MOORE Advent

TAX FLASH

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Updated Guidelines on Restriction on Deductibility of Interest

Following the gazettement of the Income Tax (Restriction on Deductibility of Interest) (Amendment) Rules 2022 ["amendment Rules"] on 31st January 2022, the IRB has updated the *Restriction on Deductibility of Interest Guidelines* (uploaded on 22nd August 2022) to incorporate the changes made in relation to the restriction of interest deduction from the gross income of a person for any financial assistance in a controlled transaction in respect of his business income for a year of assessment.

The salient amendments included in the above updated Guidelines are as follows:-

i. Ascertainment of Tax-EBITDA

- The maximum amount of interest allowable under Section 140C of the Income Tax Act 1967 ["ITA 1967"] shall be an amount equal to 20% of Tax-EBITDA of a business source of a person for the basis period for a year of assessment which is ascertained in accordance with the formula as below:-

  Tax-EBITDA = A + B + C

  Where,

  A is the amount of the adjusted income of a person from a business source for the basis period for a year of assessment before any restriction on deductibility of interest under Section 140C of the ITA 1967 is made;

  B is the total amount of qualifying deductions allowed in ascertaining the amount of the adjusted income in A; and

  C is the total amount of interest expense incurred in relation to the gross income of a person for any financial assistance in a controlled transaction from a business source for the basis period for a year of assessment.

- "**Qualifying Deduction**" (in "B" above) has been redefined as:-
  - where there is business expenditure incurred in the profit and loss account ["P&L"] is allowed as deduction under the ITA 1967 and the amount of the deduction allowed exceeds the amount of the business expenditure incurred, an amount equal to the difference between the amount of the deduction allowed and the amount of the business expenditure incurred in the P&L account; or
  - where there is no business expenditure incurred in the P&L account, the amount of deduction allowable under the ITA 1967.

ii. Scope of Application of Interest Expense

- The scope of interest expense subject to restriction under Section 140C of the ITA 1967 has been amended i.e. applicable to interest expense which is "due to be paid" in line with the tax treatment of interest expenses under Section 33(4) and Section 33(5) of the ITA 1967.
- Any interest not due to be paid in a particular year of assessment would have been excluded in the computation of adjusted income (in "A" above) as provided under Section 33(4) and Section 33(5) of the ITA 1967 and hence, excluded from the computation of total amount of interest expense incurred in relation to gross income of a person for financial assistance in a controlled transaction from business source subject to restriction of interest under Section 140C of the ITA 1967 (in "C" above).
- When the interest payable is due to be paid, a revision of the assessment will be made to allow a deduction of the interest expense for the relevant year of assessment and hence a revision of the Tax-EBITDA will have to be made.

iii. Effective Date

- The amendments [i.e. in respect of (i) above] made under the amendment Rules shall have effect for the basis period beginning on or after 1st February 2022.

Note: *For further details, kindly refer to our Tax Flash – July 2019 and Tax Flash – March 2022 issues.*

Guidelines on Tax Treatment of Digital Currency Transactions

The Inland Revenue Board ["IRB"] has issued the *Guidelines on Tax Treatment of Digital Currency Transactions* dated 26th August 2022 to provide guidance on income tax treatment in respect of e-Commerce transactions. The Guidelines apply to any person that acquire or dispose digital currencies as well as involve in business of digital currencies such as trading, mining and exchanges of digital currencies.

For the purpose of the Guidelines, the IRB makes reference to the definitions of digital currency and digital token by the Securities Commission Malaysia as follows:-

"**Digital currency**" means a representation of value which is recorded on a distributed ledger whether cryptographically-secured or otherwise, that functions as a medium of exchange and is interchangeable with any money, including the crediting or debiting of an account.

"**Digital token**" means a representation which is recorded on a distributed ledger whether cryptographically-secured or otherwise.

The terms "digital currencies" and "digital tokens" are used interchangeably in the Guidelines and they include digital currencies such as Bitcoin, Ethereum ["Ether"].

Salient points of the abovementioned Guidelines include:-

i. General Tax Treatment on Acquisitions and Disposals of Digital Currencies

- Generally, the taxability of digital currency transactions in Malaysia is based on Section 3 of the ITA 1967 where income of any person accruing in or derived from Malaysia or received in Malaysia from outside of Malaysia is taxable. The IRB regards the transactions involving digital currency to be subjected to Malaysian tax if:-
  - the key activities and business operations are performed in Malaysia; or
  - where there is a business presence in Malaysia.
- The IRB applies the following badges of trade in determining whether the gain or loss from the disposal of digital currencies is capital or revenue in nature:-
  - nature of subject matter;
  - length of ownership;
  - frequency of transactions;
  - supplementary work;
  - circumstances of the realization;
  - motive;
  - mode of financing; and
  - other factors.
- A person who actively trades in digital currencies may be viewed as generating revenue from the activity thus gains from this trading activity are taxable, whereas gains derived by an individual who trades occasionally may be viewed as capital gains not subject to tax in Malaysia.

ii. Tax Treatment for Specific Business Transactions

- Trading of digital currencies
  - Businesses that buy and sell digital currencies in the ordinary course of their businesses will be taxed on the profit derived from trading in the digital currencies similar to the trading of stock. Any expenses incurred in the production of the taxable income or losses incurred from the digital currencies trading activity would be tax deductible.
- Mining of digital currencies
  - The taxability of a miner's profit from the disposal of payment tokens would depend on whether the gain is capital or revenue in nature based on badges of trade.
- Business transactions in digital currencies
  - Businesses that accept digital currencies as a mode of payment for goods or services should record the sales based on the open market value of the goods and services in Ringgit Malaysia ["MYR"]. The same applies to payment of expenses and purchases of assets by the business.
  - In situations where the transactions are agreed based on number of digital currencies, the value of the goods sold or purchased, or the contract of services are determined based on the value of the digital currencies at the point of transactions.
- Paying salaries and wages to employees in digital currencies
  - Salaries and wages paid in digital currencies are taxable in the hands on the employees and deductible to the employer based on the value stated in the employment contract and the employment services performed.
  - The employer's responsibilities under the Monthly Tax Deductions Rules remains applicable even if the salaries and wages are paid in digital currencies.

iii. Tax Treatment for Investment in Digital Currencies

- A person's investments in digital currencies and digital tokens are considered to be a business activity of that person, if the investments activities are continuous, systematic, active, carry a financial risk and are aimed at making a profit.
- The taxability of a profit from the investment would depend on whether the gain is capital or revenue in nature based on badges of trade.

iv. Tax Treatment for Certain Situations

- Mere acquisition and disposal of digital currencies
  - When a person buys digital currencies merely as part or full payment of any goods and services, the disposal of digital currencies in such situation is not subject to tax.
- Receiving digital currencies as a result of free distribution or splitting
  - A person may receive digital currency for free as a promotion or marketing tools or splitting of existing digital currency such as airdrop and hardfork. These tokens are not considered as an income to the recipient, thus not taxable at the time of receipt.
- Exchanges of digital currencies
  - Where there is a conversion of one digital currency to another digital currency, any gain or loss arising from the conversion may be subject to tax, depending on whether the digital currency was held as a capital or revenue asset.

v. Acquisition Cost of Digital Currency

- The acquisition cost of digital currencies is to be determined in MYR and on the basis of the First In, First Out ["FIFO"] principle unless the movement of the digital currencies can be proven otherwise.
- If the acquisition cost of the current asset cannot be determined, the digital currency will be valued using fair value, i.e. at the rate in force on the day of the transaction and based on the acceptable and verifiable digital currency exchanges.

vi. Digital Currency with No Published Value

- Where digital currency is received in exchange for property or services and that digital currency is not traded on any digital currency exchange (i.e. no published value), then the fair value of the digital currency received is equal to the fair value of the property or services exchanged for the digital currency when the transaction occurs.

vii. Record Keeping

- Taxpayers are required to keep the necessary supporting documents / records in relation to digital currency for tax purposes.

Updated FAQ on Remittance of 2% Withholding Tax on Payments Made by a Company to Agents, Dealers or Distributors

The IRB has earlier issued a media release on 9th July 2022 to announce certain administrative changes on the remittance of the withholding tax ["WT"] on payments made by a company to agents, dealers or distributors ["ADDs"].

Following the above announcement, the IRB has revised the *FAQ on Remittance of 2% WT on Payments Made by a Company to ADDs (Updated on 19th August 2022)* to take into account the administrative change as announced in the media release where companies are required to accumulate and remit the 2% WT applicable on payments to ADDs on monthly basis by the last day of the following month, commencing from the month of July 2022 as illustrated below:-

Accumulated 2% WT on Monthly Basis	Due Date for Remittance
01.01.2022 to 31.07.2022	31.08.2022
01.08.2022 to 31.08.2022	30.09.2022
01.09.2022 to 30.09.2022	31.10.2022

Prior to making the 2% WT payment, the payer companies are required to furnish the Form CP107D - Pin 2/2022 in PDF format and Appendix CP107D(2) in Excel format via email to the relevant payment centres as below:-

Payment Centres	Email Address
Kuala Lumpur Payment Centre	pbkl-cp107d@hasil.gov.my
Kuching Branch	pbkc-cp107d@hasil.gov.my
Kota Kinabalu Branch	pbkk-cp107d@hasil.gov.my

Note: *For further information, kindly refer to our Tax Flash - August 2022 issue.*

Automatic Exchange of Financial Account Information Between the Government of Malaysia and the Government of the United States of America to Improve International Tax Compliance and to Implement the Foreign Account Tax Compliance Act

The Foreign Account Tax Compliance Act ["FATCA"] requires all the financial institutions ["FIs"] outside the United States of America ["USA"] to provide information regarding their customers who are USA persons to the US Internal Revenue Service with the aims at reducing tax evasion by USA persons.

The Malaysia – USA Intergovernmental Agreement was signed on 21st July 2021 to implement the FATCA. Following this, the following legislations have been gazetted in connection with the implementation of provisions on the obligations arising under the aforesaid Agreement:-

- *Income Tax (Agreement Between the Government of Malaysia and the Government of USA to Improve International Tax Compliance and to Implement the FATCA) Order 2022*; and
- *Income Tax (Automatic Exchange of Financial Account Information Between the Government of Malaysia and the Government of the United States of America to Improve International Tax Compliance and to Implement the Foreign Account Tax Compliance Act) Rules 2022*.

Similarly, the *Labuan Business Activity Tax (Automatic Exchange of Financial Account Information between the Government of Malaysia and the Government of the United States of America to Improve International Tax Compliance and to Implement the Foreign Account Tax Compliance Act) Regulations 2022* has been gazetted to apply to Labuan entities for the same purpose.

The above Rules and Regulations apply to Malaysian FIs and set out the obligations to be complied with. Every reporting Malaysian FI shall:-

(a) in respect of the calendar year 2014 to calendar year 2022, furnish a return to the Director General, on or before 30 June 2023; and
(b) in respect of every following calendar year, furnish a return to the Director General, on or before 30 June of the year following the end of the calendar year to which the return relates.

The return shall set out the required information that is maintained by the Reporting Malaysian FIs at any time during the relevant calendar year.

Sales Tax Policy No. 2/2022

The Royal Malaysian Customs Department ["RMCD"] has published the *Sales Tax Policy No. 2/2022* dated 24th August 2022 (currently only made available in *Bahasa Malaysia*) in respect of facilitation of dropshipment activity.

The salient points pertaining to the abovementioned sales tax policy are as summarised below:-

i. A registered manufacturer ["RM"] who exports taxable finished goods produced or manufactured is exempt from payment of sales tax under Item 56 to Schedule A of the Sales Tax (Persons Exempted from Payment of Tax) Order 2018.
ii. The exemption is also applicable to a RM who exports its finished goods that are sold to a trader in Malaysia. This situation occurs when a trader receives a purchase order from his customers outside Malaysia. The trader then makes a purchase from the RM and instructs the RM to directly export the finished goods to his customers outside Malaysia from the premises of the RM on his behalf.
iii. The RM is required to issue a sales invoice to the trader without charging sales tax. The details of the invoice must comply with Regulation 7 of the Sales Tax Regulations 2018 by stating the details of the billing party (i.e. "bill to") and the address where the goods are to be delivered to (i.e. "ship to").
iv. This exemption is only applicable to situations where there is only one level of trader, i.e. does not involve other traders who purchase taxable goods from the trader.

v. The Form K2 shall indicate the following:-

Column in Form K2	Details to be Filled
a) Consignor	Name of the RM
b) Consignee	Name of the customer outside Malaysia
c) At the left of Form K2 (near the forwarding agent section)	To indicate it is "care of" the trader and state the name and address of the trader

vi. The Bill of Lading should be filled as per the Form K2 and indicate the trader as the notifying party.

vii. The RM needs to declare the sales value of finished goods exported on behalf of the trader in column 18(a) – Export / Special Area / Designated Area of the Form SST-02.

Service Tax Policy No. 1/2022 (Amendment No. 1)

RMCD has published the *Service Tax Policy No. 1/2022 (Amendment No. 1)* dated 1st August 2022 (currently only made available in *Bahasa Malaysia*) which provides for service tax exemption on the provision of digital payment services by local non-bank service providers.

The amended Service Tax Policy No. 1/2022 was issued to loosen one of the conditions whereby the local non-bank service providers also include those regulated but not licensed by Bank Negara Malaysia ["BNM"] under the Financial Services Act 2013 [*Act 758*] or Islamic Financial Services Act 2013 [*Act 759*].

Note: *For further details, kindly refer to our Tax Flash – August 2022 issues.*

Service Tax Policy No. 2/2022

RMCD has published the *Service Tax Policy No. 2/2022* dated 8th September 2022 (currently only made available in *Bahasa Malaysia*) which provides for full exemption of service tax and facility of service tax refunds to companies operating in Joint Development Area ["JDA"].

The salient points pertaining to the abovementioned service tax policy are as summarised below:-

i. With effect from 15th August 2022, the Minister of Finance ["MOF"] has pursuant to Section 34(3)(b) of the Service Tax Act 2018 determined that companies operating in the JDA are granted facilitation of service tax refund on all taxable services as listed in the Service Tax Regulations 2018, subject to the following conditions:-
   - The services acquired must be used solely for official purposes of the companies operating in the JDA and represent the main and important requirements in managing the JDA's daily affairs and operations. Services used for unofficial/private/personal purpose are not eligible for the service tax refund;
   - For the purposes of control and coordination, the company needs to make a declaration and the Malaysia-Thailand Joint Authority ["MTJA"] needs to make a confirmation that the service is used solely for the official purpose of the company operating in the JDA;
   - The payment for services was made by the companies operating in the JDA;
   - Applications for service tax refund must be made to the Director General of Customs and Excise ["DG"] within the period prescribed by the DG; and
   - The applicant must comply with any other conditions and procedures set by the DG.

ii. An application for service tax refund needs to be submitted to the DG on a quarterly basis (i.e. every 3 months). The application for refund should be submitted not later than the last day of the following month after the end of the 3-month period as follows:-

Period of Services Acquired	Due Date for Application for Service Tax Refund
a) 15th August 2022 to 30th September 2022	31st October 2022
b) 1st October 2022 to 31st December 2022	31st January 2023
c) 1st January 2023 to 31st March 2023	30th April 2023
d) Every subsequent 3 months	Not later than the last day of the following month after the end of the said 3-month period.

Note: Applications submitted after the said period will not be processed for refund claims.

iii. No service tax exemption will be given on imported taxable services including service tax on digital services which is provided by a foreign registered person to MTJA and companies operating in the JDA.

iv. With the coming into operation of this service tax policy, the upfront service tax exemption granted previously via Service Tax Policy No. 1/2021 is only applicable until 14th August 2022.

Note: *For further details, kindly refer to our Tax Flash – June 2021 issues.*