



# Tax Flash



January 2012

## PR No. 10/2011 – Gratuity

The Inland Revenue Board [“IRB”] has recently issued the Public Ruling [“PR”] No. 10/2011 – Gratuity. This PR provides guidance on the method used to characterise lump sum payments received by employees upon termination of their employment and the tax treatment of gratuity.

Salient points of the abovementioned PR include:-

- i. Lump Sum Payment on Termination of Employment
  - The circumstances and nature of the lump sum payment made by employer on termination of employment must be reviewed to determine the real character of the payment.
  - Lump sum payment on the termination of an employment may consist of the following elements:-
    - Payment attributable to the loss of employment such as redundancy (compensation); and
    - Payment attributable to the past services of the employee (gratuity).
- ii. Situation for Payment of Gratuity
  - When an individual ceases employment upon resignation or retirement, the payment received by him in respect of past services would generally be characterised as gratuity.
- iii. Determination of Elements of Gratuity and Compensation
  - The method used in the apportionment of a lump sum payment between gratuity and compensation depends on the circumstances of each case. Generally, the employer’s normal practice in granting gratuities to employees leaving services will be considered first in determining the amount of gratuity and the balance will be considered as compensation.

### Hyperlinks

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### References

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- A lump sum payment received due to premature termination of an employment which has the prospect of continuing up to the retirement age is treated as compensation for loss of employment.
- Any lump sum paid to the employee upon expiry of the contract of employment or upon reaching the retirement age should not be treated as compensation for loss of employment.

iv. Tax Treatment of Gratuity

- Gratuity forms part of gross income from an employment under Section 13(1)(a) of the Income Tax Act 1967 [“the Act”]. However, gratuity received upon retirement from employment would be exempted from tax pursuant to Paragraph 25(1), Schedule 6 of the Act if:-
  - the Director General [“DG”] is satisfied that the retirement was due to ill-health;
  - the retirement takes place on or after reaching the age of 55, or on reaching the compulsory age of retirement from employment satisfied under any written law and in either case from an employment which has lasted 10 years with the same employer or with companies in the same group; or
  - the retirement takes place on reaching the compulsory age of retirement pursuant to a contract of employment or collective agreement at the age of 50 but before 55 and that employment has lasted for 10 years with the same employer or with companies in the same group.
- Gratuity that is not exempted from tax under Paragraph 25(1), Schedule 6 of the Act will be taxed in the relevant basis period pursuant to Section 25(4) of the Act. A lump sum payment received by an employee on cessation of his employment by way of gratuity, deferred pay, or otherwise, [other than gross income under Section 13(1)(d) or (e) of the Act] will be:-
  - spread over the last 6 basis periods if the employment commenced more than 5 years before the beginning of the basis period in which the employment ceased; or
  - spread over the period of employment, including periods during which the employee was employed by a different company, but within the same group of companies.

v. Gratuity Payment Credited to EPF

- In a situation where gratuity (either compulsory or optional) is credited to the employee's Employees Provident Fund ["EPF"] account when a resignation takes place prior to retirement, the gratuity accrues as income at the time when the payment arises and subject to tax under Section 25(4) of the Act.
- Employers are required to credit the net amount (after deducting income tax) to the EPF account.
- To determine the amount of tax to be deducted, employers are required to file the Notification of Cessation of Employment (Employment of Private Sector Employees) ["Form 22A"] to the IRB. The employer must withhold the money payable to the employee until a tax clearance letter is received from the IRB.

The above PR takes effect from the year of assessment ["YA"] 2011.

**PR No.11/2011 – Bilateral Credit and Unilateral Credit**

The IRB has recently issued the PR No.11/2011 – Bilateral and Unilateral Credit which provides guidance on the bilateral credit and unilateral credit that may be claimed by a person who has been charged to tax on the same income in Malaysia and in another country.

Salient points of the abovementioned PR include:-

i. Double Taxation Agreement ["DTA"]

- Double taxation occurs when two countries impose income tax with respect to the same income on the same taxable person.
- To mitigate the effects of double taxation on its residents deriving income from outside its own national boundary, many countries including Malaysia have entered into Agreements for the Avoidance of Double Taxation.
- Under a DTA, if the income is taxable in both countries, a relief is given by way of credit known as bilateral credit.
- Where there is no DTA between Malaysia and a foreign country, a claim for unilateral credit may be made if the income is taxable in both countries.

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ii. Bilateral Credit

- Bilateral credit can be claimed by a person resident in Malaysia for the basis year for a YA.
- Where foreign income is charged to Malaysian tax for more than one YA or is charged to foreign tax more than once, bilateral credit may be allowed for the YA in respect of the total amount of foreign tax charged on that foreign income provided that:-
  - the credit so allowed must not exceed the total amount of Malaysian tax charged on that foreign income; and
  - if any credit has been allowed for the YA for foreign tax, no further credit is given for the same tax for any other YA.
- Any claim for bilateral credit for a YA has to be made in writing within 2 years after the end of that YA.
- If the person is aggrieved by the decision of the DG on the claim, he may appeal within 6 months after being informed of the decision and request the DG to send the application to the Special Commissioners of Income Tax in accordance with Section 131(5) of the Act.
- If the bilateral credit allowed is excessive or insufficient as a result of any adjustment made to the amount of Malaysian tax or foreign tax, an application for relief or a notice of appeal may be made or given not more than 2 years after the time when all such assessments, adjustments or other determinations have been made.
- The formula for computation of bilateral credit is as follows :-

$$\frac{\text{Foreign income (statutory income) (Note)}}{\text{Total income}} \times \text{Malaysian tax payable (before bilateral credit)}$$

Or

Foreign tax charged in respect of the foreign income, whichever is lower.

**Note** : Foreign income for the purposes of claiming bilateral credit includes income derived from Malaysia and charged to foreign tax

iii. Unilateral Credit

- Unilateral credit can be claimed by a person resident in Malaysia in the basis year for a YA. However, unilateral credit relief may be allowed to an employee who is charged to Malaysian tax and foreign tax in respect of the same income from an employment exercised outside Malaysia, whether or not he was resident for the basis year for the YA.
- The formula for computation of unilateral credit is as follows:-

$$\frac{\text{Foreign income (statutory income) (Note)}}{\text{Total income}} \times \text{Malaysian tax payable (before unilateral credit)}$$

Or

$\frac{1}{2}$  X foreign tax, whichever is lower.

**Note** : Foreign income for the purposes of claiming bilateral credit includes income derived from Malaysia and charged to foreign tax

- Other than the above, unilateral credit shall be allowed in the same way as bilateral credit

iv. Foreign Sourced Income and Remittance

- Tax residents of Malaysia in receipt of foreign sourced remittances which are exempt from tax pursuant to Paragraph 28, Schedule 6 of the Act are not eligible to claim bilateral credit or unilateral credit as the remittance had not been subject to Malaysian tax.

v. Documents Required For Double Taxation Relief Claim

- Any of the following documents may be submitted to substantiate the foreign tax suffered by taxpayers to compute bilateral or unilateral credit:-
  - notice of assessment from the foreign tax authority or receipt for the tax paid; or
  - statement from the foreign tax authority setting out the particulars that would normally be recorded on a notice of assessment or receipt for payment.

The above PR takes effect from the YA 2011.



## **PR No. 12/2011 – Tax Exemption on Employment Income of Non-Citizen Individuals Working for Certain Companies in Malaysia**

The IRB has recently issued the PR No. 12/2011 – Tax Exemption on Employment Income of Non-Citizen Individuals Working for Certain Companies in Malaysia. This PR provides guidance on the tax treatment of employment income derived by non-citizen individuals working for an Operational Headquarters Company ["OHQ"], Regional Office ["RO"], International Procurement Centre Company ["IPC"] or Regional Distribution Centre Company ["RDC"] in Malaysia.

Salient points of the abovementioned PR include:-

### **i. Non-Citizen Individuals Working with Certain Companies**

- Effective YA 2003, non-citizen individuals working at an OHQ and RO are exempted from the payment of income tax in respect of the portion of their chargeable income attributable to the number of days they exercise their employment outside Malaysia. Hence, they are taxed only on the portion of their chargeable income attributable to the number of days they exercise employment in Malaysia [Income Tax (Exemption) (No. 6) Order 2003].
- Effective YA 2008, the above special tax treatment is extended to non-citizen individuals who are employed by an IPC and RDC [Income Tax (Exemption) (No. 2) Order 2008].

### **ii. Computation of Tax Exempt Income**

- The income of a non-citizen individual from an employment with an OHQ, RO, IPC or RDC exercised by him in Malaysia would be tax exempt in accordance with Paragraph 21, Schedule 6 of the Act if his employment is:-
  - for a period or periods which together do not exceed 60 days in a basis year for a YA;
  - for a continuous period not exceeding 60 days which overlaps over 2 successive years of assessment; or
  - for a continuous period not exceeding 60 days which overlaps over 2 successive years of assessment and for a period or periods which together with that continuous period do not exceed 60 days.
- The income of a non-citizen individual from an employment with an OHQ, RO, IPC or RDC exercised by him in Malaysia would be subject to tax if the period of employment under the abovementioned circumstances exceeds 60 days. However, he will be taxed only on the portion of his chargeable income attributable to the number of days he exercises employment in Malaysia.

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- The amount of income exempted in respect of the employment exercised outside Malaysia is determined in accordance with the following formula:-

$$\frac{A}{B} \times C$$

Where,

- A – Number of days in the YA he is in employment with the OHQ, RO, IPC or RDC exercised outside Malaysia;  
(The number of days outside Malaysia does not include vacation leave overseas)
  - B – Number of days in the YA he is in employment with the OHQ, RO, IPC or RDC;  
(The number of days is the entire period of employment inclusive of vacation leave overseas)
  - C – Chargeable income for a YA attributable to an OHQ, RO, IPC or RDC.
- If a non-citizen individual has sources of income other than that of employment with an OHQ, RO, IPC or RDC, the chargeable income (C) shall be determined in accordance with the following formula:-

$$\frac{D}{E} \times F$$

Where,

- D – Gross income from employment with the OHQ, RO, IPC or RDC for a YA;
- E – Total gross income from all sources for a YA; and
- F – Chargeable income for a YA in respect of gross income from all sources.

### iii. Documents Required for Claim of Exemption

- Documents that may be acceptable to substantiate a claim for exemption are a copy of the employment contract and a confirmation from the employer as to the number of days the employment is exercised in Malaysia and outside Malaysia.

The above PR takes effect from the YA 2011.

### **Guidelines on SIP Tax Incentive**

Following the 2012 Budget announcement, Talent Corporation Malaysia Berhad ["TalentCorp"] has recently issued the Guidelines on Structured Internship Programme ["SIP"] Tax Incentive to provide guidance for companies (including partnerships) participating in the SIP and eligibility to claim for double deduction of the expenses incurred on SIP.

Pertinent points of the abovementioned guidelines include:-

- i. Qualifying criteria for the participating companies (including partnerships):-
  - Share capital of at least RM 2.5 million.
  - Average revenue record of RM 21 million and more over the past 3 years.
  - Headcount:-
    - For non-manufacturing companies - at least 50 full-time employees; or
    - For manufacturing companies - at least 100 full-time employees.
  - Must have been established for 5 years and more (3 to 5 years may be considered).
- ii. Application for endorsement must be submitted online to TalentCorp together with the following documents:-
  - Company search results from the Companies Commission of Malaysia (dated within 14 days from the date of application).
  - A write-up of the SIP to detail out the following:-
    - Objectives of the programme;
    - Programme framework;
    - Process and procedures;
    - Internal policy;
    - Assessment of the interns during the training; and
    - Allowances.
- iii. The participating intern / student must:-
  - be a Malaysian citizen;
  - be pursuing a degree programme (or equivalent as defined by TalentCorp) on full-time basis in a local based university; and
  - complete the approved internship programme before completion of his final semester of his degree (and equivalent) programme.



- iv. The claim for double deduction on expenses incurred on the internship programme will be granted in the YA in which the endorsement is issued.
- v. Each intern must be given a minimum of cash or / and cash equivalent of RM500 monthly allowance.
- vi. The claim for double deduction on other direct expenses (i.e. meals, transport and accommodation allowances, training offered during the internship programme, payment to outsourced party running or administering the programme) limited to a maximum average total expenses of RM5,000 per student per YA will be allowed.
- vii. Participating companies must also observe the necessary criteria when designing its SIP.
- viii. For the purposes of making a claim for the double deduction on expenses incurred on SIP, the claimant must:-
  - attach the Letter of Endorsement from TalentCorp; and
  - ensure that the following supporting documents (non-exhaustive) are available to substantiate the double deduction claim:-
    - Proof of attendance during the internship.
    - Proof of expenses incurred for the interns such as cash, meals, transport, and accommodation allowances, i.e. receipts, etc.
    - Proof of training incurred during the internship.
    - Proof of payment to outsourced party developing, running or administering the programme.

## **Tax Exemption on Income Derived from Qualifying Professional Services Rendered in Labuan**

Pursuant to the Income Tax (Exemption) (No.6) Order 2011, a person is exempted from tax on 65% of statutory income derived from the provision of qualifying professional services (i.e. legal, accounting, financial or secretarial services) rendered in Labuan to a Labuan entity from the YA 2011 to YA 2020.

Income Tax (Exemption)  
(No. 6) Order 2011

## **Tax Exemption on Director Fees Received from a Labuan Entity**

Pursuant to the Income Tax (Exemption) (No. 7) Order 2011, an individual who is a non-Malaysian citizen is exempted from the payment of income tax in respect of fees received in his capacity as a director of a Labuan entity from the YA 2011 to YA 2020.

Income Tax (Exemption)  
(No. 7) Order 2011



## **Tax Exemption for Income from Employment in a Managerial Capacity with a Labuan Entity, Co-located Office or Marketing Office**

Pursuant to the Income Tax (Exemption) (No. 8) Order 2011, an individual who is a non-Malaysian citizen is exempted from the payment of income tax on 50% of gross income from exercising an employment in a managerial capacity with a Labuan entity in Labuan, co-located office or marketing office from the YA 2011 to YA 2020.

“co-located office” means a co-located office of a Labuan entity approved by the Labuan Financial Services Authority which operates in other parts of Malaysia to perform the functions assigned by the Labuan entity.

“marketing office” means a marketing office of a Labuan entity approved by the Labuan Financial Services Authority which is located in other parts of Malaysia to facilitate meetings with clients and establish contracts with potential clients except exercising trading activities on behalf of the Labuan entity.

## **Tax Exemption for Housing Allowance and Labuan Territory Allowance Received from a Labuan Entity**

Pursuant to the Income Tax (Exemption) (No.9) Order 2011, an individual who is a Malaysian citizen is exempted from the payment of income tax on 50% of the gross housing allowance and gross Labuan Territory allowance received from exercising an employment in Labuan with a Labuan entity from the YA 2011 to YA 2020.

## **Deduction for Implementation of RosettaNet**

The Income Tax (Deduction for Implementation of RosettaNet) (Revocation) Rules 2011 have been gazetted to revoke the Income Tax (Deduction for Implementation of RosettaNet) Rules 2004 which previously allowed a qualifying company a deduction for the expenses incurred for the purpose of implementation of RosettaNet.

The above revocation Rules shall have effect from the YA 2012.

Income Tax (Exemption)  
(No. 8) Order 2011

Income Tax (Exemption)  
(No. 9) Order 2011

Income Tax (Deduction for  
Implementation of  
RosettaNet) (Revocation)  
Rules 2011



### Review of RPGT Rates

With the gazette of Real Property Gains Tax (Exemption) Order 2011 following the 2012 Budget announcement, the Real Property Gains Tax ["RPGT"] rates on the gains from the disposal of chargeable assets (including shares in a real property company) on or after 1<sup>st</sup> January 2012 will be revised to:-

- 10% for holding period up to 2 years;
- 5% for holding period exceeding 2 years but within 5 years;
- 0% for holding period exceeding 5 years.

It is noteworthy that the above revised rates apply to disposal of all chargeable assets instead of only residential and commercial properties as proposed in the 2012 Budget.

The above Order comes into operation on 1<sup>st</sup> January 2012 and the RPGT (Exemption) (No. 2) Order 2009 is revoked.

### Increase of Rate of Employer's Contribution to EPF

From January 2012 onwards, the rate of the employer's contribution to the EPF for employees below the age of 55 earning a monthly wage of not exceeding RM5,000 will be increased from 12% to 13%.

For employees who are 55 years and above and earning a monthly wage of not exceeding RM5,000, the rate of the employer's contribution to EPF will also be increased from 6% to 6.5%.

"wage" is defined in Section 2 of the EPF Act 1991 as all remuneration in money, due to an employee under his contract of service or apprenticeship whether agreed to be paid monthly, weekly, daily or otherwise and includes any bonus, commission or allowance payable by the employer to the employee.

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