

# TAX UPDATE

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# TAX DEVELOPMENTS

## WITHHOLDING TAX ON INCOME UNDER SECTION 4(f)

The Inland Revenue Board has issued the PR No. 1/2010 [Withholding tax on income under paragraph 4(f)] on 19 April 2010 in respect of the tax provision which was effective from 1 January 2009.

The salient points of the Ruling are as follows:-

### 1. *Income falling under Section 4(f) of the Income Tax Act, 1967 (the Act)*

Income under Section 4(f) of the Act is gains or profits which are not income from a business, employment, dividends, interest, discount, rental, royalty, premium, pensions, annuities or other periodical payment. Special classes of income under Section 4A are also excluded. Examples of Section 4(f) income include commission and guarantee fees.

The determination of whether a payment made to a non-resident falls under Section 4(f) would depend on the facts and circumstances of each case. As a guidance, the following criteria may be considered:-

- the payment is revenue in nature;
- the payment received by a non-resident person is in the nature of a miscellaneous/ casual income, which is received outside the ordinary course of business;
- the payment is for an isolated transaction; and
- there is an absence of repetition of transactions to indicate the commercial nature of the transaction.

The income received is chargeable to tax regardless of whether the payment is in the form of cash or in-kind and shall be deemed to be derived from Malaysia irrespective of whether the transactions are carried on in Malaysia or not.

### 2. *Deduction of withholding tax*

Gains or profits under Section 4(f) paid to a non-resident are subject to a withholding tax of 10% under Section 109F of the Act. The payer has to pay the withholding tax so deducted to the Inland Revenue Board within one month after paying or crediting the recipient together with the Form CP37F. The withholding tax is a final tax for the non-resident.

Failure to remit the tax deduction within the stipulated period will result in a 10% penalty on that tax. In addition, such payment to the non-resident will be disallowed as a deduction in computing the adjusted income of the payer.

### 3. *Documentation*

The payer is required to keep documents to substantiate the determination of the nature of the payment to the non-resident. The documents required include the following:-

- copy of the business contract or agreement;
- copy of an auditor's confirmation that verifies the income derived by the non-resident is in the ordinary course of business or profession of that person;
- copy of the non-resident's audited accounts;
- copy of a notice of assessment of the non-resident; and
- copy of a business registration or license of the non-resident.

### 4. *Comments*

It is important to ascertain whether the income in question is a Section 4(f) income. There may be instances where certain income constitutes business income to the non-resident. In such instances, there is no need to deduct tax from that payment to the non-resident. As such, the wrong characterization will result in the non-resident suffering unnecessary withholding tax.

Another important point to consider is the determination of the effective date for the derivation of the income before making a deduction of the withholding tax. As the tax provision is effective from 1 January 2009, withholding tax is only applicable if the liability to make payment is on or after 1 January 2009. If the liability to pay arose prior to 1 January 2009 and actual payment is made after that date, no withholding tax is applicable.

## BENEFITS-IN-KIND

The Inland Revenue Board has issued the Fourth Addendum to the PR No. 2/2004 (Benefits-in-kind) on 19 April 2010. The Addendum serves to provide clarification in relation to the tax exemption on the benefit of free petrol received by an employee pursuant to his employment.

Effective from the Year of Assessment (YA) 2008, an employee is given the option to determine value of the free petrol provided by his employer on the following basis:-

- (a) Using the annual prescribed value for petrol provided in the PR No. 2/2004 as follows (without any exemption given); or

Cost of motorcar (New) (RM)	Annual prescribed benefit of petrol (RM)
Up to 50,000	600
50,001-75,000	900
75,001-100,000	1,200
100,001-150,000	1,500
150,001-200,000	1,800
200,001-250,000	2,100
250,001-350,000	2,400
350,001-500,000	2,700
500,001 and above	3,000

- (b) If the actual value of petrol provided can be identified, then the amount exempted is as follows:-

- RM2,400 per year for travelling between home and place of work (**from YA 2008 to YA 2010 only**); and
- RM6,000 per year for travelling in exercising his official duties.

Where the employer is unable to identify the amount of value of petrol provided for the above purposes, then the exemption will be limited to a maximum of RM6,000 per year instead of RM8,400 per year.

The employee can claim the actual amount expended for official duties exceeding RM6,000 as a deduction against his employment income if proper records pertaining to the claim are kept.

**If you need any assistance in formulating a tax efficient employee's remuneration package, please contact Ms Mayadevi at [mayadevi@rsmi.com.my](mailto:mayadevi@rsmi.com.my)**

## TAX CASES

The following is a summary of the tax cases decided by the Special Commissioners of Income Tax and the High Court which were reported recently.

### CH SDN BHD v. KETUA PENGARAH HASIL DALAM NEGERI

#### *Subject*

Whether the interest income derived by a Malaysian company from advances to a non-resident is a tax-exempt foreign source income by virtue of Paragraph 28 of Schedule 6 of the Income Tax Act, 1967.

#### *Facts*

CH Sdn Bhd (CH) is a locally incorporated company and carried on the business of manufacturing and exporting latex and synthetic gloves. AHBV, a related company of CH, is an investment holding company in the Netherlands with a central treasury role within the group. In addition, it is a financing entity for the group, monitoring the funding requirements and channeling any surplus funds within the group thus reducing the need for external debt.

During the Years of Assessment 1999 to 2005, CH and AHBV entered into a Cross-Revolving Credit Agreement and agreed to make advances to each other from time to time. Interest is payable on any unpaid principal amount on an arm's length basis. CH treated the interest received from AHBV as tax-exempt foreign source income on the basis that it arose in the Netherlands and was therefore, sourced and derived in the Netherlands and received in Malaysia. However, the Director General of the Inland Revenue Board (IRB) contended that the interest income is a Malaysian source income as the originating cause of the interest income is the loans given by CH in Malaysia and accordingly, raised additional assessments to tax the interest income together with penalties being imposed.

#### *Decision*

The case was held in favour of CH where the Special Commissioners decided that the location of the source of the interest income is in the Netherlands and accordingly, the receipt of the interest income from AHBV by CH in Malaysia is not chargeable to tax. In citing the Hang Seng Bank case, the Special Commissioners held that the source of income is where the interest arose. The originating cause is not the origin of funds but the origin of the acts from which those funds generated income.

(Note: The IRB is appealing against the decision in the High Court)

## SYARIKAT KION HOONG COOKING OIL MILLS SDN BHD v. KETUA PENGARAH HASIL DALAM NEGERI

### *Subject*

Whether a company which was granted a pioneer certificate in respect of promoted products is precluded from claiming reinvestment allowance for its non-promoted products.

### *Facts*

Syarikat Kion Hoong Cooking Oil Mills Sdn Bhd (SKH) was granted a pioneer certificate under the Promotion of Investment Act, 1986 for a period of 5 years on the manufacturing of shortening and margarine (the promoted products). SKH also manufactures non-promoted products and incurred substantial capital expenditure on the plant and machinery used in the manufacture of the non-promoted products for a qualifying project. It made a claim of Reinvestment Allowance (RA) under Schedule 7A of the Income Tax Act, 1967 on the non-promoted products during the pioneer income tax relief period.

The IRB disallowed the claim of RA on the basis that a company that has already been granted a pioneer certificate is excluded from claiming RA under Paragraph 7(a)(ii) of Schedule 7A of the Income Tax Act, 1967. The case was brought to the Special Commissioners of Income Tax which ruled in favour of the IRB. SKH then appealed against the decision of the Special Commissioners to the High Court.

### *Decision*

The High Court overturned the Special Commissioners' decision and ruled that a pioneer company, during its tax relief period in respect of promoted products, is not excluded from claiming RA on the capital expenditure incurred in respect of its non-promoted products. The words "a company" or "the company" does not appear in isolation in Paragraph 7(a)(ii). It should be read as a whole together with the words "which has been granted pioneer certificate in respect of a **promoted activity or promoted product**". Hence this paragraph seeks to exclude a company with a pioneer certificate from claiming both RA and tax relief in respect of the **same product or activity**. A company claiming tax relief for a promoted product should not be prejudiced from claiming RA on its non-promoted products since it has nothing to do with the tax relief granted for a promoted product.

## TAX ADMINISTRATION

### PAYMENT OF TAX THROUGH POS MALAYSIA BERHAD

Effective from 15 April 2010, payment of income tax and real property gains tax can be made at the post office counters throughout Malaysia as well as via Pos online. The services are free of charge.

For payment at the counter:-

- Cash payment only
- Payment slip will be proof of payment of tax

For online payment:-

- Taxpayer is required to have existing account with CIMB Bank, Hong Leong Bank, Bank Rakyat, Bank Islam, EON Bank, Al-Rajhi Bank and Affin Bank
- Register online with Pos Malaysia
- Confirmation of online payment will be proof of payment of tax

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