

## In this Issue

- Earning Stripping Rules
- Guidelines for Application of Social Enterprises for Approval under Section 44(11C) of the Act
- Allowance for Increase in Exports
- Further Deduction for Employment of Senior Citizen, Ex-Convict, Parolee, Supervised Person and Ex-Drug Dependant
- Extension of Stamp Duty Exemption for the Purchase of Residential Property Valued Between RM300,001 and RM2,500,000 under the National Home Ownership Campaign 2019
- Sales Tax
- Service Tax

## Earning Stripping Rules

The Income Tax (Restriction on Deductibility of Interest) Rules 2019 ["the Rules"] has recently been gazetted to restrict the 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 basis period for a year of assessment. In addition, the Guidelines on Restriction on Deductibility of Interest ["the Guidelines"] has also been issued by the Inland Revenue Board ["IRB"] to provide clarification with regard to the application of the earning stripping rules under the Rules.

Salient points of the abovementioned Rules include:-

## Hyperlinks

- [Moore Stephens Malaysia](#)
- [Moore Stephens International](#)
- [Inland Revenue Board](#)
  
- [Income Tax \(Restriction on Deductibility of Interest\) Rules 2019](#)
- [Guidelines on Restriction on Deductibility of Interest](#)

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## Hyperlinks

- i. Application
  - The above Rules apply to a person who has been granted any financial assistance in a controlled transaction and the total amount of interest expenses from such financial assistance exceeds RM500,000 in a basis period for a year of assessment.
  - Based on the Guidelines, the Rules will only be applicable to the financial assistance granted by associated person(s) outside Malaysia, including the financial assistance granted by an independent lender outside Malaysia where the holding company (or its related company) is the guarantor for such financial assistance.
- ii. Non-Application
  - The Rules shall not apply to:-
    - an individual;
    - a licenced financial institution such as bank, insurer, reinsurer, *takaful* and *retakaful* operator (including Labuan financial institution);
    - a construction contractor as defined under the Income Tax (Construction Contracts) Regulations 2007;
    - a property development as defined under the Income Tax (Property Developer) Regulations 2007; and
    - a person who has been granted an exemption under Sections 127(3)(b) and 127(3A) of the Income Tax Act 1967 ["the Act"] in respect of the adjusted income of the person.
- iii. Maximum Amount of Interest Allowable for Deduction
  - The maximum amount of interest referred to in Section 140C of the Act shall be an amount equal to 20% of the amount of "tax-EBITDA" of that person from each of his sources consisting of a business for the basis period for a year of assessment.
- iv. Ascertainment of Tax-EBITDA
  - The amount of "tax-EBITDA" is ascertained in accordance with the following formula:-

$$A + B + C$$

where,

A is the amount of the adjusted income of that person from his sources consisting of a business for the basis period for a year of assessment before any restriction on deductibility of interest under Section 140C of the Act is made;

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

## Hyperlinks

- C is the total amount of interest expense incurred in relation to the gross income of the person for any financial assistance in a controlled transaction from his sources consisting of a business for the basis period for a year of assessment.
- “Qualifying deduction” (in “B” above) is defined as:-
    - an amount equal to the amount of expenditure incurred by the person computed in any deduction falling to be made under the Act where the amount of deduction is twice the amount of the expenditure incurred by a person; and
    - any claim for deduction under any rules made under Section 154(1)(b) of the Act where the deduction is allowed for purposes of ascertaining the adjusted income of the person.
- v. Carry Forward of Excess Interest Expense
- The amount in excess of the maximum amount of interest is allowed to be carried forward and deducted against the adjusted income of the company for the subsequent years of assessment (subject to the maximum amount of interest for the relevant year), until the whole amount of that excess has been fully utilised.
  - The excess of the maximum amount of interest expenses allowable for deduction in a basis period for a year of assessment and the unutilised interest expenses brought from the preceding year is eligible to be carried forward provided that the shareholders of the company on the first day and the last day of the basis period for the following year of assessment are substantially the same.

The above Rules comes into operation on 1<sup>st</sup> July 2019 and is applicable in respect of the basis period beginning on or after 1<sup>st</sup> July 2019 and subsequent basis period.

### **Guidelines for Application of Social Enterprises for Approval under Section 44(11C) of the Act**

Following the Budget 2019 announcement, the IRB has recently issued the Guidelines for Application of Social Enterprises for Approval under Section 44(11C) of the Act. The said Guidelines provide guidance on the application procedure, criteria for application of approval and conditions to be complied with after obtaining the approval under the Section 44(11C) of the Act and deduction for donors in respect of cash contribution to an approved social enterprise.

- [Guidelines for Application of Social Enterprises for Approval under Section 44\(11C\) of the Act \(in Bahasa Malaysia\)](#)

## Hyperlinks

A person (donor) is eligible to claim deductions in respect of cash contribution to approved social enterprise under Section 44(11C) of the Act, subject to restrictions of the person's aggregate income (i.e. 7% for a person other than a company and 10% for companies, as the case may be). The deduction under Section 44(11C) of the Act is given after the deductions under Sections 44(6) and 44(11B) of the Act.

The Guidelines stipulate that the application for approval under Section 44(11C) of the Act must be submitted during the period from 1<sup>st</sup> January 2019 to 31<sup>st</sup> December 2020. The approval period for an approved social enterprise under Section 44(11C) of the Act is 3 consecutive years of assessment.

### Allowance for Increase in Exports

Presently, a qualifying company which achieves increase in export sales of agricultural produce or product from manufacturing in the basis period for a year of assessment is eligible for allowance for increased exports ["AIE"].

The Income Tax (Exemption) (No. 5) Order 2019 and Income Tax (Exemption) (No. 6) Order 2019 have been gazetted to revise the eligibility and requirements in respect of the claim for AIE incentives.

The AIE incentives available to a qualifying company remain unchanged as shown below:-

#### a. Income Tax (Exemption) (No. 5) Order 2019

	<b>Achievements</b>	<b>AIE</b>
•	The value of increased exports is at least 50%	30% of value of increased exports
•	Penetrated a new market for export as determined by the Malaysia External Trade Development Corporation	50% of value of increased exports
•	Awarded an Export Excellence Award by the Minister of International Trade and Industry for achieving the highest increase in export sales	100% of value of increased exports

- [Income Tax \(Exemption\) \(No. 5\) Order 2019](#)
- [Income Tax \(Exemption\) \(No. 6\) Order 2019](#)

## Hyperlinks

## b. Income Tax (Exemption) (No. 6) Order 2019

	<b>Achievements</b>	<b>AIE</b>
•	The manufacturing product exported attained at least 30% of value added	10% of value of increased exports
•	The manufacturing product exported attained at least 50% of value added	15% of value of increased exports
•	Increased exports of agricultural produce	10% of value of increased exports

The AIE claimable for a year of assessment is deducted against a maximum of 70% of the statutory income for a year of assessment. Any unabsorbed AIE shall be carried forward to be set-off against statutory income for the subsequent years.

The important updates in respect of the above Orders are as follows:-

- i. Definitions and Conditions in Relation to “Agricultural Produce” and “Manufacturing”
  - The AIE is available to a qualifying company which achieves increase in export sales of agricultural produce or product from manufacturing. The terms “agricultural produce” and “manufacturing” are defined as:-
    - **“agricultural produce”** means fresh and dried fruits, fresh and dried flowers, ornamental plant, and includes ornamental fish, frozen raw prawn, frozen cooked and peeled prawn, frozen raw cuttlefish and frozen raw squid
    - **“manufacturing”** has the meaning assigned to it in paragraph 9 of Schedule 7A to the Act (for the purposes of reinvestment allowance)
  - The agricultural produce must be planted, reared or caught by the qualifying company
  - The product from manufacturing must be manufactured by the qualifying company
- ii. Ownership of the Qualifying Company
  - At least 60% of the issued share capital of the qualifying company must be owned directly by Malaysian citizen
- iii. Determination of Value of Increased Exports
  - In the event that the basis period for the current year of assessment and the basis period for the immediate preceding year of assessment are not made out of 12 months period ending on the same date, the average free-on-board [“FOB”] value of export sales shall be used to determine the value of increased exports for the current year of assessment
  - The value of FOB export sales used in any case shall not be equal to zero

## Hyperlinks

#### iv. Revised Non-Application Clauses

- AIE shall not be allowed for a company in respect of the same export of agricultural produce or product from manufacturing if in the basis period of a year of assessment, the company:-
  - has been granted reinvestment allowance under Schedule 7A of the Act
  - has been granted investment allowance for service sector under Schedule 7B of the Act
  - has been granted any incentive under the Promotion of Investments Act 1986 including deductions for promotion of exports
  - has been granted any exemption under Section 127(3)(b) or Section 127(3A) of the Act
  - has made a claim for deduction under any Rules made under Section 154 of the Act except:-
    - Rules in relation to allowance under Schedule 3 of the Act
    - the Income Tax (Deduction for Audit Expenditure) Rules 2006
    - the Income Tax (Deduction for Expenses in Relation to Secretarial Fee and Tax Filing Fee) Rules 2014

The abovementioned Orders are deemed to have come into operation from the year of assessment ["YA"] 2016.

In addition to the above, following the 2016 Budget announcement, the Income Tax (Exemption) (No. 7) Order 2019 has been gazetted to provide AIE with relaxed conditions to companies with paid-up capital not exceeding RM2.5 million. The types of AIE covered under this Order are as shown below:-

	<b>Achievements</b>	<b>AIE</b>
•	The manufacturing product exported attained at least 20% of value added	10% of value of increased exports
•	The manufacturing product exported attained at least 40% of value added	15% of value of increased exports

The conditions for the claim of AIE under this Order are similar to those contained in the Income Tax (Exemption) (No. 6) Order 2019 except that there is no specific requirement in respect of the ownership of the qualifying company as per item (ii) above.

This Order is deemed to have operation from the YA 2016 until the YA 2020.

- [Income Tax \(Exemption\) \(No. 7\) Order 2019](#)

### Further Deduction for Employment of Senior Citizen, Ex-Convict, Parolee, Supervised Person and Ex-Drug Dependant

Following the 2019 Budget announcement, the Income Tax (Deduction for Employment of Senior Citizen, Ex-Convict, Parolee, Supervised Person and Ex-Drug Dependant) Rules 2019 has been gazetted to allow a further deduction of remuneration incurred by an employer in the basis period for a year of assessment for employment of senior citizen ( $\geq 60$  years of age), ex-convict, parolee, supervised person and ex-drug dependant, who is a citizen and resident in Malaysia. The Rules apply to an employer who has a business source of income only.

To qualify for further deduction of remunerations payable to the above individuals, the following conditions must be complied with:-

- the employee is employed on a full-time basis;
- the remuneration paid to each employee does not exceed RM4,000;
- the employer and the employee must not be the same person;
- the employer is not a relative of the employee.

The employer claiming for the further deduction is required to obtain a written confirmation from:-

- the Malaysia Prison Department, confirming that the employee is an ex-convict, a parolee, or a supervised person; or
- the National Anti-Drug Agency, confirming that the employee is an ex-drug dependant.

The above Rules shall have effect for the YA 2019 and YA 2020.

### Extension of Stamp Duty Exemption for the Purchase of Residential Property Valued Between RM300,001 and RM2,500,000 under the National Home Ownership Campaign 2019

The Stamp Duty (Exemption) (No. 2) Order 2019 and Stamp Duty (Exemption) (No. 3) Order 2019 were gazetted previously to provide exemption from stamp duty in respect of any loan agreement and all instrument of transfer for the purchase of residential property under the National Home Ownership Campaign 2019, valued between RM300,001 and RM2,500,000, to an individual (i.e. a purchaser or co-purchaser who is a Malaysian citizen).

The Stamp Duty (Exemption) (No.2) Order 2019 (Amendment) Order 2019 and Stamp Duty (Exemption) (No.3) Order 2019 (Amendment) Order 2019 have been gazetted to extend the stamp duty exemption for sale and purchase agreement executed during the period from 1<sup>st</sup> January 2019 to 31<sup>st</sup> December 2019 (previously up to 30<sup>th</sup> June 2019).

**Note:** For further information on the previous Orders, kindly refer to our Tax Flash – April 2019 issue.

## Hyperlinks

➤ [Income Tax \(Deduction for Employment of Senior Citizen, Ex-Convict, Parolee, Supervised Person and Ex-Drug Dependant\) Rules 2019](#)

➤ [Stamp Duty \(Exemption\) \(No. 2\) Order 2019 \(Amendment\) Order 2019](#)

➤ [Stamp Duty \(Exemption\) \(No. 3\) Order 2019 \(Amendment\) Order 2019](#)

➤ [Tax Flash – April 2019](#)

## Sales Tax

- i. The Guide on Drawback of Sales Tax as at 12<sup>th</sup> June 2019 was published by Royal Malaysian Customs Department ["RMCD"] on 14<sup>th</sup> June 2019 (currently only made available in our National language).
- ii. The Guide on Sales Tax Exemption under Items 33A, 33B, 55, 63, 64 and 65 of Schedule A of the Sales Tax (Persons Exempted From Payment of Tax) Order 2018 as at 25<sup>th</sup> June 2019 was published by RMCD on the even date.

## Service Tax

The Guide on Information Technology Services as at 13<sup>th</sup> December 2018 is withdrawn and replaced with the same publication as at 25<sup>th</sup> June 2019.

The pertinent amendments to the Guide are summarised below:-

- a. Exemption from payment of service tax [business to business (B2B) exemption]; and
- b. Service tax treatment on imported taxable services.

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.

## Hyperlinks

- [Guide on Drawback of Sales Tax \(in Bahasa Malaysia\)](#)
- [Guide on Sales Tax Exemption under Items 33A, 33B, 55, 63, 64 and 65 of Schedule A of the Sales Tax \(Persons Exempted from Payment of Tax\) Order 2018](#)
- [Guide on Information Technology Services](#)