Crowe

Crowe Chat

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Tax

Audit / Tax / Advisory

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1. PR 2/2020 and PR 3/2020 – Tax Treatment of Stock in Trade Part I – Valuation of Stock and Part II – Withdrawal of Stock

Introduction

Stock in trade is anything a business acquires, produces or manufactures, for the purpose of manufacturing, selling at a profit or exchanging. It is important for stock in trade of a business to be valued correctly at the end of a financial period to enable the profits and income tax payable of the business to be ascertained accurately.

Previous PR

PR4/2006 - Valuation of Stock In Trade and Work In Progress Part I was issued on 31 May 2006.

New PR

The Inland Revenue Board of Malaysia (IRBM) issued the following PRs on 3 June 2020 to provide guidance on the valuation and withdrawal of stock in trade:

- PR2/2020 - Tax Treatment of Stock in Trade Part I - Valuation of Stock
- PR3/2020 - Tax Treatment of Stock in Trade Part II - Withdrawal of Stock

1. PR 2/2020 and PR 3/2020 – Tax Treatment of Stock in Trade Part I – Valuation of Stock and Part II – Withdrawal of Stock

Details of new PR

<u>PR2/2020 - Tax Treatment of Stock in Trade Part I - Valuation of Stock</u>

Subsection 35(3) of the Income Tax Act 1967 (ITA) addresses the basis of valuation of stock in trade which is acceptable for income tax purposes as follows:

- stock is valued either by using the market value or the cost of acquiring the stock; and
- stock consisting of immovable properties, stocks, shares or marketable securities is valued at the lower of its cost price or market value.

1. PR 2/2020 and PR 3/2020 – Tax Treatment of Stock in Trade Part I – Valuation of Stock and Part II – Withdrawal of Stock

PR2/2020 - Tax Treatment of Stock in Trade Part I - Valuation of Stock

The new PR clarifies the acceptable valuation of stock in trade at market value as follows:

Acceptable	Not acceptable
Fair value	Replacement cost method (Note 1)
Estimated selling price	Conservative method (Note 2)
	Net realisable value

Note 1: The replacement cost method is not acceptable for tax purposes as it involves determining a price from a market in which traders transact.

Note 2: The conservative method is also not acceptable for tax purposes as the value taken would be the anticipated price that could be obtained if the business has no choice but to sell the goods at a lower price or when the business is about to cease.

1. PR 2/2020 and PR 3/2020 – Tax Treatment of Stock in Trade Part I – Valuation of Stock and Part II – Withdrawal of Stock

PR2/2020 - Tax Treatment of Stock in Trade Part I - Valuation of Stock (cont'd)

The new PR also clarifies the acceptable cost methods of valuing stock in trade as follows:

Acceptable	Not acceptable
First-in-first-out (FIFO) Weighted average cost formula	Last-in-last-out (LIFO)

In practice, a business may comply with the generally accepted accounting principles which are *MFRS 102 Inventories* and *Section 13 of MPERS* where inventories are recognised and measured at the lower of cost and net realisable value.

Where the net realisable value of the stock is lower than the cost, a tax adjustment has to be made as follows:

- The value of the inventory from net realisable value has to be reinstated to its market value; and
- The estimated cost to sell or estimated selling cost which has been deducted from the estimated selling price has to be added back in the tax computation.

1. PR 2/2020 and PR 3/2020 – Tax Treatment of Stock in Trade Part I – Valuation of Stock and Part II – Withdrawal of Stock

PR3/2020 - Tax Treatment of Stock in Trade Part II - Withdrawal of Stock

Subsections 24(2) and 24(3) of the ITA address that when an item of stock in trade of a business is withdrawn whether for own use or for other reasons by a person carrying on the business, the market value of the item at the time of withdrawal will be treated as gross income from the business.

The new PR also explains the tax treatment of withdrawal of stock in the following scenarios:

- **Withdrawal of stock in trade for use in a different business activity**
  - treated as if a transaction of sale or purchase at market value has taken place.
- **Reclassification from trading to capital or vice versa due to a change of intention of the business**
  - the trading stock / capital asset is valued at the market value.
- **Withdrawal of stock in trade without any consideration received**
  - the market value at the time of withdrawal is treated as gross income from the business.

1. PR 2/2020 and PR 3/2020 – Tax Treatment of Stock in Trade Part I – Valuation of Stock and Part II – Withdrawal of Stock

PR3/2020 - Tax Treatment of Stock in Trade Part II - Withdrawal of Stock (cont'd)

- **Withdrawal of stock in trade for a consideration consisting of any property that is not a debt to the taxpayer and is not cash or its equivalent ("a sum")**
  - the market value at the time of withdrawal is treated as gross income from the business.

- **Withdrawal of stock in trade for a consideration consisting of any property together with a debt to the taxpayer and / or a sum**
  - the market value of stock is reduced by the debt and the sum received.

- **Stock in trade parted with by way of compulsion including requisition or compulsory acquisition**
  - the amount receivable will be treated as gross income of the business in the year the stock in trade is parted with by way of compulsion.

2. PR4/2020 - Tax Treatment of Any Sum Received and a Debt Owing that Arises in Respect of Services to be Rendered

Introduction

Prior to the year of assessment (YA) 2016, paragraph 24(1)(b) of the ITA only dealt with debts arising in respect of any services rendered which were brought to tax in the YA the debt arises. With effect from YA 2016, an amendment was made to paragraph 24(1)(b) of the ITA to also bring to tax debts arising in respect of any services to be rendered in the YA the debt arises. In YA 2016, a new subsection 24(1A) of the ITA was introduced to tax any advance payments for services in the year of receipt, notwithstanding that the services have yet to be rendered and there is no debt owing.

New PR

The IRBM issued the following PR4/2020 - Tax Treatment of Any Sum Received and a Debt Owing that Arises in Respect of Services to be Rendered on 16 June 2020 to explain the application of paragraph 24(1)(b) of the ITA and subsection 24(1A) of the ITA.

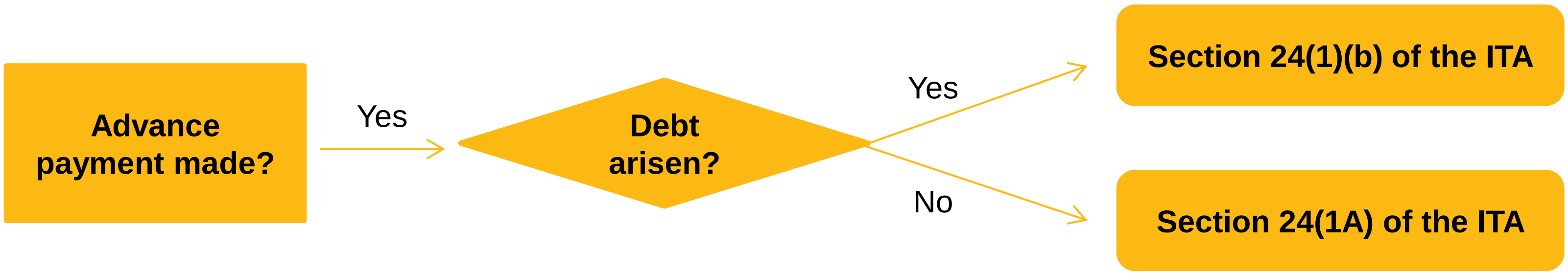
2. PR4/2020 - Tax Treatment of Any Sum Received and a Debt Owing that Arises in Respect of Services to be Rendered

Details of new PR

The new PR highlights the following points in respect of the new provisions:

Tax treatment effective from YA 2016

- By virtue of paragraph 24(1)(b) of the ITA, a debt owing would arise when there is a contractual obligation to pay or a liability to pay exists.
- The application of paragraph 24(1)(b) of the ITA would have to be considered first before applying subsection 24(1A) of the ITA.



2. PR4/2020 - Tax Treatment of Any Sum Received and a Debt Owing that Arises in Respect of Services to be Rendered

Details of new PR (cont'd)

Transitional tax treatment for advance payments received prior to YA 2016

- The advance payments were received in respect of services that will be rendered subsequent to YA 2016.
- The advance payments received will continue to be taxed when the services are rendered.

Tax treatment in respect of a refund of an advanced payment

If a person refunds any sum of money received in respect of services that have yet to be rendered, a tax deduction can be claimed in the YA when the refund is made.

Services that are Not Subject to Paragraph 24(1)(b) and Subsection 24(1A) of the ITA

- Services that are governed by separate Income Tax Rules – i.e. construction contract or property development.
- Pursuant to Subsection 24(8) of the ITA, Section 24 of the ITA shall not apply to income under Section 4A of the ITA.
- Refundable deposits – i.e. security deposit and refundable deposit, but does not include deposits that are forfeited.

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3. Guidelines - Stamp Duty on the Instruments of Transfer for Unlisted Shares

Introduction

Stamp duty is chargeable on instruments of transfer and not on transactions. The sale of shares in a Malaysian incorporated company will be subject to stamp duty at the rate of RM3 for every RM1,000 i.e. 0.3%.

Previous Guidelines

Guidelines On the Stamping Of Share Transfer Instruments For Shares That Are Not Quoted On The Kuala Lumpur Stock Exchange (Guidelines 2001) was issued in the year 2001.

New Guidelines

The IRBM released the Guidelines On the Stamping Of Share Transfer Instruments For Shares That Are Not Quoted On The Kuala Lumpur Stock Exchange (Guidelines 2020) on 23 June 2020. Guidelines 2019 dated 6 November 2019 was also released on the same day but it was superseded by Guidelines 2020.

3. Guidelines - Stamp Duty on the Instruments of Transfer for Unlisted Shares

Details of the new Guidelines

The IRBM published these technical guidelines which are available in the Bahasa Malaysia language only, to provide guidance on the calculation of stamp duty on instruments of transfer for unlisted shares and to replace the previous guidelines which were issued in the year 2001. A comparison of the guidelines is as follows:

Category	Basis of valuation	
	Guidelines 2001	**New Guidelines 2020** (effective from 1 March 2020)
Sale of shares which requires Securities Commission's approval	Price or value per share as approved by the Securities Commission	
Sale of shares in loss-making companies	The higher of: • Par or nominal value; or • Net tangible asset; or • Sale consideration	The higher of: • Net tangible asset • Sale consideration
Sale of shares in profit making companies	The higher of: • Par or nominal value; or • Price Earning Ratio; or • Sale consideration	The higher of: • Net tangible asset; or • Sale consideration

3. Guidelines - Stamp Duty on the Instruments of Transfer for Unlisted Shares

Details of the new Guidelines (cont'd)

Category	Basis of valuation	
	Guidelines 2001	**New Guidelines 2020** (effective from 1 March 2020)
Newly incorporated companies	Par value	Sale consideration
Inactive companies: • dormant companies • zero-revenue companies • Threshold-qualified companies	Par value	Sale consideration

4. An article on Tax Implications on Digital Services

Tax Implications on Digital Services

By Foo Meng Huei and Liza Ooi,
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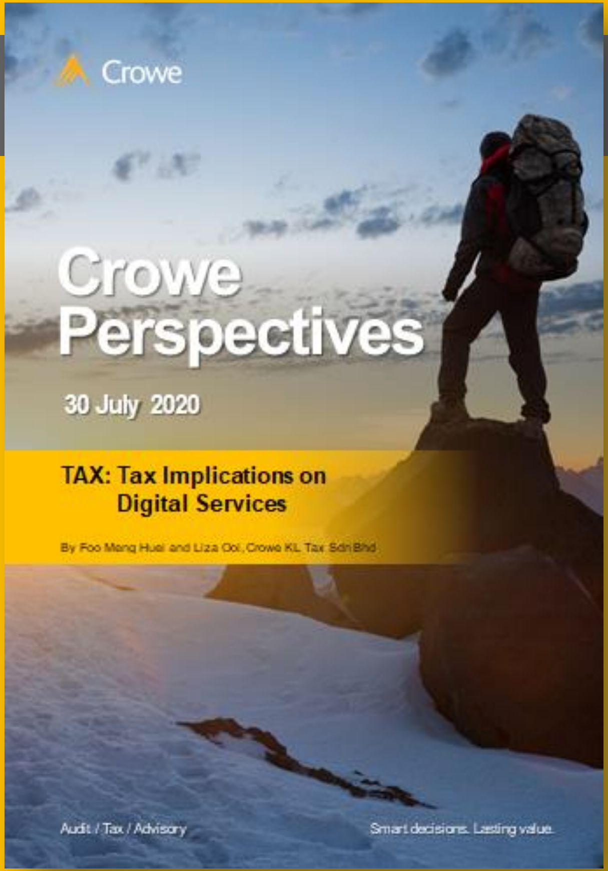
Read more



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