made in the prescribed form and shall contain particulars as may be required by the Director General. This proposal takes effect from the year of assessment 2014.

CLARIFICATION ON MEANING OF "CHARGEABLE PERSON" IN SECTION 72A

Further to the introduction of a transfer pricing and thin capitalisation provision i.e. Section 72A, each chargeable person is required to determine and apply an arm's length price with respect to any controlled transaction with another person for the acquisition or supply of property or services.

It is proposed that in the case of a petroleum agreement, the "chargeable person" referred to in subsections 71A(2), (3) and (4) shall refer to the person in that petroleum agreement who enters into a controlled transaction. This proposal shall be effective upon the coming into operation of the Finance (No. 2) Act 2013.

POWER TO MAKE RULES PERTAINING TO APAs

In line with the introduction of Section 71A governing APAs, it is proposed that a specific provision be introduced in the PITA to empower the Minister to make rules pertaining to the scope and procedure applied in relation to APAs. This proposal shall take effect from the year of assessment 2014.

AMENDMENT TO FIRST SCHEDULE OF THE PITA

Presently, qualifying exploration expenditure (QEE) incurred by a chargeable person (first-mentioned chargeable person) under a petroleum agreement, prior to the basis period for the first year of assessment that the chargeable person is chargeable to tax, can be deducted against the gross income of another chargeable person (second-mentioned chargeable person) in another petroleum agreement, provided that the original parties to both petroleum agreements are the same. The deduction is determined by a prescribed formula.

Where the QEE exceeds the gross income from petroleum operations of the second-mentioned chargeable person, the excess of the QEE:

(a) shall be allowed to be deducted from the gross income of that petroleum operation for the subsequent years of assessment of the second mentioned chargeable person; or
(b) may be deducted from the gross income of another chargeable person in another petroleum agreement if the original parties to the petroleum agreements are the same.

This "transfer of QEE" between more than one petroleum agreements is not applicable to petroleum operations in the Joint Development Area or in an area under any agreement or arrangement made by the Malaysian Government with the government of any territory outside Malaysia for the joint exploration and exploitation of petroleum in overlapping areas.

It is proposed that in order for the QEE to be deducted against the gross income of the second-mentioned chargeable person, the QEE incurred by the first-mentioned chargeable person must be in relation to an agreement area where chargeable petroleum is not being produced. Further, it is proposed that any excess of QEE over gross income can no longer be used by another chargeable person (other than second-mentioned chargeable person) in another petroleum agreement, even though the original parties to the petroleum agreements are the same.

The purpose of allowing the QEE under a petroleum agreement to shelter the gross income under another petroleum agreement (where the original parties to these agreements are the same) is to provide incentive to contractors to undertake exploration activities in high-risk areas. However, such incentive will be curtailed with the above proposal where any excess QEE cannot be utilised by a chargeable person under another petroleum agreement although the original parties to these agreements are the same.

H. REAL PROPERTY GAINS TAX ("RPGT")

CHANGES IN REAL PROPERTY GAINS TAX RATES

Presently, gains from the disposal of real properties (including residential homes, commercial buildings, land as well as gains from the disposal of shares in real property companies) are taxed under the Real Property Gains Tax Act 1976 (PRGTA). RPGT is imposed on the net gains from the disposal of the real property after deducting the acquisition price and other expenses incurred such as stamp duty, legal fee, cost of renovation and commission for sales agent.

The current RPGT are between 0% to 15%, depending on the holding period of the real properties and shares in real property companies:

Date of Disposal	Real Property Gains Tax Rates		
	Companies	Individual (Citizen & Permanent Resident)	Individual (Non-Citizen)
Within 2 years from date of acquisition	15%	15%	15%
Between 2-5 years from date of acquisition	10%	10%	10%
Disposal after 5 years from date of acquisition	0%	0%	0%

It is proposed that RPGT rates on the gains from disposal of real properties and shares in real property companies be reviewed as follows:

Date of Disposal	Real Property Gains Tax Rates		
	Companies	Individual (Citizen & Permanent Resident)	Individual (Non-Citizen)
Within 3 years from date of acquisition	30%	30%	30%
In the 4th year	20%	20%	30%
In the 5th year	15%	15%	30%
In the 6th year and subsequent years	5%	0%	5%

This measure is introduced to further curb real estate speculation activities that have exerted pressures on property prices and is effective for disposals of real properties and shares in real property companies from January 1, 2014.

INTERPRETATION OF DIRECTOR

Presently, any director and other person who is concerned in the management of a company's business and, either on his own or with one or more associates within the meaning of subparagraph 5(5) of Schedule 1 of the RPGTA, is the owner or able directly through the medium of other companies or by any other indirect means to control more than 50% of the ordinary share capital of the company shall be jointly and severally liable for the payment of tax during the period in which the tax is liable to be paid by the company.

It is proposed that any director and other person who is concerned in the management of a company's business and, either on his own or with one or more associates within the meaning of subparagraph 5(5) of Schedule 1 of the RPGTA, is the owner or able directly through the medium of other companies or by any other indirect means to control not less than 20% of the ordinary share capital of the company shall be jointly and severally liable for the payment of tax during the period in which the tax is liable to be paid by the company. With this amendment, any director and other person who is concerned in the management of a company who has at least 20% control over a company shall be jointly and severally liable for the payment of tax due by that company. This is in line with a similar proposed amendment to the Income Tax Act, 1967 and will take effect upon the coming into operation of the Finance (No. 2) Act 2013.

DEFINITION OF TAX PAYABLE FOR PENALTIES IMPOSED UNDER SUBSECTIONS 14(5) AND 15(4) OF THE RPGTA

Presently, a penalty of 10% of the tax payable can be imposed pursuant to subsections 14(5) and 15(4) of the RPGTA on the disposer of a chargeable asset in the assessment and additional assessment raised respectively, as the case may be, where the acquirer fails to retain and remit tax as required under Section 21B by reason of an incorrect or wrong notification furnished by the disposer to the acquirer on the chargeability of the asset disposed.

It is proposed that for purposes of the penalty imposed pursuant to subsections 14(5) and 15(4), "tax payable" shall mean the amount of tax charged on the chargeable gain excluding any allowable loss referred to under subsection 7(4).

This proposal takes effect upon the coming into operation of the Finance (No. 2) Act 2013 and will result in heavier penalties being imposed on the disposer in cases where there is an incorrect or wrong notification furnished by the disposer to the acquirer on the chargeability of the disposed asset.

DEFINITION OF TAX WHICH IS PAYABLE FOR PENALTY IMPOSED UNDER SUBSECTION 29(3) OF THE RPGTA

Subsection 29(3) of the RPGTA presently provides for a penalty equal to treble the amount of the tax which is payable to be imposed on a disposer of a chargeable asset who fails to make a return pursuant to subsection 13(1) or fails to make a declaration of such disposal in his income tax return pursuant to subsection 13(5) and where no prosecution under subsection 29(1) has been instituted in relation to that failure.

It is proposed that for purposes of the penalty imposed pursuant to subsection 29(3, "tax which is payable" shall mean the amount of tax charged on the chargeable gain excluding any allowable loss referred to under subsection 7(4).

This proposal takes effect upon the coming into operation of the Finance (No. 2) Act 2013.

I. GOODS AND SERVICES TAX ("GST")

The current indirect tax regime covers customs duties, excise duties, sales tax and service tax.

Sales tax is governed by the Sales Tax Act 1972. It is a single-tier tax imposed on taxable goods manufactured in Malaysia and taxable goods imported into Malaysia, both for domestic consumption. The sales tax rates are 5% or 10%.

Service tax is governed by the Service Tax Act 1975 and is a single-tier tax applicable on "taxable services" prescribed under the Service Tax Regulations 1975. The current service tax rate is 6% whist specific rates are charged on credit cards.

It has finally been announced that the Goods and Services Tax (GST) regime will be introduced to replace the current sales and service tax. The proposed GST model to be implemented in Malaysia is detailed below: -

1. Scope of Tax

(i) GST is to be charged on goods and services at all levels starting from production, manufacture, wholesale and retail;

(ii) GST is to be charged on goods and services supplied within the country or imported into the country;

(iii) Supplies made by the Federal and State Government departments are not within the scope of GST except for some services prescribed by the Minister of Finance;

(iv) Supplies made by the local authorities and statutory bodies in relation to regulatory and enforcement functions are not within the scope of GST; and

(v) GST charged on all business inputs such as capital assets and raw materials is known as input tax whilst GST charged on all supplies made (sales) is known as output tax. For eligible businesses, the input tax incurred is fully recoverable from the Government through the input tax credit mechanism.

2. Zero-Rated Supply

Zero-rated supply means goods and services sold by businesses that are charged GST at a zero rate. For such businesses, GST paid on their inputs can be claimed as credits. Examples of goods and services subject to GST at zero rate are:

(i) Agriculture products (paddy and vegetables);

(ii) Foodstuff (rice, table salt, sugar, plain flour, milk and cooking flour);

(iii) Livestock supplies (live animals and unprocessed meat of cattle, buffaloes, goats, sheep and swine);

(iv) Poultry (live and unprocessed meat of chickens and ducks);

(v) Eggs (fresh and salted);

(vi) Fish, prawns, cuttlefish, crabs, oysters, cockles and lobsters;

(vii) Supply of treated water (excluding distilled water, de-ionised water, oxygenised water and mineral water) to domestic consumers;

(viii) Supply of the first 200 units of electricity to a domestic household for a minimum period of twenty eight days;

(ix) Goods supplied to designated areas (Labuan, Langkawi and Tioman) from Malaysia; and

(x) International services.

Note: The above list is not exhaustive.

3. **Exempt Supply**

Exempt supply means goods and services sold by businesses that are exempt from GST. For such businesses, GST paid on their inputs cannot be claimed as credits. Examples of goods and services exempted from GST are as follows:

(i) Land used for residential or agricultural purposes or general use;
(ii) Buildings used for residential purposes;
(iii) Financial services;
(iv) Private education services;
(v) Childcare services;
(vi) Private healthcare services;
(vii) Transport services;
(viii) Tolled highways or bridges;
(ix) Funeral, burial and cremation services; and
(x) Supplies made by societies and similar organisations.

Note: The above list is not exhaustive.

4. **Standard Rate**

The standard GST rate is 6%.

5. **Threshold**

The threshold for purposes of registration under GST is annual sales value of RM500,000. Businesses below the threshold are not required to register but may register on a voluntary basis.

It is proposed that GST would be implemented from April 1, 2015.

CONCLUSION

From a fiscal perspective, the 2014 Budget proposals provide for a shift from a narrow base towards consumption-based with the introduction of GST. As expected, a GST incentive package will be rolled out to help with the smooth transition to GST and this includes:-

- Reduction in corporate and personal tax rates
- Deductions for secretarial and tax filing fees
- Double deductions for GST related training for employees
- Accelerated capital allowances for purchase of ICT equipment

Besides GST, the other key proposals relate to the upward revision to RPGT rates to curb speculative activities.

Tax administration will be tightened with the requirement for companies to file their tax returns electronically and the need for such returns to be prepared based on audited accounts.

There are several proposals that curtail the right of appeal which will have serious repercussions to taxpayers should these proposals be enacted.

Overall, there is no significant rollback of tax incentives but with the increase in tax revenue target for 2014, taxpayer can expect more tax audits to be conducted by the IRB in the coming year.

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2. *2014 Budget Speech*
3. *Finance Bill 2013*

Note: This article is largely developed from the "2014 Budget Commentary and Tax Information" for the MICPA.