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

The Inland Revenue Board ["IRB"] has recently issued the Public Ruling ["PR"] No. 1/2017 – Income Tax Treatment of GST Part I - Expenses to provide guidance on the income tax treatment of goods and services tax ["GST"] paid or to be paid as:-

- input tax on the acquisition of goods and services (other than capital assets); and
- output tax on sale of goods and services borne by a person if he is registered or liable to be registered under the GST Act 2014 ["the GST Act"].

Hyperlinks

- [Moore Stephens Malaysia](#)
- [Moore Stephens International](#)
- [Inland Revenue Board](#)

- [PR No. 1/2017](#)

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Hyperlinks

Salient points of the above PR include:-

i. Tax Treatment on GST Incurred on Acquisition of Goods and Services

- Sections 39(1)(o) of the Income Tax Act 1967 [“the Act”] provides that input tax paid or to be paid on acquisition of goods and services by a person who is:-
 - liable to be registered under the GST Act but failed to do so; or
 - registered under the GST Act and entitled under that Act to claim the input tax credit,
 is not admissible for tax deduction.
- Input tax not claimable from the Royal Malaysian Customs Department [“RMCD”] includes:-
 - input tax in respect of exempt supply;
 - blocked input tax; and
 - input tax in respect of imported services incurred by a non-registered person.

The above input tax incurred would be deductible under Section 33(1) of the Act but subject to any specific prohibitions under Section 39 of the Act.

- In the case where a person fails or chooses not to claim any input tax credit (of which he is entitled to claim from RMCD), he would still be deemed as eligible for such claim. Hence, the input tax incurred is not allowable for tax deduction. For examples:-
 - choose not to claim input tax as the amount incurred is negligible;
 - not claiming input tax as the valid tax invoice is not available;
 - choose not to obtain full tax invoice and claim restricted input tax credit based on simplified tax invoice.
- In cases where a person is liable to be registered under the GST Act but failed to do so or register late, appropriate income tax treatment shall be applied in accordance to the period when the GST is incurred (i.e. before or after he is liable to be registered).
- A person who has made a voluntary registration and approved by RMCD would be regarded as a registered person entitled to claim input tax credit.
- For mixed suppliers (i.e. making both taxable and exempt supplies), unless the *de minimis* rule applies (where the residual input tax would be treated as wholly attributable to taxable supply), the residual input tax attributable to exempt supply (based on annual adjustment) would be allowed for tax deduction, subject to Sections 33(1) and 39 of the Act.

ii. Tax Treatment of Output Tax Borne by a Person

- Sections 39(1)(p) of the Act provides that output tax borne by a person who is registered or liable to be registered under the GST Act is not admissible for tax deduction.
- This includes output tax borne by a person in respect of deemed supplies (e.g. free gifts of more than RM500) and imported services.

Hyperlinks

iii. GST Adjustments Made by RMCD

- After conducting an audit, the following adjustments may be made by RMCD:-
 - the input tax credit claimed is not claimable from RMCD; or
 - the input tax credit that was initially not claimed from RMCD is actually claimable from the RMCD.

The above adjustments would have impact on the GST incurred by that person and hence, income tax adjustments shall be made accordingly.

- Pursuant to Section 91(6) of the Act, the Director General of Inland Revenue ["DGIR"] may at any time:-
 - raise an assessment or reduced assessment for the year of assessment to which the adjustment made by RMCD relates; or
 - if the year to which the adjustment relates cannot be ascertained, give effect to the adjustment made by RMCD in the year of assessment in which such adjustment is discovered by the DGIR.
- As for adjustments made by RMCD in respect of under-declaration of output tax due to:-
 - understatement of output tax (not accounting for output tax on deemed supply or reverse charge);
 - incorrectly application of zero rate or exemption on taxable supply; or
 - under-declaration of sales,
 the additional output tax assessed by RMCD would be disallowed for tax deduction under Section 39(1)(p) of the Act. In addition, assessment / additional assessment will be raised for sales under-declared and penalties for incorrect return or wilful evasion will be imposed by the IRB.
- Penalty imposed by RMCD is not admissible for tax deduction.

iv. Bad Debt Relief

- GST not recoverable from RMCD by way of bad debt relief is not allowable for tax deduction.

v. Documentation Required

- Documents to be kept to substantiate the claim for tax deduction in respect of input tax incurred are:-
 - GST return form (GST-03 / GST-04);
 - Tax invoice;
 - Adjustments on input tax made by RMCD;
 - Report on tax codes used in the accounting system;
 - Reconciliation of GST-03 and income statement;
 - GST audit file; and
 - Other relevant documents.

A summary of GST credits / blocked input tax and income tax treatment is provided in Appendices 1 and 2 of the abovementioned PR.

Hyperlinks

➤ [PR No. 2/2017](#)

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

The IRB has recently issued the PR No. 2/2017 – Income Tax Treatment of GST Part II – Qualifying Expenditure for Purposes of Claiming Allowances to provide guidance on the tax treatment of GST in respect of the qualifying expenditure incurred on the purchase or acquisition of capital assets for the purposes of claiming allowances.

Salient points of the abovementioned PR include:-

- i. Capital Assets, Capital Goods and Capital Goods Adjustments ["CGA"]
 - Capital asset includes:-
 - all goods that can be capitalised under the Generally Accepted Accounting Principles ["GAAP"];
 - any capital goods used by a person in the course or furtherance of a business;
 - any capital goods not solely for the purposes of selling;
 - any capital goods valued at RM100,000 and above per unit excluding GST; and
 - any capital goods which do not fall under disallowed goods by the Director General of Customs for CGA purposes.
 - The GST treatment on capital goods are as follows:-
 - a supply (acquisition) of capital goods is standard-rated;
 - input tax can be claimed in full on all capital goods acquired that are used to make wholly taxable supplies;
 - if capital goods acquired are used solely for exempt supply, no input tax can be claimed;
 - where capital goods acquired are used for making both taxable and exempt supplies, input tax would need to be apportioned according to its proportional use; and
 - intangible assets such as trademark and goodwill are taxable supplies.
 - CGA is the adjustment to the initial amount of input tax claimed during a specified period if there is a change in the proportion of the capital goods on taxable supplies.
 - A GST registered person who is a mixed supplier is required to account for input tax in accordance with the CGA if:-
 - he acquires, imports, manufactures, produces, constructs, or appropriates for use a capital asset;
 - the capital asset is used for making both taxable and exempt supplies; and
 - the proportion of taxable use of the capital asset changes over time.

Hyperlinks

- CGA does not apply in the following cases:-
 - when a registered person makes wholly taxable supply;
 - when a mixed supplier acquires a capital asset to be used solely for making exempt or taxable supply;
 - when an asset is acquired or import solely for resale;
 - asset acquire for non-business purposes;
 - asset acquired is excluded from input tax credit (blocked input tax), e.g. passenger motor vehicle;
 - when the value of a capital asset acquired is less than RM100,000 excluding GST; and
 - asset acquired is an exempt supply.
- ii. Tax Treatment of GST Incurred on the Acquisition of Capital Assets and Qualifying Expenditure ["QE"]
- Effective year of assessment ["YA"] 2015, QE incurred by a person shall not include any amount paid or to be paid in respect of GST by a person if:-
 - the person is entitled to the input tax credit under the GST Act; or
 - he is liable to be registered under the GST Act but failed to do so.
 - Generally, for capital assets used in a business by a GST-registered person, the input tax that is not claimable under the GST Act is considered part of the QE for the purposes of allowances under the Act.
 - However, input tax that is claimable under the GST Act in respect of the capital assets acquired would not be considered as part of the QE of the assets.
 - For a company which is liable to register for GST but registers late, the capital assets acquired before the registration date shall not include the input tax credit as part of the QE of the assets even though the assets were acquired to be used in making exempt supplies. The above income tax treatment is maintained in respect of the input tax credit attributable to the capital assets, even though the company is to be registered subsequently.
 - For a company that changes from not liable to liable to register for GST purposes, the QE of the assets acquired previously, i.e. before the company is liable to register, has to be adjusted to exclude the GST claimable which was previously included as part of the QE.
- iii. Income Tax Adjustment in relation to CGA
- The determination of the QE and claim of allowance for assets used in making mixed supplies are as follows:-
 - the usage of the asset in the first year will be the basis for determining the QE and the computation of allowance; and
 - the adjustment will only be made once in the last year the CGA is made or on the date the said asset is disposed of, i.e. when the actual input tax claimable from RMCD can be determined with certainty.

Hyperlinks

- Where an additional amount of input tax credit is not claimable under the GST Act, such amount shall be deemed to be part of the QE incurred, and the residual expenditure in relation to the asset shall include that additional sum, and vice versa.
 - If the amount of the capital allowance made or ought to have been made exceeds the residual expenditure, the excess shall be part of the statutory income of that person from a source consisting of a business in the basis period the adjustment is made.
- iv. Control Transfer
- Where there is a transfer of assets between related parties, the acquirer is deemed to have incurred the QE in relation to the asset of an amount equal to the residual expenditure of the disposer after the CGA.
- v. Reinvestment Allowance ["RA"]
- The adjustment to the RA claim is made in the final period of the CGA. If there is a reduction in RA claim, the difference shall be taxed as part of the statutory income of the person in the year where the CGA adjustment is made.

Tax Audit Framework

The IRB has recently issued the Tax Audit Framework (Amendment 1/2017) on 1st May 2017. This amended tax audit framework replaces the tax audit framework issued in February 2015 with some updates as follows:-

- i. Besides the taxpayer's premises, field audit can take place at the IRB office or any location agreed by both parties.
- ii. The years of assessment to be covered during tax audit has been extended from a year of assessment to 3 years of assessment covering all aspects.
- iii. Commencement of a tax audit:-
 - For field audit, it is deemed to have commenced from the date of the letter requesting for documents or from the first day of the visit to the taxpayer's premises (in the absence of letter of request for documents).
 - For desk audit, it is deemed to have commenced from the date of notification via Form CP800 / CP800A.
 - The IRB can visit the taxpayer's premises or any of the premises connected to the taxpayer without any further notice in the event that there is no response within 21 days from the date of the letter / Form CP800 / CP800A.
 - The taxpayer selected for audit will be notified at least 14 days before audit visit. However, the IRB can also carry out the audit without any prior notification.

- [Tax Audit Framework \(Amendment 1/2017\) \(in Bahasa Malaysia\)](#)

Hyperlinks

- iv. Example of the cases where taxpayer will be listed under Monitoring Deliberate Tax Defaulters Programme ["MDTD"] are:-
- Audit findings with penalty imposed for company, other than company and employment cases (excluding relief and rebates);
 - Incomplete records;
 - Failure to insert the correct business code or no business code is indicated in the tax return form.
- v. Offences and penalty rates for under-statement or omission of income are summarised as follows:-

Disclosure/ Discovery	Period from the due date of submitting tax return	Rate of penalty on tax undercharged
<ul style="list-style-type: none"> • Voluntary disclosure before case is selected for tax audit 	<ul style="list-style-type: none"> • Within 60 days 	10%
	<ul style="list-style-type: none"> • > 60 days but not later than 6 months 	15.5%
	<ul style="list-style-type: none"> • > 6 months 	35%
<ul style="list-style-type: none"> • Non-disclosure (discovery of omission during tax audit) 		45% / 100%
<ul style="list-style-type: none"> • Repeated offences under the MDTD cases 		100%

- vi. The concessionary penalty rates under voluntary disclosure only apply to taxpayers who have submitted their tax returns on or before the stipulated due date.
- vii. Voluntary disclosure will not be accepted by IRB once the tax audit has commenced

The above Tax Audit Framework (Amendment 1/2017) takes effect from 1st May 2017.

Note: For further information on the Tax Audit Framework, kindly refer to our Tax Flash – April 2015 issue.

➤ [Tax Flash – April 2015](#)

Tax Exemption on Income Derived from Group Inclusive Tour Package

Pursuant to the Income Tax (Exemption) (No. 12) Order 2016, tax exemption is granted to a company resident in Malaysia in respect of its income derived from tour operating business which provides domestic tour packages of not less than 1,500 **local tourist** in the basis period for a year of assessment.

The Income Tax (Exemption) (No. 12) 2016 (Amendment) Order 2017 has been gazetted to replace the words “tourist from outside Malaysia” with “local tourist” in Paragraph 5 of the previous Order in line with the above.

Note: For further information on the above exemption of income, kindly refer to our *Tax Flash – January 2017* issue.

IRB’s Media Release on Imposition of 100% Penalty for Failure to Declare Income and Correct Information

The IRB has recently issued a media release dated 17th April 2017 to clarify on the imposition of 100% penalty for the offence for failure to declare income or correct information which will be implemented with effect from 1st January 2018 as a step towards elevating the level of voluntary compliance among taxpayers.

Hyperlinks

- [Income Tax \(Exemption\) \(No. 12\) 2016 \(Amendment\) Order 2017](#)
- [Tax Flash – January 2017](#)
- [IRB’s Media Release dated 17th April 2017](#)

This publication is provided gratuitously and without liability. It is intended as a general guide only and the application of its contents to specific situations will depend on the particular circumstances involved. Readers should seek appropriate professional advice regarding any particular problems that they encounter, and this tax update should not be relied on as a substitute for advice. Accordingly, Advent MS Tax Consultants Sdn Bhd assumes no responsibility for any errors or omissions it may contain, whether caused by negligence or otherwise, or for any losses, however caused, sustained by any person that relies on it. Should further information, clarification or advice be required on any of the contents stated herein, please feel free to contact our tax team.