Tax Flash

January 2013

PR No. 9/2012 – Taxation of REIT/PTF

The Inland Revenue Board ["IRB"] has recently issued the Public Ruling ["PR"] No. 9/2012 – Taxation of Real Estate Investment Trusts ["REIT"] / Property Trust Funds ["PTF"]. This PR provides guidance on the tax treatment accorded to approved REIT/PTF.

Salient points of the abovementioned PR include:-

i. Rental Income of REIT/PTF – Special Treatment

- Effective year of assessment ["YA"] 2005, REIT/PTF is given special treatment pursuant to Section 63C of the Income Tax Act 1967 ["the Act"] as follows:-
  - Rental income received by REIT/PTF from its investment in real properties is treated as business income.
  - In ascertaining the adjusted income for a year of assessment:-
    - amount of deductible expenses is restricted to the gross income from the rental source for that year and any excess of expenditure not absorbed is disregarded; and
    - no deduction of expenses is allowed if that source does not produce any income.
  - In ascertaining the statutory income for a year of assessment:-
    - amount of capital allowance is restricted to the adjusted income from the rental source for that year; and
    - any excess of capital allowance not absorbed is disregarded.
- Transitional provision – any unabsorbed business loss and unabsorbed capital allowance prior to YA 2005 (i.e. prior to the introduction of Section 63C of the Act) can be carried forward to YA 2005 and thereafter until it is fully absorbed.

ii. Deductibility of Expenses

- Expenses wholly and exclusively incurred in the production of rental income are allowable against that rental income.
- Pursuant to the Income Tax (Deduction for Establishment Expenditure of REIT/PTF) Rules 2006, legal, valuation and consultancy fees for establishing REIT/PTF prior to approval by the Securities Commission ["SC"] are allowed for tax deduction in the basis period for the year of assessment in which the business commences (effective YA 2006).

Hyperlinks

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iii. Capital Allowance and Industrial Building Allowance ["IBA"]

- REIT/PTF qualifies for capital allowance which is deductible against the adjusted rental business income from rental source.
- REIT/PTF deriving rental income from an industrial building used for specific purposes is eligible to claim IBA.
- A company which has claimed IBA and disposes the industrial building to REIT/PTF is deemed to have disposed for an amount equal to its residual expenditure on the first day of the company's final period (i.e. not subject to balancing charge or balancing allowance). REIT/PTF is eligible to claim IBA on the remaining balance of the unclaimed tax written down value of the building (effective YA 2008).
- Where an industrial building is disposed of together with the plant and machinery, balancing charge or balancing allowance of the plant and machinery has to be computed separately.

iv. Tax Treatment on Income of REIT/PTF

- REIT/PTF is fully exempt from tax for a year of assessment if it distributes to its unit holders 90% or more of its total income in the basis period for that year of assessment. Where distribution made by the REIT/PTF to its unit holders is less than 90% of the total income, the whole chargeable income will be subject to tax at prevailing corporate tax rate (effective YA 2007).
- Certain interest income earned by REIT/PTF is exempt from tax (such as interest from securities or bonds issued or guaranteed by the government, a bank or financial institution licensed under the Banking and Financial Institutions Act 1989 or Islamic Banking Act 1983, etc).
- Taxable dividend income received by REIT/PTF forms part of its total income and the tax credits attached to taxable dividends are given to the REIT/PTF. When the total income (i.e. taxable dividend income) of REIT/PTF is distributed to the unit holders, the distribution (with tax credit attached) is subject to tax at the unit holder level.
- Tax exempt income received by REIT/PTF (e.g. capital gains and certain interest income) is not included in computing its total income.

v. Rental Income of a Unit Trust (Other than REIT/PTF)

- Other property trusts that do not qualify as REIT/PTF (i.e. approved by the SC) will continue to have their rental income treated as a non-business source income under Section 4(d) of the Act.

vi. Distribution of Income by REIT/PTF to Unit Holders

- REIT/PTF is given a grace period of 2 months from the closing of its account to distribute the 90% or more of its total income so as to qualify for tax exemption at the REIT/PTF level.

- Deduction of Withholding Tax ["WT"]
  - A REIT/PTF that is fully exempt from tax i.e. distribute 90% or more of its total income to unit holders is required to deduct WT under Section 109D (final tax) of the Act as summarised below:-

Non-resident company	25%
Foreign institutional investor	10%
Individual/Others – resident – non-resident	 10% 10%

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

- Accumulated Income of REIT/PTF
  - The undistributed accumulated income of REIT/PTF from prior years could fall under the following categories:-
    - previous years' income (tax exempt); or
    - previous years' undistributed income (already been subjected to tax at the REIT/PTF level).
  - The distribution of REIT/PTF from prior years that has been subjected to tax previously would carry with it a tax credit. This tax credit can be utilised to set-off against the tax payable by the unit holders for the year of assessment in which the accumulated income is distributed.

PR No. 10/2012 – Tax Treatment of Malaysian Ship

PR No. 10/2012

The IRB has recently issued the PR No. 10/2012 – Tax Treatment of Malaysian Ship to provide guidance on the tax treatment and exemption of shipping income from a Malaysian Ship received by a resident in Malaysian prior to the YA 2014 [i.e. before implementation of the amendments of Sections 54A(1) and 54A(2) of the Act which has been deferred to the YA 2014].

Salient points of the abovementioned PR include:-

i. Malaysian Ship

- To qualify as a Malaysian Ship as defined under Section 54A(6) of the Act, a vessel has to be:-
  - registered as a Malaysian Ship under the Malaysian Shipping Ordinance 1952,
  - a sea-going ship, and
  - not a ferry, barge, tug-boat, supply vessel, crew boat, lighter, dredger, fishing boat or other similar vessel.

ii. Shipping Income from Malaysian Ships

- The exemption of shipping income from Malaysian Ships under Section 54A of the Act is as summarised below:-

Qualifying person	A person resident in Malaysia
Qualifying business	a. Transporting passengers or cargo by sea on a Malaysian Ship, or b. Letting out on charter a Malaysian Ship (owned by the person) on a voyage or time charter basis
Exemption	100% of statutory income of the qualifying business
Effective	YA 1984

- Income of a resident person from the business of transporting passengers or cargo by sea wherever accruing or derived (i.e. world income scope) is chargeable to tax, unless it qualifies for exemption under Section 54A(1)(a) of the Act as summarised above.
- Income derived from all Malaysian Ships that qualifies for the exemption under Section 54A of the Act shall be treated as a single business source.

iii. Treatment of Capital Allowance of Malaysian Ships

- The capital allowance for every asset owned and used in the business which has not been claimed shall be deemed to have been claimed and given for the purpose of ascertaining the statutory income exempted from tax under Section 54A(1) of the Act (effective YA 2009).
- The capital allowance claimed or deemed to have been claimed for a Malaysian Ship is deductible against the adjusted income of other Malaysian Ships that qualifies for exemption under Section 54A of the Act.
- Unabsorbed capital allowance of a Malaysian Ship shall only be utilised to set-off against exempt income under Section 54A of the Act in subsequent years of assessment (i.e. not deductible against income from non-Malaysian Ships).

iv. Adjusted Loss of Malaysian Ships

- Any adjusted loss in respect of a Malaysian Ship for any year of assessment shall only be deducted against the exempt income under Section 54A of the Act (i.e. not deductible against income from non-Malaysian Ships or other sources of income for that year of assessment).
- The unabsorbed adjusted loss of the operation of a Malaysian Ship in a basis year has to be carried forward to the following year of assessment to be deducted against the income exempt under section 54A of the Act.

- The unabsorbed adjusted loss of the operation of a Malaysian Ship brought forward from the previous year of assessment is prohibited from deducting against:
  - the income from non-Malaysian Ships used in the business, or
  - the aggregate of statutory income from all business sources

  for that year of assessment.

v. Disposal of a Malaysian Ship

- Balancing allowance arising from the disposal of a Malaysian Ship shall be deducted against exempt income of Malaysian Ships under Section 54A of the Act. Any unabsorbed allowance shall be carried forward to be deducted against the exempt income of Malaysian Ships in the subsequent years of assessment.
- Balancing charge shall not exceed the amount of capital allowance claimed or deemed to have been claimed prior to the disposal.

vi. Operating More Than One Qualifying Business Activity

- Where a resident person is carrying on both qualifying business activities (i.e. business of transporting cargo or passengers by sea on a Malaysian Ship and the activity of letting out his Malaysian Ship on a voyage or time charter basis) in respect of which his income is exempt under Section 54A of the Act, the business activities shall be deemed to be 2 separate and distinct business source.

vii. Exempt Account

- Pursuant to Section 54A(3)(b) of the Act, the exempt income of a Malaysian Ship has to be credited to an exempt account.
- Dividend paid, credited or distributed out of the exempt account is exempt from income tax in the hands of the shareholders.

PR No. 11/2012 – Employee Share Scheme Benefit

PR No. 11/2012

The IRB has recently issued the PR No. 11/2012 – Employee Share Scheme Benefit. This PR provides guidance on the tax treatment on the share benefit that arising from employee share schemes received by an employee from his employer, the determination of the value of the share benefit and the responsibilities of the employer and employee related thereto.

Salient points of the abovementioned PR include:-

i. Tax Treatment of Benefit Arising from Share Scheme

- Prior to YA 2006
  - The computation of benefit from share scheme is as shown below:-

	RM
Market value of share on the date the option is offered	XXX
Less : Offer price of the shares on the date the option is offered	(XXX)
Perquisite under Section 13(1)(a) of the Act	XXX

- The benefit from the share scheme arises on the date the option is exercised. This benefit is related to the basis period in which the option was offered.

- Effective YA 2006
  - The method for the determination of the share benefit for employees is provided under Sections 25(1A) and 32(1A) of the Act.
  - Section 25(1A) of the Act provides that a benefit is derived from a share scheme if:-
    - the right to acquire shares in a company exists; and
    - the right is exercised within the relevant period.

    The benefit is considered as part of the gross income from an employment in the relevant period in which the rights are exercised.
  - Section 32(1A) of the Act provides specifically the formula to determine the share scheme benefit as shown below:-

	RM
Market value of share on the date the scheme is exercisable or exercised, whichever is lower	XXX
Less : Price paid for the share (if any)	(XXX)
Perquisite under Section 13(1)(a) of the Act	XXX

- Transitional Period
  - As a concession, for those options offered prior to the introduction of the new provisions under Sections 25(1A) and 32(1A) of the Act which are not exercisable yet or have not been exercised, the employees are allowed to opt for the tax treatment prior to YA 2006 provided that:-
    - the offer price has been determined at the time the offer was made to the employee; and
    - the share scheme has the feature of an Employee Share Option Scheme ["ESOS"].
  - Should an employee opt for the tax treatment applicable to prior YA 2006, when he exercises the option 6 years after the date of offer, the share benefit will be taxed in the year of assessment which began 5 years before the beginning of the year of assessment in which he exercises the option.

ii. Computation of the Value of the Share Benefit

- The PR provides various examples on the computation of the value of the share benefit for share scheme offered by the employers under the following scenarios:-
  - ESOS
  - Employee share purchase plan
  - Share award scheme
  - Share appreciation rights scheme
  - Warrant scheme
  - Additional shares (bonus) issued before employees exercise the share scheme offered
  - Right to acquire shares is replaced

iii. Responsibility of Employee

- The employee is required to:-
  - make an assessment by including the share benefit as income from employment for the basis period in which that share scheme is exercised;
  - report in the income tax return form, the amount in respect of benefits from the share scheme that has been exercised; and
  - ensure that income tax on that benefit is paid either by deductions from remuneration under the Monthly Tax Deductions ["MTD"] scheme in the month the option is exercised or upon furnishing the income tax return form or by making arrangement with the IRB to pay the amount of tax by instalments.

iv. Responsibility of Employer

- The employer is required within 30 days after the expiry of the period of acceptance of the offer as specified in the by-laws of the share scheme to notify the IRB concerning the launch of the share scheme (via Form BT/MSSP/2012).
- Where an employee who has been offered a share scheme has exercised his right under the scheme, the employer must:-
  - ensure that the tax to be charged on the benefit that arises from the share scheme is deducted from the employee's salary based on the MTD schedule in the month the scheme is exercised;
  - make the tax deductions from the remuneration of the employee who chooses to pay the tax by instalments; or
  - ensure that an election made by the employee to pay by himself the income tax arising on the perquisite upon furnishing the income tax return form is done at the time the share scheme is exercised.
- The employer is also required to report the share benefit in the Form EA of the employee for the year the scheme is exercised and submit the details of the employees who have exercised their rights under a share scheme to the IRB.

v. Expenses Related to Newly Issued Shares of a Company or Holding/Subsidiary Company

- No deductions are allowed for expenses claimed as staff costs in the income statement related to the issuance of newly issued shares of a company or its holding/subsidiary company to fulfill the company's obligations under an employee share scheme.

Tax Exemption of Income Derived from Domestic Tours

Following the 2013 Budget announcement, the Income Tax (Exemption) (No. 11) Order 2012 has been gazetted to provide tax exemption on income derived from domestic tours. Pursuant to this Order, a resident company is exempted from payment of income tax in respect of the statutory income derived from domestic tours if the total number of local tourists on domestic tours is not less than 1,500 in the basis period for a year of assessment as certified by a letter from the Ministry of Tourism Malaysia.

Income Tax (Exemption) (No. 11) Order 2012

"Domestic tours" means a tour package for travel within Malaysia undertaken by local tourists inclusive of transportation by air, land or sea and accommodation.

"Local tourists" means individual who are Malaysian citizens or residing in Malaysia.

The above Order shall have effect from the YA 2013 until YA 2015.

Double Deduction for Contribution by Licensed Insurers to the Malaysian Motor Insurance Pool

The Income Tax (Deduction for Contribution by Licensed Insurers to the Malaysian Motor Insurance Pool) Rules 2012 have been gazetted to allow double deduction for contribution made by a licensed insurer to the Malaysian Motor Insurance Pool in arriving at the adjusted income of the general business of the licensed insurer.

Income Tax (Deduction for Contribution by Licensed Insurers to the Malaysian Motor Insurance Pool) Rules 2012

"Malaysian Motor Insurance Pool" means a high-risk insurance pool established collectively by licensed insurers to provide insurance for risks in respect of motor vehicles which are unable to obtain such insurance elsewhere;

"contribution" means the payment to the Malaysian Motor Insurance Pool by a licensed insurer in respect of the insurer's share of the losses suffered by the Malaysian Motor Insurance Pool.

The above Rules shall have effect from the YA 2011 until YA 2015.

Exemptions for ASEAN Infrastructure Fund Limited

4 exemption orders have recently been gazetted to provide exemption to ASEAN Infrastructure Fund Limited in respect of:-

i. Income Tax
   - Pursuant to the Income Tax (Exemption) (No. 10) Order 2012, tax exemption is given to:-
     - o ASEAN Infrastructure Fund Limited from all provisions of the Act;
     - o a non-resident employee in respect of all gains or profits derived from his employment with ASEAN Infrastructure Fund Limited.

Income Tax (Exemption) (No. 10) Order 2012

ii. Labuan Business Activity Tax
   - Pursuant to the Labuan Business Activity Tax Act (Exemption) Order 2012, ASEAN Infrastructure Fund Limited is exempted from all provisions of the Labuan Business Activity Tax Act 1990.

Labuan Business Activity Tax Act (Exemption) Order 2012

iii. Real Property Gains Tax
   - Pursuant to the Real Property Gains Tax (Exemption) (No. 2) Order 2012, ASEAN Infrastructure Fund Limited is exempted from all provisions of the Real Property Gains Tax Act 1976 in respect of any disposal of chargeable assets after 24th April 2012.

Real Property Gains Tax (Exemption) (No. 2) Order 2012

iv. Stamp Duty
   - Pursuant to the Stamp Duty (Exemption) (No. 5) Order 2012, exemption on stamp duty is given to all instruments executed by ASEAN Infrastructure Fund Limited from 24th April 2012 onwards.

Stamp Duty (Exemption) (No. 5) Order 2012

The above Orders are deemed to have come into operation on 24th April 2012.

Deferment on Implementation of Income Tax (Thin Capitalisation) Rules

The Minister of Finance has further deferred the implementation of Income Tax (Thin Capitalisation) Rules until 31st December 2015.

Letter dated 11th December 2012 from Ministry of Finance