INLAND REVENUE BOARD OF MALAYSIA

DEDUCTION OF INTEREST EXPENSE AND RECOGNITION OF INTEREST INCOME FOR LOAN TRANSACTIONS BETWEEN RELATED PERSONS

PUBLIC RULING NO. 9/2015

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DIRECTOR GENERAL'S PUBLIC RULING

Section 138A of the Income Tax Act 1967 [ITA] provides that the Director General is empowered to make a Public Ruling in relation to the application of any provisions of the ITA.

A Public Ruling is published as a guide for the public and officers of the Inland Revenue Board of Malaysia. It sets out the interpretation of the Director General in respect of the particular tax law and the policy as well as the procedure applicable to it.

The Director General may withdraw this Public Ruling either wholly or in part, by notice of withdrawal or by publication of a new Public Ruling.

Director General of Inland Revenue,
Inland Revenue Board of Malaysia.

1. Objective

The objective of this Public Ruling (PR) is to explain in relation to a loan transaction between related persons:

(a) when a deduction is allowed in respect of interest expense in computing the adjusted income from a source for the basis period for a year of assessment; and

(b) the recognition of interest income.

2. Relevant Provisions of the Law

2.1 This PR takes into account laws which are in force as at the date this PR is published.

2.2 The provisions of the Income Tax Act 1967 (ITA) related to this PR are sections 2 and 27, subsections 29(3), 33(2) and 33(4), paragraphs 4*(c)* and 33(1)*(a)*.

3. Interpretation

The words used in this PR have the following meaning:

3.1 “Interest” is the return or compensation for the use or retention by a person of a sum of money belonging to or owed to another.

3.2 “Relative” means a parent, a child (including a stepchild and a child adopted in accordance with any law), a brother, a sister, an uncle, an aunt, a nephew, a niece, a cousin, an ancestor or a lineal descendant.

3.3 “Person” includes a company, a body of persons, a limited liability partnership and a corporation sole.

3.4 “Related persons” in subsection 29(3) of the ITA means –

(i) between persons one of whom has control over the other;

(ii) between individuals who are relatives of each other*; or

(iii) between persons both of whom are controlled by some other person.

***Note:**

Paragraph 3.4(ii) is effective for the year of assessment 2015 and subsequent years of assessment.

3.5 "Company" means a body corporate and includes any body of persons established with a separate legal identity by or under the laws of a territory outside Malaysia and a business trust.

3.6 "Year of assessment" subject to subsection 2(5) of the ITA means calendar year.

3.7 "Basis period" in relation to a person, a source of his and a year of assessment, means such basis period, if any, as is ascertained in accordance with section 21 or 21A.

4. Tax Treatment of Interest Expense

4.1 Interest expense incurred and payable

For the purpose of paragraph 33(1)*(a)* and subsection 33(2) of the ITA, subsection 33(4) of the ITA provides that interest expense incurred and payable on monies borrowed for the basis period for a year of assessment is only deductible in ascertaining the adjusted income of a person when the said interest is due to be paid. The monies borrowed by that person must be –

(a) employed in that period in the production of gross income from that source; or

(b) laid out on assets used or held in that period for the production of gross income from that source.

For claims on deduction of interest expense and a review of the relevant prior years of assessment, a taxpayer is required to inform the Inland Revenue Board of Malaysia (IRBM) branch office that handles the taxpayer's file via letter and submit together the amended tax computation in respect of the interest expense payable for each year of assessment. After a review and confirmation is made, IRBM would amend the assessment for each year of assessment to allow the claims for deduction of the relevant interest expense that is payable.

Example 1

A Sdn Bhd (closes its accounts on 31 December annually) made a loan to B Sdn Bhd for business purposes and details of the loan and interest are as follows:

Date of Loan	Loan Amount (RM)	Rate of Interest (%)	Loan Period	Date the Loan and Interest is Due to be Paid
1.1.2014	40,000	5% (non-cumulative)	3 years	31.12.2016

Interest payable for each year of assessment is as follows:

Year of Assessment 2014	Year of Assessment 2015	Year of Assessment 2016
Interest - RM2,000 Payable for 1.1.2014 to 31.12.2014 but only due to be paid on 31.12.2016	Interest - RM2,000 Payable for 1.1.2015 to 31.12.2015 but only due to be paid on 31.12.2016	Interest - RM2,000 Payable for 1.1.2016 to 31.12.2016 and due to be paid on 31.12.2016

Loan on 1.1.2014

Total interest of RM6,000 is due to be paid on 31.12.2016 by the borrower

(i) Based on the agreement, the loan is charged with interest at a rate of 5% for each year although the total interest is due to be paid by B Sdn Bhd on 31.12.2016. As such, the interest expense of RM2,000 is payable for each year ending on 31.12.2014, 31.12.2015 and 31.12.2016.

(ii) According to subsection 33(4) of the ITA, a claim of interest expense payable for a particular year of assessment under paragraph 33(1)*(a)* and subsection 33(2) of the ITA can only be allowed against gross income from that year of assessment when the interest is due to be paid. Total interest of RM6,000 is due to be paid by B Sdn Bhd on 31.12.2016. Interest payable for each year of assessment is to be claimed as follows:

Year of Assessment	Year of Assessment Deduction is Allowable	Amount of Interest Deductible (RM)	When the Interest Deduction can be Claimed
2014 - 2016	2014 - 2016	2,000 each year	From 31.12.2016

(iii) As the interest payable for the years of assessment 2014 and 2015 is not due to be paid until 31.12.2016, B Sdn Bhd is only entitled to claim a deduction for the interest expense against the gross income for the year of assessment 2014 and the year of assessment 2015 from 31.12.2016.

B Sdn Bhd has to inform IRBM from 31.12.2016 via letter attaching the amendments to the tax computation in respect of the interest expense claimed for years of assessment 2014 and 2015. After a review and confirmation is made, IRBM would amend the assessments for years of assessment 2014 and 2015 to allow the claim for interest payable of RM2,000 for each of the years of assessment concerned.

(iv) Since the interest payable of RM2,000 for the year of assessment 2016 is due to be paid on 31.12.2016 before the filing deadline (31.7.2017), the claim for the deduction of interest expense should be made in B Sdn Bhd's Income Tax Return Form (ITRF) for year of assessment 2016.

Example 2

C Sdn Bhd (closes its accounts on 31 December annually) obtained a loan from its holding company for the purpose of its business as follows:

Date of Loan	Loan Amount (RM)	Rate of Interest (%)	Loan Period	Date the Loan and Interest is Due to be Paid
1.6.2014	1 million	6% (non-cumulative)	10 years	31.5.2024

The interest expense payable for each year of assessment (year of assessment 2014 to year of assessment 2024) can only be claimed and allowed to C Sdn Bhd when the said interest is due to be paid on 31.5.2024. Interest payable for each year of assessment is to be claimed as follows:

Year of Assessment	Year of Assessment Deduction is Allowable	Amount of Interest Deductible (RM)	When the Interest Deduction can be Claimed
2014	2014	35,000	From 31.5.2024
2015 - 2023	2015 – 2023	60,000 each year	From 31.5.2024
2024	2024	25,000	From 31.5.2024

C Sdn Bhd has to inform IRBM from 31.5.2024 via letter attaching the amendments to the tax computation in respect of the interest expense claimed for years of assessment 2014 to 2022. After a review and confirmation is made, IRBM would amend the assessments for years of assessment 2014 to 2022 to allow the claim for interest payable for each of the years of assessment concerned.

As C Sdn Bhd is allowed to make a claim for the interest expense from 31.5.2024 and the ITRF for the year of assessment 2023 is due on 31.7.2024, the interest expense of RM60,000 should be claimed by C Sdn Bhd in its ITRF for the year of assessment 2023.

Since the interest payable of RM25,000 for the year of assessment 2024 is due to be paid on 31.5.2024 before the filing deadline (31.7.2025), the claim for deduction of interest expense should be made in C Sdn Bhd’s ITRF for the year of assessment 2024.

Example 3

D Sdn Bhd (accounting period ends on 31 December each year) is one of the subsidiaries of E Sdn Bhd. On 1.1.2014, D Sdn Bhd obtained a loan from its holding company and the details of the loan agreement are as follows:

Date of Loan	Loan Amount (RM)	Rate of Interest (%)	Loan Period	Date the Interest is Due to be Paid
1.1.2014	5 million	6% (non-cumulative)	15 years	31.12.2028

Based on the loan agreement, the interest is due to be paid by D Sdn Bhd on 31.12.2028. Interest payable for each year of assessment are to be claimed as follows:

Year of Assessment	Year of Assessment Deduction is Allowable	Amount of Interest Deductible (RM)	When the Interest Deduction can be Claimed
2014	2014	300,000	From 31.12.2028
2015 - 2027	2015 – 2027	300,000 each year	From 31.12.2028
2028	2028	300,000	From 31.12.2028

D Sdn Bhd has to inform IRBM from 31.12.2028 via letter attaching the amendments to the tax computation in respect of the interest expense claimed for years of assessment 2014 to 2027. After a review and confirmation is made, IRBM would amend the assessments for years of assessment 2014 and 2027 to allow the claim for interest payable of RM300,000 for each of the years of assessment concerned.

The interest expense of RM300,000 for the year of assessment 2028 should be claimed in D Sdn Bhd's ITRF for the year of assessment 2028.

4.2 Loan agreement prior to the year of assessment 2014

Subsection 33(4) of the ITA is applicable to loan agreements signed before and after the year of assessment 2014. For agreements that were effective prior to the year of assessment 2014 but the date the interest is due to be paid has not occured, then from the year of assessment 2014 the interest expense will only be allowed on the date the interest is due to be paid. The interest incurred that had been allowed as a deduction prior to the year of assessment 2014 is maintained.

Example 4

E Sdn Bhd (closes its accounts on 31 December annually) obtained a loan of RM3 million from its holding company on 1.1.2010. The terms of the agreement are as follows:

Date of Loan	Loan Amount (RM)	Rate of Interest (%)	Loan Period	Date the Loan and Interest is Due to be Paid
1.1.2010	3 million	5% (non-cumulative)	10 years	31.12.2019

The interest expense of RM150,000 that had been claimed and allowed for each of the years of assessment 2010, 2011, 2012 and 2013 would be maintained.

The interest expense payable for each year of assessment (year of assessment 2014 to 2019) can only be claimed and allowed to E Sdn Bhd when the interest is due to be paid on 31.12.2019.

Interest payable for years of assessment 2014 to 2019 are to be claimed as follows:

Year of Assessment	Year of Assessment Deduction is Allowable	Amount of Interest Deductible (RM)	When the Interest Deduction can be Claimed
2014 - 2019	2014 – 2019	150,000 each year	From 31.12.2019

E Sdn Bhd has to inform IRBM from 31.12.2019 via letter attaching the amendments to the tax computation in respect of the interest expense claimed for years of assessment 2014 to 2018 for a review of the assessments concerned.

The interest expense for year of assessment 2019 should be claimed in E Sdn Bhd's ITRF for the year of assessment 2019.

4.3 No payment is made on the date interest is due to be paid

If interest is not paid by the borrower on the date the interest is due to be paid, the interest expense can still be claimed and allowed as a deduction under paragraph 33(1)*(a)* of the ITA as the liability to pay the interest arises on the due date.

Example 5

Same facts as in Example 4. E Sdn Bhd failed to make payment on the date the interest is due to be paid on 31.12.2019. Payment is only made on 1.1.2025.

Although interest is not paid on the date interest is due to be paid, a deduction of the interest expense payable under paragraph 33(1)*(a)* of the ITA is allowable to E Sdn Bhd because the liablity to pay arises on 31.12.2019. Interest payable is allowable as a deduction for the years of assessment 2014 to 2019 from 31.12.2019.

The claim for the interest expense is the same as explained in Example 4.

4.4 Payment is made before the date interest is due to be paid

If payment is made before the date interest is due to be paid, then the interest payment will be allowed as a deducton in the year of assessment the interest is paid.

Example 6

Same facts as in Example 3 except that the loan is for a period of 10 years and interest is due to be paid on 31.12.2023. D Sdn Bhd made the interest payment of RM800,000 on 31.12 2018. The balance of the interest is paid on the date interest is due to be paid i.e on 31.12.2023.

Since D Sdn Bhd paid RM800,000 being part of the total interest on 31.12.2018, the interest payable each year of assessment is to be claimed as follows:

Year of Assessment	Year of Assessment Deduction is Allowable	Amount of Interest Deductible (RM)	When the Interest Deduction can be Claimed
2014 - 2015	2014 – 2015	300,000 each year	From 31.12.2018
2016	2016	200,000	From 31.12.2018
		100,000	From 31.12.2023
2017 - 2023	2017 -2023	300,000 each year	From 31.12.2023

D Sdn Bhd has to inform IRBM from 31.12.2018 (for years of assessment 2014 to 2016) and from 31.12.2023 (for years of assessment 2016 to 2022) via letter attaching the amendments to the tax computation in respect of the interest expense claimed for a review of the assessments concerned.

The interest expense for year of assessment 2023 should be claimed in its ITRF for the year of assessment 2023.

4.5 Interest restriction under subsection 33(2) of the ITA

If a loan that is obtained is not used wholly for the purpose of a business, the interest expense can still be allowed but subject to interest restriction under subsection 33(2) of the ITA. For further information on interest restriction, please refer to PR No. 2/2011 titled "Interest Expense and Interest Restriction". Interest expense can be allowed after taking into account interest restriction determined according to the formula mentioned in the PR when the interest is due to be paid.

Example 7

F Sdn Bhd closes its accounts on 31 December each year. The company obtained a loan of RM1 million from its holding company on 1.1.2014 for use in its business. F Sdn Bhd purchased 6,000 units of Air Asia shares on 1.3.2014 and a shophouse on 15.5.2014.

Details of the loan are as follows:

Date of Loan	Loan Amount (RM)	Rate of Interest (%)	Loan Period	Date Loan and Interest is Due to be Paid
1.1.2014	1 million	6% (non-cumulative)	10 years	31.12.2023

F Sdn Bhd received income from investments in 2015 as follows:

Shares	Unit	Cost (RM)	Single-tier Dividend (RM)
Air Asia	6,000	30,000	5,000

Property	**Cost (RM)**	**Rental Received (RM)**	**Revenue Expense (RM)**
Shophouse	570,000	60,000	8,000

As the loan was used for business and non-business purposes, interest restriction is applicable in accordance with the following formula –

Interest restriction

$$= \frac{\text{RM600,000 (Amount of loan utilised for non-business purposes)}}{\text{RM1,000,000 (Loan amount)}} \times \text{RM60,000 (Interest payable)}$$

$$= \text{RM36,000}$$

The interest expense in relation to business source payable for each year of assessment amounting to RM24,000 a year (after taking into consideration the interest restriction) for years of assessment 2014 to 2023 can only be claimed and allowed to F Sdn Bhd when the interest is due to be paid on 31.12.2023.

The amount of RM36,000 that is not allowed in the computation of the company's adjusted income from business source is allowable as a deduction against the dividend income and rental income of the respective years of assessment. However, the interest expense relating to the derivation of single-tier dividend is disregarded under paragraph 12B of Schedule 6 of the ITA. The deduction of interest expense against rental income can only be claimed for the relevant years of assessment once the interest expense is due to be paid on 31.12.2023.

Interest expense in relation to a non-business source and allowed as a deduction against investment income (dividend and rental income) for each year of assessment from 2014 to 2023 is apportioned as follows:

Formula	**Dividend (RM)**	**Rental (RM)**
$\frac{\text{Cost of investment}}{\text{Total loan utilised for investments}} \times \text{Interest}$	$\frac{30,000}{600,000} \times 36,000$ = 1,800 (Disregarded under paragraph 12B of Schedule 6 of the ITA)	$\frac{570,000}{600,000} \times 36,000$ = 34,200

Interest payable for each year of assessment in respect of business source is to be claimed as follows:

Year of Assessment	Year of Assessment Deduction is Allowable	Amount of Interest Deductible (RM)	When the Interest Deduction can be Claimed
2014 - 2023	2014 – 2023	24,000 each year	From 31.12.2023

5. Recognition of Interest Income

5.1 Basis period to which gross income in respect of interest is related

Section 27 of the ITA provides that income from interest, discount, rental, royalty or any pensions, annuity or other periodical payments to which paragraph 4(*e*) of the ITA applies are part of the gross income of a person when received and would be taxable on a receipt basis although the income could relate to an earlier period.

5.2 Basis period to which income obtainable on demand is related

Although interest receivable for a particular basis period for a year of assessment is only brought to tax for that year of assessment at the time of receipt as provided under section 27 of the ITA but there are circumstances where interest income is deemed received in the absence of any payment received. Section 29 of the ITA, an anti-avoidance provision provides the following:

(i) Loan transactions between unrelated persons

Subsection 29(1) of the ITA provides that for loan transactions between unrelated persons, interest income will only be recognised as income of the lender if the said interest has been received or obtainable on demand by the lender. Interest would be taxable according to the basis period for a year of assessment the said interest is receivable as provided in section 27 of the ITA.

(ii) Loan transactions between related persons

Effective from the year of assessment 2014, subsection 29(3) of the ITA (except subparagraph 29(3)*(aa)* which is effective for the year of assessment 2015 and subsequent years of assessment) was introduced to provide that a lender is deemed to be able to obtain on demand the receipt of interest from a loan transaction between related persons in the basis period for a year of assessment where such interest is due to be paid by the borrower in the said period. This means that interest income is deemed to be received by the lender on the date interest is due to be paid by the borrower whether or not the interest has been received.

Example 8

Same facts as in Example 1 and B Sdn Bhd is controlled by A Sdn Bhd. The recognition of interest income by A Sdn Bhd is as provided under subsection 29(3) of the ITA as follows:

Date of Loan	Loan Amount (RM)	Rate of Interest (%)	Loan Period	Date The Loan and Interest Is Due to be Paid
1.1.2014	40,000	5% (non-cumulative)	3 years	31.12.2016

Interest receivable for each year of assessment are as follows -

Year of Assessment 2014	Year of Assessment 2015	Year of Assessment 2016
Interest - RM2,000 Receivable for 1.1.2014 to 31.12.2014 but is only due to be received on 31.12.2016	Interest - RM2,000 Receivable for 1.1.2015 to 31.12.2015 but is only due to be received on 31.12.2016	Interest - RM2,000 Receivable for 1.1.2016 to 31.12.2016 and is due to be received on 31.12.2016

Loan on 1.1.2014

Total interest of RM6,000 is deemed to be obtainable on demand on the date interest is due to be paid on 31.12.2016 by the borrower

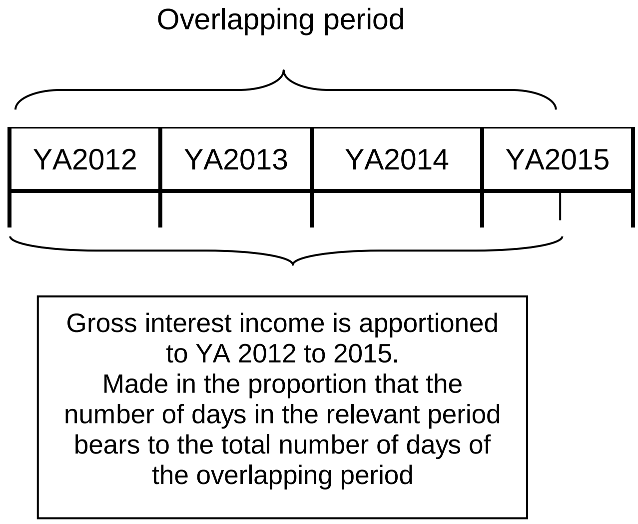
(i) Pursuant to subsection 29(3) of the ITA, interest of RM6,000 (RM2,000 X 3 years) is deemed to be obtainable on demand by the lender on the date interest is due to be paid by the borrower i.e on 31.12.2016.

(ii) As the loan interest was at the rate of 5% per annum and the date interest is due to be paid is 31.12.2016, this means that the interest receivable amounts to RM2,000 per annum for the years ending 31.12.2014, 31.12.2015 and 31.12.2016. The total interest income of RM6,000 will be brought to tax in the year 2017 and assessed for the years of assessment in which interest is receivable i.e years of assessment 2014, 2015 and 2016.

(iii) A Sdn Bhd has to disclose the interest income related to years of assessment 2014 and 2015 in its ITRF for the year of assessment 2016 under the part for income of preceding years not declared. The revised tax computations in respect of the interest income for years of assessment 2014 and 2015 have to be submitted to the IRBM branch office for a review of the assessments.

5.3 Basis period to which gross income in respect of interest is related

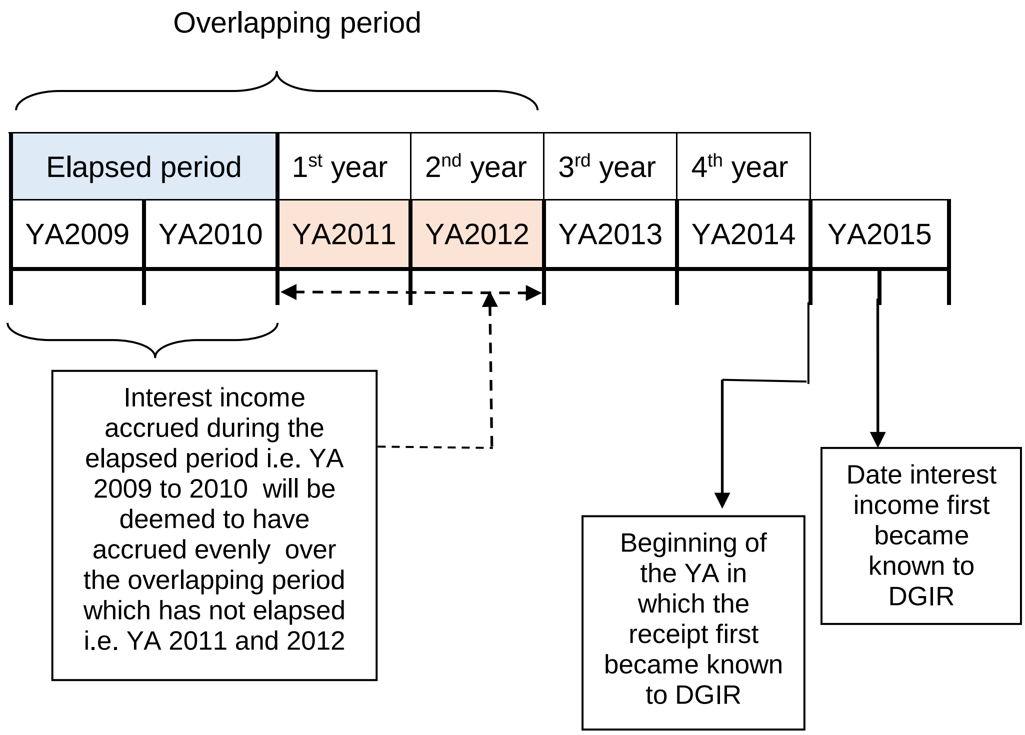
Subsection 27(2) of the ITA provides that where gross income of a relevant person consists of interest, etc is receivable in respect of a period i.e two or more basis periods (referred to as overlapping period in this subsection) which overlaps the relevant period, the gross income is apportioned between the part of the overlapping period that overlaps the relevant period and the remaining part or parts of the overlapping period. This is summarised in the following diagram:



In a situation where the interest income elapsed more than 4 years before the day on which the receipt of that interest income first became known to the Director General of Inland Revenue (DGIR), the time limit to make an assessment is applicable by virtue of subsection 91(1) of the ITA. The following provisos to subsection 27(2) of the ITA determines the basis period for which an assessment is made:

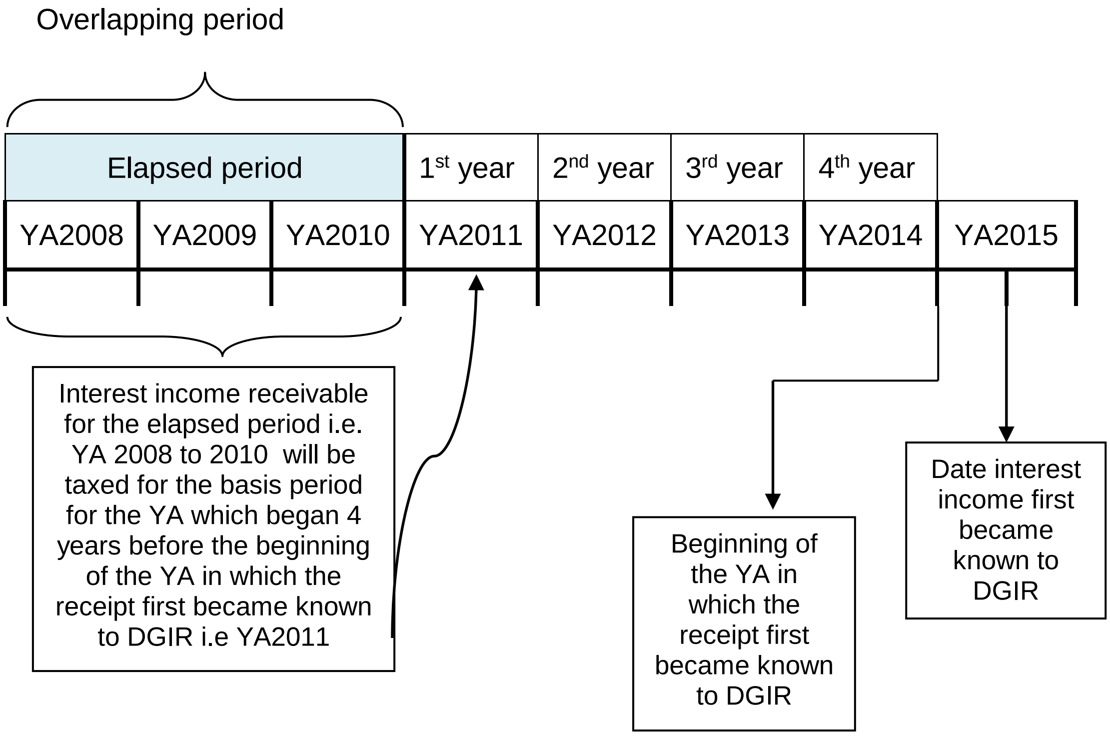
(i) Proviso (b) of subsection 27(2) of the ITA

Where **part** of an overlapping period in respect of which interest income is receivable elapsed more than four years before the day on which the receipt of the gross income first became known to the DGIR, that interest income is deemed to have accrued evenly over the overlapping period which has not elapsed. This is summarised in the following diagram:



(ii) Proviso (c) of subsection 27(2) of the ITA

Where the **whole** of the overlapping period in respect of which gross interest income is receivable elapsed more than four years before the day on which the receipt of that gross income first became known to the DGIR, that gross income would be treated as gross income for the basis period for the year of assessment which began four years before the beginning of the year of assessment which includes the day on which the receipt of the gross income first became known to the DGIR. This is summarised in the following diagram:



Example 9

The facts are the same as in Examples 4 and 5. However the transactions involve related and unrelated persons.

(a) Loan transactions between related persons

If a loan transaction is between related persons, subsection 29(3) of the ITA is applicable as the holding company is deemed to receive the interest income on 31.12.2019, whether or not the interest payment has been made by the borrower. The holding company is required to report the interest income in its ITRF 2019 which is to be furnished to the IRBM by 31.7.2020.

The gross interest income receivable of RM1,500,000 in respect of the overlapping period (1.1.2010 - 31.12.2019) is deemed to be received by the holding company on 31.12.2019.

As part (1.1.2010 – 31.12.2015) of the overlapping period (1.1.2010 - 31.12.2019) in respect of which interest income is receivable elapsed more than four years before the day on which the receipt of that interest income first became known to the DGIR (31.7.2020), proviso (b) of subsection 27(2) of the ITA is applicable. The interest income for the elapsed period (YA 2010 - 2015) of RM900,000 (RM150,000 per year X 6 years of assessment) is deemed to have accrued evenly over the period which has not elapsed (YA 2016 to 2019).

The recognition and computation of interest receivable is as follows:

Date the Loan and Interest is Deemed Obtainable on Demand – Subsection 29(3)	**Date the Interest Income First Became Known to DGIR**	**Breakdown of Interest Income Receivable for Each Year of Assessment (RM)**	**Application of Proviso (b) of Subsection 27(2) and Year of Assessment for which Income is Taxed**
31.12.2019	31.7.2020	2019 = RM150,000	2019 = RM375,000 (150,000 + 225,000)
		2018 = RM150,000	2018 = RM375,000 (150,000 + 225,000)
		2017 = RM150,000	2017 = RM375,000 (150,000 + 225,000)
		2016 = RM150,000	2016 = RM375,000 (150,000 + 225,000)
		2015 = RM150,000	RM900,000 accrued evenly over the overlapping period that has not elapsed i.e. 1.1.2016 - 31.12.2019 (4 YA) $\frac{\text{RM900,000}}{\text{4 YA}}$ = 225,000/YA
		2014 = RM150,000	
		2013 = RM150,000	
		2012 = RM150,000	
		2011 = RM150,000	
		2010 = RM150,000	

(b) Loan transactions between unrelated persons

If a loan transaction is between unrelated persons, subsection 27(1) of the ITA is applicable where the interest income will only be recognised as income of the lender when received on 1.1.2025 and not on 31.12.2019. As the lender closes its accounts on 31 December annually, it will be required to report the interest income received in the ITRF 2025 which is to be furnished to the IRBM by 31.7.2026.

The gross interest income receivable of RM1,500,000 in respect of the overlapping period (1.1.2010 - 31.12.2019) is only received by the lender on 1.1.2025. As the **whole** of the overlapping period (1.1.2010 - 31.12.2019) has elapsed more than four years before the day on which the receipt of that gross income first became known to the DGIR (31.7.2026), proviso (c) of subsection 27(2) of the ITA is applicable.

The gross income of RM1,500,000 would be treated as gross income for the basis period for the year of assessment which began four years (YA 2022) before the beginning of the year of assessment which includes the day on which the receipt of the interest first becomes known to the DGIR (YA 2026).

The computation of interest income received is as follows:

Date the Loan and Interest is Deemed Obtainable on Demand– Subsection 29(3)	Date the Interest Income First Became Known to DGIR	Breakdown of Interest Income Receivable for Each Year of Assessment (RM)	Application of Proviso (c) of Subsection 27(2) and Year of Assessment for which Income is Taxed
1.1.2025	31.7.2026	2019 = RM150,000	2022 = RM1,500,000
		2018 = RM150,000	
		2017 = RM150,000	
		2016 = RM150,000	
		2015 = RM150,000	
		2014 = RM150,000	
		2013 = RM150,000	
		2012 = RM150,000	
		2011 = RM150,000	
		2010 = RM150,000	

Example 10

The facts are the same as in Example 6. The holding company E Sdn Bhd reports the interest income in the ITRF 2019 that is filed on 31.7.2020 to IRBM. However, the balance of interest RM2.2 million is not paid on 31.12.2023. E Sdn Bhd reports the interest income that is deemed to be obtainable on demand in the ITRF 2023 on 31.7.2024. The tax treatment is as follows:

Date the Loan and Interest is Deemed Obtainable on Demand – Subsection 29(3)	Date the Interest Income First Became Known to DGIR	Breakdown of Interest Income Receivable for Each Year of Assessment (RM)	Application of Proviso (b) of Subsection 27(2) and Year of Assessment for which Income is Taxed
31.12.2018	31.7.2019	2014 = RM300,000	
		2015 = RM300,000	2015 = RM450,000
		2016 = RM200,000	2016 = RM350,000
31.12.2023	31.7.2024	2016 = RM100,000	RM1,000,000 accrued evenly over the overlapping period that has not elapsed (YA 2020 – 2023)
		2017 = RM300,000	
		2018 = RM300,000	
		2019 = RM300,000	
		2020 = RM300,000	2020 = RM550,000 (RM300,000 + 250,000)
		2021 = RM300,000	2021 = RM550,000 (RM300,000 + 250,000)
		2022 = RM300,000	2022 = RM550,000 (RM300,000 + 250,000)
		2023 = RM300,000	2023 = RM550,000 (RM300,000 + 250,000)

(i) Interest income of RM800,000 received by E Sdn Bhd first became known to the DGIR on 31.7.2019. The interest income for the elapsed period (year of assessment 2014) will be accrued evenly for the year of assessment 2015 and 2016. E Sdn Bhd has to submit the revised tax computations for the years of assessment 2015 and 2016 to the IRBM branch office for a review of the assessments when it files its ITRF for the year of assessment 2018 on 31.7.2019. The interest income for the years of assessment 2015 and 2016 has to be disclosed in the ITRF under the part for income of preceding years not declared.

(ii) The balance of interest income of RM2.2 million though not paid is obtainable on demand on 31.12.2023 and will be taxed in the years of assessment as shown above. Revised tax computations for years of assessment 2020 to 2022 have to be submitted to IRBM branch office for a review of the assessments when E Sdn Bhd files its ITRF for the year of assessment 2023 on 31.7.2024.

6. **Summary**

6.1 Tax treatment for the recognition of interest income (lender) and deduction of interest expense (borrower) on loan transactions between related persons can be illustrated by the following example.

Example 11

J Sdn Bhd (closes accounts on 31 December annually) made a loan of RM1 million to its subsidiary K Sdn Bhd in the year of assessment 2013. According to the loan agreement, K Sdn Bhd is required to repay the loan together with interest to J Sdn Bhd on 31.12.2022. J Sdn Bhd reports its interest income in the ITRF 2022 which is received by IRBM on 31.7.2023.

The tax treatment is as follows –

Subsection 33(4)	**Subsection 29(3)**
K Sdn Bhd (Borrower)	**J Sdn Bhd (Lender)**
Claims for interest deduction can only be made from 31.12.2022 i.e. on the date interest is due to be paid. Interest expense payable will be allowed as a deduction in each year of assessment commencing from the year of assessment 2013 to 2022.	Interest income is deemed received when obtainable on demand by the lender when the interest is due to be paid by the borrower on 31.12.2022. Interest income is deemed received on 31.12.2022. As part (1.1.2013 - 31.12.2018) of the overlapping period (1.1.2013 – 31.12.2022) in respect of which interest income is receivable elapsed more than four years before the day on which the

Subsection 33(4)	**Subsection 29(3)**
K Sdn Bhd (Borrower)	**J Sdn Bhd (Lender)**
	receipt of that interest income first became known to the DGIR (31.7.2023), proviso (b) of subsection 27(2) is applicable. The interest income for the elapsed period is deemed to have accrued evenly over the overlapping period that has not elapsed (YA2019 – 2022).

Note:

The expenses can only be claimed by the borrower when the interest is due to be paid whereas income is assessed on the lender when it is obtainable on demand. This means that the date the interest is due to be paid is –

(i) the date the accumulated unpaid interest expense is allowable as a deduction under subsection 33(4) of the ITA;

(ii) the date the accumulated unpaid interest income is deemed to be obtainable on demand; and

(iii) assessed to tax in the relevant years of assessment as provided for under proviso (b) of subsection 27(2) and subsections 29(3) of the ITA.

6.2 Application of section 27, subsection 29(3), paragraph 33(1)(*a*) and subsection 33(4) of the ITA

The application of the above provisions for the purpose of income recognition and deduction of interest expense for loan transactions between related persons effective from the year of assessment 2014 are as follows:

Interest Expense		**Interest Income**	
Paragraph 33(1)(*a*)	Subsection 33(4)	Section 27	Subsection 29(3)
Interest expense incurred and amount payable for loan is only allowable as a deduction when the liability to pay the interest arises. The interest expense will be allowed according to the year of assessment interest is payable.	The interest expense under paragraph 33(1)(*a*) and subsection 33(2) can only be allowed as a deduction when the interest is due to be paid.	Interest income is the gross income of a person when it is received or deemed received and will be assessed in the relevant period in which the interest is receivable. Proviso (b) or (c) of subsection 27(2) would be applicable if either **part** or **whole** of an overlapping period in respect of gross interest income is receivable elapsed more than four years before the day on which the receipt of that interest income first became known to the DGIR.	Interest income is deemed obtainable on demand by the lender when the interest is due to be paid by the borrower notwithstanding that interest has not been paid, provided that this subsection shall not apply if the income is received before it is due to be paid.

Director General of Inland Revenue,
Inland Revenue Board of Malaysia.