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Crowe Chat

Vol.2/2022 (Tax)

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1. Practice Note 1/2022: Explanation in Relation to the Definition of Factory for Reinvestment Allowance Claims

The Inland Revenue Board of Malaysia (IRBM) had previously issued Public Ruling (PR) 10/2020 – Reinvestment Allowance (Part I – Manufacturing Activity) on 6 November 2020 to assist a company resident in Malaysia and which is engaged in manufacturing activities in ascertaining its eligibility to claim reinvestment allowance incentive.

In paragraph 8.2 of the above PR, it was illustrated that the extension of a building would not qualify as a "factory" under Paragraph 9 of Schedule 7A of the MITA because the storage space exceeds 10% of the total floor area of the extension.

Practice Note

The IRBM has issued Practice Note 1/2022: Explanation in Relation to the Definition of Factory for Reinvestment Allowance Claims on 17 January 2022.

1. Practice Note 1/2022: Explanation in Relation to the Definition of Factory for Reinvestment Allowance Claims (cont.)

Details of the Practice Note

Practice Note 1/2022 was issued to clarify that storage space exceeding 10% of the total floor areas of the factory shall not be taken into account in the calculation of reinvestment allowance claims under Schedule 7A of the MITA. Nevertheless, reinvestment allowance claims would still be allowed for the portion of the extension used for the purpose of a qualifying project (excluding the storage space).

Examples of the calculation on the 10% storage space area and the relevant tax treatments were also provided in the Practice Note 1/2022.

Crowe's view: The IRBM has adopted a stricter interpretation of the law in determining the 10% threshold for the area of the building used for storage of raw materials, or goods or materials, or both. We are of the opinion that such interpretation by the IRBM under the Practice Note could lead to future disputes between taxpayers and the IRBM. Hence, taxpayers are advised to seek professional advice prior to claiming the Reinvestment Allowance incentive.

2. Amendments to the Earning Stripping Rules (ESR)

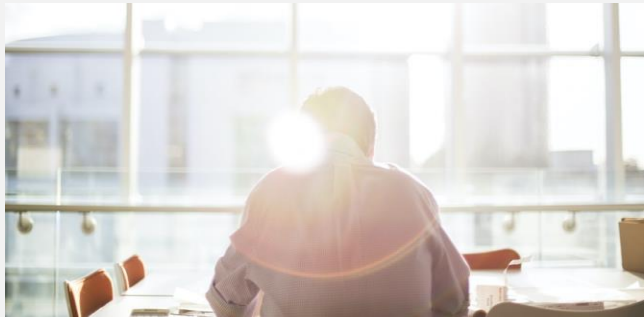
Section 140C of the MITA was legislated in the Finance Act 2018 to implement the ESR. The details of the implementation of Section 140C of the MITA were laid out in the Income Tax (Restriction on Deductibility of Interest) Rules 2019 which was gazetted on 28 June 2019. Subsequently, the IRBM issued the Restriction on Deductibility of Interest Guidelines on 5 July 2019 to provide clarification on the Rules.

In a nutshell, ESR affect the deductibility of interest expenses on financial assistance from outside Malaysia in controlled transactions – where deduction is allowed only up to a maximum of 20% of Tax-EBITDA.

Tax-EBITDA = *Adjusted income from business + Qualifying deductions + Interest expenses incurred on any financial assistance in a controlled transaction from sources consisting of business*

Amended Income Tax Rules

The Income Tax (Restriction on Deductibility of Interest) (Amendment) Rules 2022 was gazetted on 31 January 2022 and came into operation on 1 February 2022.



2. Amendments to the Earnings Stripping Rules (ESR) (cont.)

Details of the Amended Income Tax Rules

Principal Rules	Amended Rules
Qualifying deduction means *(extracted verbatim from the relevant Rules)* – *(a) an amount equal to the expenditure incurred by the person which qualifies for double deductions,* *(b) any claim for deduction under any rules made under Paragraph 154(1)(b) of the MITA where the deduction is allowed for purposes of ascertaining the adjusted income of the person.*	Qualifying deduction means *(extracted verbatim from the relevant Rules)* – *(a) where there is business expenditure incurred in the profit and loss account is allowed as deduction under the Act 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 profit and loss account; or* *(b) where there is no business expenditure incurred in the profit and loss account, the amount of deduction allowable under the Act.*
Qualifying deduction = expenditure allowed for double deductions, further deductions and specific deductions allowed by the Minister.	**Qualifying deduction <u>EXCLUDES</u> expenditure allowed for double deductions, further deductions and specific deductions allowed by the Minister.**
The carry forward of unabsorbed interest expenses is applicable only to companies.	The carry forward of unabsorbed interest expenses is now **applicable to any person, and is not restricted to a company**. For companies, the carry forward of unabsorbed interest expenses is **subject to the existing shareholders' continuity test.**

3. Frequently Asked Questions (FAQs) on the Implementation of 2% Withholding Tax on Payments Made to An Agent, Dealer or Distributor

As previously outlined in Crowe Chat Vol.1/2022, the IRBM has recently issued its FAQs (available in Bahasa Malaysia only) to provide further clarification on the application of Section 107D of the MITA.

Details of the FAQs

Major points highlighted in the FAQs are:

- Credit notes and discounts given as well as contra transactions with agents, dealers or distributors are not subject to withholding tax under Section 107D of the MITA.
- Agents, dealers or distributors include resident individuals who are sole proprietors and partners in a partnership.
- The RM100,000 threshold value refers to the payment received from each payer company.
- The RM100,000 threshold is determined by the payer company annually.
- The tax residency status of the agent, dealer or distributor in the immediately preceding year is not relevant in determining the applicability of withholding tax under Section 107D of the MITA.

3. Frequently Asked Questions (FAQs) on the Implementation of 2% Withholding Tax on Payments Made to An Agent, Dealer or Distributor (cont.)

Details of the FAQs (cont.)

Payments and Reporting by Payer Companies

- Payer companies must use the withholding tax remittance form (CP107D) when making the 2% withholding tax payment via post or at the IRBM service counters.
- If payment is made to several agents, dealers or distributors, the complete details of payment for each agent, dealer or distributor can be completed in the appendix [Lampiran CP107D(1)]. Each appendix can cater up to 20 agents, dealers or distributors.
- The 2% withholding tax payment is still applicable to the payments made to the agents, dealers and distributors even though the agents, dealers and distributors are subject to tax instalment payments under CP500.
- Upon submission of the income tax return forms by the relevant agents, dealers or distributors, the 2% withholding tax paid will be offset in arriving at the “balance of tax to be paid”.

3. Frequently Asked Questions (FAQs) on the Implementation of 2% Withholding Tax on Payments Made to An Agent, Dealer or Distributor (cont.)

Details of the FAQs (cont.)

Deferment of the 2% Withholding Tax Payment

- The deferment is given automatically to all payer companies.
- The IRBM has provided further clarification on the application of the deferment as follows:-

Payment made to the agents, dealers or distributors	Due date to remit the 2% withholding tax payment to the IRBM
1 January 2022 – 2 March 2022	On 1 April 2022
3 March 2022 onwards	Within thirty (30) days after paying or crediting the agent, dealer or distributor.

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Automation Capital Allowance Incentive

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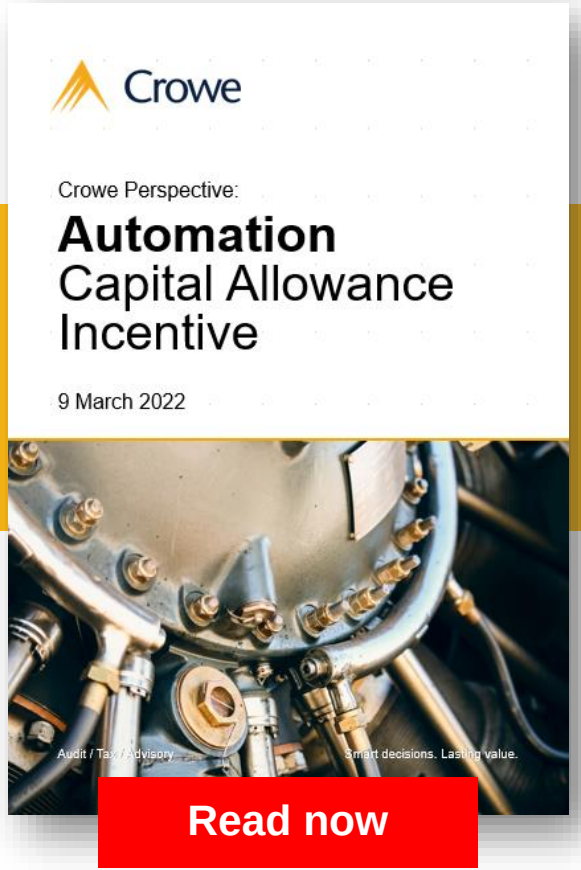

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Crowe Malaysia PLT is the 5th largest accounting firm in Malaysia and an independent member of Crowe Global. The firm in Malaysia has 15 offices, employs over 1,200 staff, serves mid-to-large companies that are privately-owned, publicly-listed and multinational entities, and is registered with the Audit Oversight Board in Malaysia and the Public Company Accounting Oversight Board in the US.

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