

MALAYSIAN INCOME TAX

(ABRIDGED)

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by

**SOHAN LAL DHAWN, A.T.I.I. (London),
A.A.I.A. (London)**

Lecturer in Taxation, School of Accountancy
and Business Administration,
University of Singapore

**AWTHER SINGH, B.A. (Hons.), B.Sc.
(Econs.) Hons. (Lon.), A.A.S.A. Cert. Edu.**

Associate of the Taxation Institute of Australia
Lecturer in School of Accountancy,
University of Singapore

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PREFACE

"MALAYSIAN INCOME TAX" AND THIS BOOK

This book is specially published for the benefit of the average taxpayer who has no interest in specialized topics like Double Taxation, Investment Incentives, Timber Profits Tax and so on. Leaving out these and related topics and putting in additional illustrations has produced a concise work on Malaysian Income Tax which can enable even the average layman reader to arrange his tax affairs to his own advantage without exposing himself to the severe penalties of the law.

OUTLINE OF THIS BOOK

At this stage it may be useful if we briefly outline to the reader the plan of this book.

In Chapters I to V we begin by asking how the Director General(D.G.) obtains the information he needs to collect income tax and the duties of the taxpayer in supplying such information. We go on to consider what the D.G. does with the information and the procedures for the taxpayer to appeal if he does not agree with the assessment of the D.G. We end this part by considering the various penalties which are laid down for the offences of not giving sufficient information or giving the wrong information.

We go on in Chapter VI—INCOME AND RESIDENCE,—to discuss which items are chargeable to income tax for this depends on whether the items are capital or income and on the residence status of the person.

In Chapters VII to IX we discuss in considerable detail the deductions which are allowed or not allowed from the income as set out in Chapter VI above in order to arrive at the chargeable income.

The discussion up to this part is in relation to the Income Tax Act (Act 53 as amended by Acts A98 and A108) and relevant case-law in order to lay a solid foundation for what follows in Chapter X.

Chapter X is the key chapter of this book for in this chapter (which can actually be read by itself) we summarize in simple language the entire subject of MALAYSIAN INCOME TAX in so far as it applies to any taxpayer, to enable him to make a maximum tax saving by arranging his tax-

affairs so that he fills his Form B to get the maximum legal benefits he is entitled to under the law.

We have an additional feature for readers who are businessmen for in the last two chapters—XI and XII we have explained in considerable detail how to prepare the tax computations of sole-traders, partners and limited companies.

There are a large number of illustrations following each of chapters X, XI and XII because we believe that this is the best way that a reader can understand that applications of the Income Tax Act to his particular problem.

The really serious reader is catered for at the end of the book in Appendix I where we give two question papers of the University of Malaya followed by worked solutions. The fact that a few of these questions are on the specialist topics we have excluded from the comprehensive "MALAYSIAN INCOME TAX" to produce this concise volume should be kept in mind. It is our hope that at least some readers of this book will be encouraged to pursue their interest further by reading the bigger book.

January 1973

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MALAYSIA, KUALA LUMPUR

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THE MACHINERY OF INCOME TAX

1. SOURCE OF INFORMATION

(i) Previous Records

We could begin by asking how the D.G. knows who should be taxed. Operationally the primary sources of information are the files maintained in the previous years on taxpayers but these are continuously up-dated by the information gathered by the following means.

(ii) Return Required

The D.G. can require a return from any person regarding his income but he has to give such person at least 30 days to submit the return. Where the person, though chargeable to tax under the Income Tax Act, by 31st March has not received any request from the D.G. as above, he must notify the D.G. on his own initiative by 14th April that he is chargeable to tax.

In the case of an individual who arrives in Malaysia during a year of assessment, *but is not chargeable in the year of his arrival* such individual is required to inform the D.G. within two months, but he only has to do this if under the existent Act he will be chargeable in the next year of assessment. [Section 77 (3).]

Illustration

Mr. X arrives in Malaysia on 2nd June 1979, and he is not chargeable to tax for the year of assessment 1979. However where the provisions of the Act in force in the year of assessment 1979 if applied to the year of assessment 1980 make him chargeable to tax in year of assessment 1980, Mr. X must inform the D.G. within two months i.e. before 2nd August 1979 ["month" means "a month reckoned according to the Gregorian Calendar." according to the Interpretation Act (Act 23 of 1967)].

(The logical possibility of a new arrival being chargeable to tax in the year of his arrival is not very real since the repeal of commencement provisions and we do not consider it here).

Onus and Burden of Proof on Taxpayer and Penalty

Thus even where no form has been sent to a person he is required to give notice to the D.G. that he is or will be chargeable to tax. The common feeling among many persons that they do not have to do anything if they do not receive a form from the D.G. is wrong. Indeed default without reasonable excuse in furnishing a return or in giving notice of chargeability makes a person guilty of an offence, which on conviction can attract a fine not exceeding one thousand dollars or to imprisonment not exceeding six months or both. Furthermore in such a case the burden of proving that a return has been made or notice given is upon the accused person. If no prosecution has been instituted as above "the D.G. may require that person to pay a penalty equal to treble the amount of the tax which, before any set-off, repayment or relief under the Act is payable for that year . . .". [Section 112 (3) (a).]

(iii) Specific Returns and Production of Books

Besides the above the D.G. can give a notice of not less than 30 days, to the person or any other person, requiring the furnishing of any specified return. Alternatively he can ask any person to attend personally before the D.G. producing all books, documents, returns etc. deemed necessary by the D.G. for the purpose of obtaining full information for ascertaining a person's chargeability to tax. In addition the D.G. can ask for both the specified return and the personal attendance with the books etc. Section 78 (a) (b) (c). It would appear that the D.G. can require any accountant to appear before him with books etc., and he cannot refuse to so appear.

(iv) Disclosure of Assets

The D.G. can also obtain information about a person's assets by requiring the person to furnish a detailed statement of bank accounts etc. which are in his own name or in the name of a wife or dependant child, as well as all other assets and sources and other facts bearing on past and present chargeability to tax. (Section 79.) Readers familiar with accounting will recall that one way to calculate profit or earnings in the absence of proper accounts is to compare net assets at different time periods. These provisions enable the D.G. to apply a similar test where normal sources of information do not appear to suffice, e.g. ostentatious living and consumption accompanied by income tax returns which show losses or little profit.

(v) Access to Buildings, Places and Books

For the purpose of this Act, the D.G. has full and free access to all buildings, lands, other places, books and documents. He can enter these places and search them at any time without a search warrant, and he can copy or make extracts from any document etc. without any charge.

(vi) Take Possession of Documents

In addition where in the D.G.'s opinion an examination of the books or documents cannot be conveniently done at the place, or where there is a risk of interference or destruction of the records—or where they are needed as evidence in proceedings under this act, he may take possession of the books and document. Section 80 (1) & (2).

(vii) Ask for a Translation

Where the books are not in the National Language in West Malaysia or in the National Language or English in East Malaysia the D.G. can give a notice requiring these books etc. to be translated into the National Language. Section 80 (3).

(viii) Oral and Written Disclosure Required except from Public Officers under Statutory Obligation to Secrecy

The D.G. can require any person except persons under a statutory obligation to secrecy who are also public officers or officers of local or statutory authority to give instantly oral information about his own or any other person's income, assets, or liabilities. He can also ask any person for this information in writing in similar circumstances except that the D.G. then has to give a notice under his hand. In the latter case the person so required to give such information must give it within the time specified in the D.G.'s notice. Section 81. Since "public officer" means "a person lawfully holding, acting in or exercising the functions of a public officer" (Interpretation Act) it seems clear that an accountant not being a "public officer" must answer oral and written queries on his clients' affairs.

(ix) Returns by Employer

The most common source of income, is income from employment and the Act contains provisions for collecting information about this income in the following ways:—

- (a) Every employer is required to furnish the D.G. on Form E the names, addresses and details of income in cash or kind and he must furnish his employees or pensioners with C.P. 8A or 8C. Section 83 (1).
- (b) With regard to new employees chargeable or liable to be chargeable a notice on the prescribed form within one month giving name, address and terms and date of the commencement of his employment must be submitted to the D.G. To be chargeable to tax an individual must earn a certain minimum sum, such minimum varying with his personal circumstances, hence in the case of employees earning a low income no return is needed under this subsection. Section 83 (2).
- (c) Where an employer is about to cease to employ an employee who is chargeable or is likely to be chargeable on the income from the employment, a notice on the prescribed form must be given to the D.G. at least one month before the date of such cessation giving the name, address and expected date of such cessation. However to provide for sudden cessation, e.g. by 24 hours'

notice, the Act provides that a shorter notice or even a notice on or after cessation may be accepted by the D.G. if he is satisfied that such notice is reasonable in the circumstances. Section 83 (3). Here again if the employee is earning an income too low to make him chargeable to tax no notice needs to be given.

- (d) Where an employer has knowledge that one of his employees who is chargeable to tax on his employment income is about to leave or is intending to leave Malaysia for a period exceeding three months, he must, not less than one month before the expected date of departure give written notice of his departure to the D.G. However shorter notice or notice given on or after departure may be accepted by the D.G. if he feels it is reasonable in the circumstances.

Where the D.G. is satisfied that an individual has to frequently leave Malaysia in the course of his employment he can exclude such individual from the application of this provision. [Section 83 (4).]

(x) Retention of Employee's Money on Cessation

An employer who possesses any money belonging to an employee who has ceased or is about to cease employment must not release this money until 30 days after the D.G. has received the notice mentioned above in (c). Similarly money belonging to an employee leaving Malaysia for a period exceeding three months and not intending to return must not be released by an employer until 30 days after the D.G. has received the notice mentioned in (d) above. The Act provides that this prohibition on the release of money shall prevail "notwithstanding the provisions of any written law to the contrary." [Section 83 (5).]

(xi) Returns Concerning Other Persons

Any person receiving or controlling money or property which is income under section 4, of a person who is chargeable to tax, can be required by the D.G. to supply a return giving particulars of income and the name and address of the owner. Agents and representatives could be required to give such information by notice of not less than 30 days given under the D.G.'s hand. [Section 84 (1).]

(xii) Selling Agents

Persons selling goods in Malaysia on behalf of a person who is not resident for the basis year for a year of assessment must deliver a quarterly return of gross proceeds to the D.G. within 30 days of the end of the quarters in March, June, September or December, but this has only got to be done if the sale of these goods is in the course of carrying on a business of such non-resident person. Thus where goods received on consignment from outside Malaysia are sold in Malaysia on behalf of a person not resident in the basis year, this return is only required if such non-resident owns the business

of the seller, e.g. independent local booksellers who sell books bought on consignment from publishers outside Malaysia need not submit such returns, but a retail outlet owned by such a publisher would need to supply such a return. [Section 84 (2) & (3).]

(xiii) Rent Payers

Occupants of land and furnished or unfurnished premises can be required to submit a return giving details of the rental and the person owning the land or collecting the rent. [Section 85.]

(xiv) Returns by Precedent Partner for Partnership

In the case of a partnership, the precedent acting partner present in Malaysia (the first named in partnership agreement or in the usual name of firm where no agreement exists); or where no acting partner is present in Malaysia, any attorney, agent, manager or factor of the firm in Malaysia, shall when required by the D.G. make the prescribed return or returns within a time (not less than thirty days) specified in the notice from the D.G. in any year of assessment. And where no such return has been required by 31st March in any year of assessment, the person must make the return on his own initiative by the 14th of April.

The Act prescribes that these returns must be made on the prescribed forms in each of the following circumstances:

- (a) Where all the partners are ordinarily resident for the basis year of a year of assessment.
- (b) Where for the basis year of a year of assessment at least one partner is either not resident or is resident but not ordinarily resident (see Chapter VII) but the other partners are ordinarily resident.
- (c) Where for the basis year of a year of assessment all the partners are not ordinarily resident or some of the partners are resident but not ordinarily resident and the others are not resident.

Even if a partnership has been dissolved with respect to every one of its partners the requirements for the submission of the returns shall continue to apply. The persons in the partnership immediately before such dissolution are required to make the returns as above as if they were still the partners. [Section 86.]

(xv) Further Returns

Whenever he thinks fit the D.G. can give a notice to any person requiring further and fuller returns regarding any matter under the Act for which a return is required. This enables the D.G. to ask for additional returns where there is a lack of clarity and such returns must be made within a reasonable time as specified in the notice. [Section 87.]

(xvi) Return Presumed Act of Person Signing

Any return furnished under the Act is legally presumed to be the act of the person whose affairs it concerns unless it is proved otherwise. Thus where an illiterate businessman has his returns prepared by some other person but has put his thumbprint on it, it is assumed that these returns are his, unless he can prove otherwise. Thus before the businessman above can disavow any return he must rebut the above presumption. The Act also specifically provides that any person signing such return shall be presumed to have knowledge of all the matters therein. This provision prevents the person charged in any proceedings relating to these returns from easily claiming that he did not know what was in it as it was prepared say by a firm of accountants. For the onus of proving that this is so, is on such a person. Besides, the standard practice, even where professionals and others prepare returns, is to always ask the client to sign or make his mark as the case may be. Yet where a client can prove that he had no knowledge of the contents representing perhaps a systematic attempt to evade tax, the person who prepares the return could be liable to the severe penalties provided by the Act. [Section 88.]

(xvii) Change of Address

To try to ensure that the notices etc. above reach the persons chargeable to tax, so that the returns made as a result provide a continuous flow of information the Act specifically provides that a person chargeable to tax who has given one address in Malaysia to the D.G. and who has changed to another address in Malaysia shall within three months inform the D.G. of the change, in writing. [Section 89.]

2. ORIGINAL SOURCE—BOOKS AND RECORDS

In the section above we have enumerated the sources from which the D.G. receives information in the form of returns. However for businesses the primary sources are the books and records kept by the persons who furnish the returns. The Act provides for such books and records to be kept and for receipts to be given as follows.

Every person carrying on a business is required to keep sufficient records to enable the income for each year of assessment or the adjusted business loss for the basis period for any year of assessment to be readily ascertained and he must keep such records in safe custody. In addition where the gross takings in the basis year from the sale of goods has exceeded eighteen thousand dollars, or from the performance of services twelve thousand dollars, he is specifically required to issue a printed receipt serially numbered, and to retain a duplicate for every receipt so issued. It should be noted that at first sight, if in the calendar year 1971, gross takings exceed the amounts stated above, the printed receipts serially numbered are required to be used in the calendar year 1972. However in the case of businesses the basis year may not be the calendar year by virtue of the fact that the D.G. may accept accounts prepared for a period ending on a date other

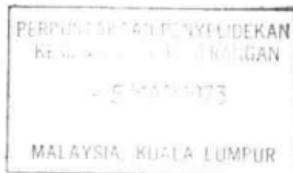
than 31st December as a basis for a year of assessment. The important thing to remember is that the Act takes account of the natural order of things where first the gross takings must exceed the above amount before action can be taken to issue receipts as required.

In cases where cash registers or other machines are used to record sales and where such machines, to the satisfaction of the D.G., automatically record all sales, and he is also satisfied that such totals are daily transferred to a sales record the printed receipt serially numbered with duplicate may be dispensed with.

The D.G. by statutory order can specify for any business the form of records to be kept, and receipts to be issued, and the manner in which this shall be done. He can also waive the keeping of records and the issue of receipts for any class of business.

Where the D.G. is of the opinion that the accounts etc. produced by a person do not sufficiently help to ascertain his income he may give such person a notice requiring him to submit a set of accounts audited by a professional accountant (as defined in paragraph 15 in schedule 5) together with a report by the Accountant containing the matters set out in section 174 (1) and (2) of the Companies Act, 1965, in so far as relevant to the case in hand.

Entries in the books and records required to be kept under the Act must be made within 60 days of each transaction. It is submitted that the keeping of temporary records on slips of paper etc. does not meet the requirement. [Section 82.]



CHAPTER II
ASSESSMENT

1. ACCEPT OR REFUSE

On the basis of the return submitted to the D.G. he can either "accept the return and make an assessment accordingly" or he can refuse to accept the return and make an assessment based on other information he has. Thus where a person does not declare his full income and the D.G. is aware of it, the D.G. can assess a person on his full income. Section 90 (1).

2. ESTIMATED ASSESSMENT

Where a person has not delivered a return as required under section 77 the D.G. may make his own estimate of the chargeable income of such person and assess him accordingly, but this does not affect that person's liability for failure to deliver the return. [Section 90 (2).]

3. ADVANCE ASSESSMENT

(i) Normal Course of Events

In the normal course of events a person submits his return for a year of assessment based on his income for the basis period of that year of assessment. The basis period is usually the calendar year immediately preceding the year of assessment except where a business makes up its accounts for a period not ending on 31st December. Where the accounts are not so made up to 31st December the basis period is usually the period for which accounts are made up in the preceding year. Thus *X* a person ordinarily resident in Malaysia will submit his return of income from the year of assessment 1973 based on:—

- (a) His salary in cash and in kind for the period 1.1.1972 to 31.12.1972 (if any).
- (b) His profit from a business for the accounting period ended in 1972 (say 1.4.1971 to 31.3.1972).
- (c) His income from Dividends, Interests, Rents, etc. for the period 1.1.1972 to 31.12.1972.

However in the following cases for reasons which are generally connected with the prompt recovery of tax, and a desire to prevent persons from defaulting on paying the tax which will become due the D.G. is empowered to alter the normal course of events and make an advance assessment.

(ii) Cessation of Business Source

Assume that Adam in the above example ceases to possess the business source w.e.f. 30.4.1973. Normally by this time Adam would have been assessed on his business income up to 31.3.1972 in the year of assessment 1973, and the income from the business up to 31.3.1973, would be brought to assessment only in the year of assessment 1974 and the income for April 1973 would be assessed in the year of assessment 1975. However since the business has ceased on 30.4.1973 the D.G. may make in 1973 itself the assessment for year of assessment 1974, or 1974 and 1975, or 1975. Alternatively the D.G. in the year of assessment 1974 may make an assessment for 1975 if not already done. Such provisions now also apply to a person who "not being resident for the basis year for that year of assessment, ceases in that year of assessment to carry on business in Malaysia in relation to a source consisting of a business," e.g. persons not resident say in 1972 who cease to possess a source of business in the year of assessment 1973 may be assessed in advance by the D.G. [Section 92 (1) (a).]

(iii) Person Leaving Malaysia

Where the D.G. is satisfied that a person about to leave Malaysia is likely to cease to possess a source in the year of departure, or in one of the two following years of assessment he may make an advance assessment in respect of that source.

Illustration

X is a partner of XY & Co., a firm of advocates and solicitors. This partnership makes up its accounts to 31st March every year. X intends to leave Malaysia on 30th April, 1972 and to retire from the partnership on that date. He may be assessed for the years of assessment 1973 and 1974 in 1972. His income for year of assessment 1973 will be based on the accounts up to 31.3.1972 and his income for the year of assessment 1974 will be based on the accounts for one month up to 30th April 1972 the date when he retires.

Even where there is no likelihood of the cessation of the source as above, the D.G. may still make an advance assessment if he is satisfied that the person is about to leave Malaysia and "it is desirable for other reasons that an assessment should be made". [Section 92 (1) (c)].

(iv) Cessation of Employment Source

Where a person has ceased to possess a source of income but still receives in a year of assessment some income from that source, such income not having been included in the gross income of this person before, an assessment in the year of such receipt and for the following year may be made by the D.G. Such a situation can arise for example where an expatriate person intends to leave Malaysia on 30th September 1970 on retirement and gets in advance his 6 months leave pay up to 31.3.1971. The money he receives for 3 months to 31.3.1971 may be assessed in 1970 for the year of assessment 1972.

We have mentioned above that the reasons for advance assessment are self-evident but it is worth mentioning here that when an income from a business source ceases say on 30.6.1972, the person's ability to pay the tax in the normal way for the year of assessment 1973 may well be in doubt and depending on the circumstances an advanced assessment may or may not be made. In other cases where a person is leaving the country it may well be that he might not return and these statutory provisions act to minimize loss of taxes due. [Section 92 (1) (d).]

(v) Persons Not Ordinarily Resident Carrying on Sea or Air Transport Business

Where a person not ordinarily resident in Malaysia in the basis year or basis period, carries on a business solely consisting of transporting passengers or cargo by air or sea he is under section 54 charged to tax at the relevant rate¹ on 5% of his gross receipts, or on such proportion of his adjusted world income attributable to Malaysia. In the case of such a person the D.G. may make an advance assessment for that year at any time in the basis year or basis period. [Section 92 (1) (e)].

E.G. Eastern Shipping Line is a company in U.S.A. operating ships between Burma and U.S.A. It ships collected freight of \$1,000,000 from Malaysia in 1972. Under section 54 the company being a non-resident shipping company is chargeable to tax on 5% of its gross receipts at a rate of 40%; or on the proportion of its adjusted profits attributable to gross receipts in Malaysia. Assuming the former the company will be assessed \$20,000 in advance in 1972 for the year of assessment 1973.

(vi) Accounts not ending on 31st December

Where a person's adjusted income is based on the accounts ended at any date other than 31st December in any basis year the D.G. may make an advance assessment in that basis year. [Section 92 (1) (f)].

E.G. X Co. makes up its accounts to 30.6.1972 and the adjusted profit is \$30,000. Normally this would be assessable in the year of assessment 1973 but the D.G. may make an advance assessment in say November 1972 for year of assessment 1973 and the tax so assessed must be paid within 30 days.

(vii) Commencement year Income from Employment or Pension etc.

From the y/a 1972, where a person begins in a certain year to receive such income the D.G. may assess him in that year itself for the next and subsequent years of assessment. [Section 92 (1) (b)]. This applies even to persons who continue in employment after receipt of their West Malaysian credit [Section 92 (1) (g)].

(viii) Assumptions for Advance Assessment

When an advance assessment is made in any of the cases above on any person it is made on the following assumptions:

- (a) There is no change in the law as between the year in which the assessment is made and the year *for* which the assessment is made.

¹ Non resident individuals and companies at 40% and resident but not ordinarily resident individuals at scale rate.

Example

If an advance assessment is made *in 1971 for* year of assessment 1972 it is assumed that the law applicable to year of assessment 1971 is also applicable to year of assessment 1972.

- (b) In the case of individuals the personal circumstances in the basis year for the year of assessment *in* which the advance assessment is made are assumed to be the same for the basis year *for* which the advanced assessment is made.

Example

If the advance assessment for 1972 is made in 1971 the personal circumstances of the individual in this year (1971) shall be assumed to be the same as for the basis year for year of assessment 1971 i.e. 1970. Thus where an individual is married and is maintaining his wife in the basis year 1970 then for the purposes of the advance assessment made in 1971 for year of assessment 1972 he shall be assumed to be married in 1971 also.

Where such advance assessments have been made under these assumptions, and subsequently when the year of assessment comes around it appears to the D.G. that these assumptions lead to less or more favourable results for the person, as compared to the normal method of assessment laid down in section 90, the D.G. may either, make an additional assessment, or repay tax as appropriate. [Section 92 (2).]

(ix) Advance Assessment does not preclude Additional Assessment

Where in one of the above cases, the D.G. has made an advance assessment in 1971 say for the year of assessment 1972, and he thinks that an additional assessment (see below) is necessary he may still make this additional assessment, and "section 91 (1) shall apply as if the year of assessment referred to therein were that particular year." [Section 92 (3).]

(x) Advance Assessment or its Absence not Bar to Ordinary Assessment

Where an advance assessment has been made in one of the above cases on a person in respect of a source of his, this shall not prevent the D.G. from making an assessment on that person in respect of any other source of his.

Also where an advance assessment in the cases mentioned may not in fact have been made because there was not enough total income to produce chargeable income i.e. the reliefs are more than the income, this shall not prevent the D.G. from making an assessment under the Act. [Section 92 (4).]

4. ADDITIONAL ASSESSMENT

The fact that an assessment or advance assessment has been made does not prevent the D.G. from making additional assessments. Thus where new information comes to his attention he may make additional assessments. Normally such additional assessments

have to be made within twelve years of the relevant year of assessment but where it appears to the D.G. that there has been fraud, wilful default, or negligence, either by the person or on his behalf, resulting in loss of tax, an additional assessment may be made at any time whatever.

Where tax has been repaid to a person by mistake of fact or law, an assessment may be made within twelve years of such repayment to recover such tax but this may not be done for the reason that the practice of the D.G. prevailing at the time of repayment has subsequently changed. Also where the repayment of the tax is because of an agreement between the person and the D.G. following a review of an assessment by the D.G. under section 101 (2), or where the repayment is a result of an appeal being determined, no additional assessment may be made, on the identical facts and circumstances comprised in such appeal or agreement.

5. TAX EVASION NOT STATUTE BARRED

The provision in section 91 (3) by which fraud, wilful default or negligence in tax matters renders the person liable to assessment at any time ensures that the tax offender can never rely on the effluxion of time to erase the possibility of being assessed or prosecuted for his fraud, default or negligence. During an appeal the onus of proving that the facts of the case are such that there was no fraud or wilful default bringing the case within section 91 (3) would be on the appellant (see *A.B.C. v. C.I.T. Singapore*, [1959] M.L.J. 162 on the comparable proviso to section 73 (1) of the Singapore Act).

6. WAIVER

Where tax chargeable is five dollars or less the D.G. may waive the assessment but this does not prevent him from including the chargeable income and the tax in another assessment.

Also where two assessments have been made on the same income for a year of assessment the D.G. may discharge one of them so that such income is charged to tax only once for that year. [Section 95.]

7. FORM OF ASSESSMENT AND RECORD OF ALL ASSESSMENTS

An assessment on a person must be made in the appropriate form and include particulars of: the year of assessment, chargeable income, and tax charged. Also it must specify the date on which it was completed. Where all the above appear to have been duly completed the assessment is presumed to have been made on the date shown. [Section 93.]

The D.G. is required by law to have maintained a record of all assessments made for each year of assessment, in such manner as he thinks fit. [Section 94.]

This provides an important source of information but it is only available to the D.G. and his staff for tax purposes and may not be disclosed to any unauthorized person on pain of severe penalties.

8. COMPOSITE ASSESSMENT

Where a person for any year of assessment has not made a return or not given notice of his chargeability, or has made an incorrect return by omitting or understating his own or his principal's income or has given incorrect information regarding his own or his principal's chargeability to tax, the D.G. and such person may come to an agreement in writing on an amount to be paid by such person in respect of this. Such an amount will consist of the amount of tax under-charged, as a result of any of the acts listed above and the amount of any penalties, or where such penalties have been reduced under section 124 (3), such reduced penalty, if any. [Section 96A (1).]

Note: Under section 112 (3) a person may be required to pay a penalty equal to treble the amount of tax payable for a year of assessment, if he has not filed his return or not given notice of his chargeability to tax and he has not already been fined under section 112 (1).

Under section 113 (2) a person may be required to pay a penalty equal to the amount of tax payable for a year of assessment if he makes an incorrect return or gives incorrect information in relation to any matter affecting his or any other person's chargeability to tax (even if made or given in good faith) and he has not already been fined under section 113 (1).

Section 124 (3) states that the D.G. may abate or remit any penalty compounded by him.

Illustration 1

X, for failing to file his return, agrees with the D.G. that tax payable by him for year of assessment 1972 is \$500. He has not been fined already under section 112 (1). The D.G. will issue a composite assessment as follows:

Year of Assessment 1972	
Tax under-charged for year of assessment 1972 (as agreed) ..	\$ 500
Penalty (three times)	1,500

Total tax payable	\$2,000

The D.G. will serve a notice of this on the person. Such notice must include: the years concerned, the tax under-charged, the penalty if any, and the place at which the total amount is to be paid. Such amount shall be collected as if it were tax payable by the person but only the provisions of section 103 to section 106 for expeditious recovery and collection of tax shall apply to this. Notwithstanding any other provisions of the Act such a composite assessment shall be final and conclusive under this Act and no appeal shall lie against it.

9. NOTICE OF ASSESSMENT

After the assessment has been made or where after an appeal the tax charged in an assessment has been increased, the D.G. is required to serve a notice on the person assessed, on the prescribed form which shall include: the year of assessment, the amount assessed and the tax charged. The place where the tax may be paid, the penalty for late payment under section 103 (4), and the right of appeal under the Act if any, must also be included in such notice. [Section 96 (1), (2) & (4).]

Such a notice of assessment must also be served on a person who has been appointed by the D.G. under section 68 (1) to be the agent of another person, as well as the other person, if such agent and the other person have a right to appeal the assessment under section 99 (2). [Section 96 (3).]

10. MISTAKES DO NOT NULLIFY NOTICES ETC.

Notices of assessment or other documents used for the purposes of the Act are not rendered ineffective by defects or omissions of form if the substance and effect are in accordance with the intent and meaning of the Act. Thus a person cannot rely on a wrong spelling of his name in a notice of assessment, to ignore the notice, if the wrongly spelt name has in reality the effect of designating him. E.g. if a notice to Ahmad Marizan is addressed "Ahmed bin Marizan" the person cannot ignore the notice on this ground.

The Act goes even further than this so that even where—

- (a) the name is wrong, or
- (b) the description of income is wrong, or
- (c) the amount of chargeable income or tax charged is wrong,

a notice of assessment having any of these mistakes is still of effect if it is in fact served on a person on whom the assessment is intended to be made or on a representative of a principal as per section 67 (5); and contains the substance of the assessment. To repeat, if you receive a notice or other document which is for you, do not ignore it by relying on some formal defect. Even further, if the amount of tax charged in a notice of amount has been incorrectly calculated, this amount "may if the D.G. so directs, be taken to be the amount of tax which ought to have been charged if it had been correctly calculated."

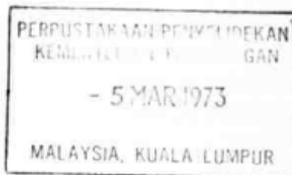
Lastly if a notice to pay tax has been served on the person who is in fact liable to pay that tax, a mistake on the notice as to the name of the person does not render this notice ineffective. [Section 143.]

11. ASSESSMENT FINAL AND CONCLUSIVE — SECTION 97

Where no valid notice of appeal against an assessment has been given, or where the person and the D.G. have come to an agreement after a review by the D.G. under section 101 or where after valid notice of appeal the appellant dies before or during the hearing, and the personal representative does not apply to the Special Commissioners,

within two years of death, or where the amount has been determined on appeal, leaving no right of further appeal, the assessment shall be final and conclusive, but the Act provides that the above shall not prejudice an exercise of the D.G.'s power to:

- (a) Make assessments and additional assessments under section 91.
- (b) Waive small assessments or give relief to double assessments on same income under section 95.
- (c) To take incorrectly calculated amounts of tax "to be the amount of tax which ought to have been charged if it had been correctly calculated," under section 143 (3).



APPEALS

1. SPECIAL COMMISSIONERS AND THE CLERK

(i) Appointment

The Act provides for the appointment by the Yang di-Pertuan Agong, of three or more Special Commissioners of Income Tax among whom there must be persons with judicial or other legal experience i.e. advocates, judges etc. and one of such experienced persons is to be appointed the Chairman of the Special Commissioner if the Yang di-Pertuan Agong considers it expedient. [Section 98 (3).] There is also a Clerk to the Special Commissioners. Each Special Commissioner holds office for a period and at a remuneration etc., specified by the Minister and is deemed to be a public servant. The office of the Clerk is a federal public office.

(ii) Powers of Special Commissioners

Paragraph 19 of Schedule 5 sets out these powers as follows:—

- (a) power to summon to attend at the hearing of an appeal any person who in their opinion is or might be able to give evidence respecting the appeal;
- (b) power, where a person is so summoned, to examine him as a witness on oath or otherwise;
- (c) power, where a person is so summoned, to require him to produce any books, papers or documents which are in his custody or under his control and which the Special Commissioners may consider necessary for the purposes of the appeal;
- (d) power where a person is so summoned, to allow him any reasonable expenses incurred by him in connection with his attendance;
- (e) all the powers of a subordinate court with regard to the enforcement of attendance of witnesses, hearing evidence on oath and punishment for contempt;
- (f) subject to section 142 (5), power to admit or reject any evidence adduced, whether oral or documentary and whether admissible or inadmissible under the provisions of any written law for the time being in force relating to the admissibility of evidence; and
- (g) power to postpone or adjourn the hearing of an appeal from time to time (including power to adjourn to consider their decision).

2. APPEAL WITHIN 30 DAYS OF SERVICE OF NOTICE OF ASSESSMENT

A person who does not agree with the notice of assessment, and who wishes to contest such an assessment has to appeal to the Special Commissioners by giving a notice on the prescribed form to the D.G. within thirty days of such notice being served on the person. In the case of an advance assessment an appeal must be made within the first three months of the year for which the advance assessment has been made. This right to appeal also extends to an agent appointed under section 68 as well as his principal, and for the purposes of appeals each of them is treated as the person in respect of whom the assessment was made. Even if both appeal, their appeals will if possible be dealt with together. However in the case of a receiver deemed appointed as agent of a court, the principal being the court, this provision (Section 99 (2)) does not apply.

3. EXTRA TIME FOR APPEAL

A person seeking to appeal may at any time apply to the D.G. on the prescribed form for an extension of the time within which the notice of appeal has to be given (30 days or 3 months as the case may be—see above). The D.G. if he is satisfied that a reasonable cause prevented the person from giving notice of appeal within the usual time, can grant additional time, and will notify the person in writing of any extension given. When the D.G. is not satisfied he will forward the application to the Clerk together with a statement of the reason for this dissatisfaction. Simultaneously, the person will be informed that the D.G. has done as above, and be given a copy of the D.G.'s statement giving the reason for his dissatisfaction. If he wishes, the person may, within 21 days, of the receipt of the above, forward to the Clerk, written representations regarding the matter. The D.G.'s statement and any representations made by the person are brought to the attention of one of the Special Commissioners by the Clerk and he shall decide whether or not to extend the period. Such decision shall be notified to the person and is final. To summarize—where you have not appealed within the given time you may apply to the D.G. for an extension of the time giving the reasons as to why you were prevented from giving the notice of appeal. If your reasons do not convince the D.G. in the first instance you will have a chance to make representations which are finally decided on by one Special Commissioner. If he does not give you an extension that is the end of the matter. (Section 100).

4. REVIEW BY D.G.—SECTION 101

(i) Procedure on Review

On receipt of an appeal under Section 99(1) the D.G. may review the assessment and for this purpose may:

- (a) Obtain additional details from the appellant,

- (b) require production of books and other documents by the appellant which are relevant to the matter,
- (c) summon any person who in the D.G.'s opinion has relevant evidence and examine him on oath or otherwise. [Section 101 (1).]

(ii) Written Agreement after Review

If as a result of this review the D.G. and the appellant come to a written agreement about the assessment appealed then the original assessment is held to be adjusted according to the written agreement. [Section 101 (2).]

(iii) Oral Agreement

Where there is only an oral agreement and the D.G. serves a written confirmation of the oral agreement on the appellant, and where within 21 days of such service the appellant does not repudiate the agreement, then such agreement becomes as binding as the written agreement above, with one difference—while the written agreement *is* final the above oral agreement confirmed in writing may still be set aside by a Special Commissioner given that:

- (a) the appellant has applied to the Special Commissioner within thirty days of such an agreement coming into being; and
- (b) after giving an opportunity to the D.G. to be heard the Special Commissioner has decided that it is just and reasonable to do so in the circumstances. [Section 101 (3) & (5).]

(iv) D.G.'s Proposal

After a review by the D.G. following an appeal, there may be neither a written nor an oral agreement so the D.G. may make a proposal to the appellant to alter the assessment. Within thirty days of being served with such a proposal the person should either accept or reject the proposal, (but if he needs further time he should apply to the D.G. who may give him additional time). If the person neither accepts nor rejects such a proposal within the time limit then the proposal is deemed to be a written agreement, with the following difference, that it can be set aside by a Special Commissioner as for (iii) above. [Section 101 (4) & (5).]

(v) Special Commissioner's Decision Final

Where the Special Commissioner sets aside an 'agreement' as in (iii) or (iv) above he is required to notify both the D.G. and the appellant through the Clerk and such decision is final. [Section 101 (6).]

(vi) Agent

The provisions of section 101, referring to review, agreements etc. where they refer to an appellant also include a person duly authorised by the appellant e.g. his accountant. [Section 101 (7).]

(vii) **Notice of Assessment after agreement**

Where the eventual effective agreement increases the tax chargeable the D.G. will serve a notice on the appellant on the prescribed form, and this shall include the increased tax charged. The tax in such a notice may be collected or recovered under Part VII of the Act, which provides for expeditious collection. The Act also provides that such notice should be served "as soon as may be" as soon as the agreement becomes effective. [Section 101 (8) & (9).]

(viii) **Summary of "Review by D.G."**

Where a person appeals against an assessment the Act provides a procedure by which the D.G. can review the assessment and the evidence and come to an agreement with the person. While a written agreement is final an oral agreement or the D.G.'s proposal can achieve the status of a written agreement but may be set aside by the Special Commissioners. Of course there may be no agreement at all. The next section of the text deals with this.

5. DISPOSAL OF APPEALS BY D.G.—SECTION 102

Where no agreement has been reached and there is no reasonable prospect of an agreement of any kind being reached the D.G. must forward the appeal to the Special Commissioners. [Section 102 (1).]

If the appellant has, when asked, done all he can reasonably do to facilitate the review by the D.G., he can six months after his notice of appeal request the D.G. to forward his appeal to the Special Commissioners and the D.G. must so forward the appeal within three months of receiving this request. This means that in Malaysia nine months is the maximum period that the appeal process can be delayed by the D.G. [Section 102 (2).] This contrasts with the situation where the tax authorities can indefinitely hold-up an appeal by refusing to give a notice of refusal to amend an assessment. Since in every case the tax has to be paid within 30 days of the service of the notice of any assessment, any delay in dealing with an appeal can work a considerable hardship on the taxpayer.

The appeal is heard and determined in accordance with Schedule 5 to the Act, the major provisions of which are briefly discussed below.

However at any time the D.G. and the appellant may come to an agreement and the D.G. sends a copy of this to the Special Commissioners, and when they are satisfied the proceedings abate and the agreement is effective. Alternatively the appellant may withdraw his appeal at any time, and on the Special Commissioners being satisfied that such withdrawal has taken place the proceedings abate and the assessment becomes final and conclusive. [Section 102 (5) (6) (7) (8) & (9).]

6. DISPOSAL OF APPEALS BY SPECIAL COMMISSIONERS — Schedule 5

(i) Hearing of Appeals

At least three Special Commissioners are required to hear every appeal and at least one of them must be a person with legal or judicial experience (advocate, judge etc.). If a Chairman has been appointed and is present he chairs the hearing but otherwise one of the three shall be chosen, but he must be a person with legal or judicial experience. In effect then, no hearing of an appeal can be held without a Special Commissioner with relevant experience presiding, and with two other Special Commissioners.

(ii) Place of Sitting

The Special Commissioners sit in all the major towns of Malaysia, as far as possible according to a programme drawn up half-yearly in advance.

(iii) Change in Address of Appellant

On the D.G. forwarding an appeal, this appeal is considered as a petition of appeal and the address given by the appellant there is used for service, but he can change the address by giving notice to the Clerk and the other party.

(iv) Place and Date of Hearing

The D.G. and the appellant can make an agreement in writing on this, in terms of the Special Commissioners' programme, or the Clerk will fix a place and date giving at least twenty-eight days notice to both parties. However on appeal to one of the Special Commissioners an appellant may be able to vary the above, even where the appeal has been partly heard.

(v) Appeals may be Heard Together

Where, the same person has made more than one appeal, or where different persons have made two or more appeals and they agree, one Special Commissioner may order the appeals to be heard together.

This order can be made either on the Special Commissioner's own motion or on the application of one party but the parties must be given an opportunity to be heard before such an order is made.

(vi) Onus of Proof and Additional Grounds

The onus of proving that an assessment is erroneous or excessive is on the appellant, but this only means that he has to make out a case beyond reasonable doubt, and the burden is no higher than a proof on a preponderance of probability. At this hearing the appellant may introduce new grounds or vary the grounds given in his petition, but where he does so without giving reasonable notice to the D.G., the Special Commissioners are required to adjourn the hearing for a reasonable period if requested to do so by the D.G.

(vii) Representation Attendance and Postponement

While the D.G. is represented by an authorised officer, a legal officer or an advocate the appellant may be represented by his advocate or his accountant or both. Such persons must be qualified persons under the law. Where a representative exists within the meaning of Section 67, such person can represent the principal at appeals.

With both parties to an appeal present the Special Commissioners may, on application of one or both parties, postpone the hearing making such order as to costs, against the party or parties asking for a postponement, as they consider reasonable (Schedule 5 para. 16A).

Where one party is absent, but satisfies the Special Commissioners then and there that it is for a reasonable cause, they shall postpone the hearing or at the request of the absent party decide it. Where the Special Commissioners are not so satisfied, they may either hear and decide the appeal in the absence of the defaulting party or postpone the hearing (para. 17(1)).

With both parties absent, and each failing to satisfy the Special Commissioners, the appeal may be decided or the hearing postponed with either or both parties being ordered to pay the reasonable costs to the Special Commissioners (para. 17(2) (a)).

With both parties absent, and only one party (say A) satisfying the Special Commissioners with a reasonable cause, the hearing may be postponed, or at the request of A decided by the Special Commissioners (para. 17(2) (b)).

With both parties absent, and both satisfying the Special Commissioners, the hearing shall be postponed or at the request of both parties decided by the Special Commissioners (para. 17(2) (c)).

However where in any of the above instances (under para. 17) a deciding order has been made as a result of a party's absence, but such party within thirty days satisfies the Special Commissioners with a reasonable cause, the order may be set aside and a time and place set for a fresh hearing (paragraph 18).

(viii) Witnesses

Where a witness is summoned to appear before the Special Commissioners he is legally bound to produce books etc. in his possession and to tell the truth whether under oath or not.

His reasonable expenses will be allowed and paid by the appellant or the D.G. as the Special Commissioners may direct. Where the representative is the appellant he may be directed to pay these expenses.

(ix) Decision of Special Commissioners

On completion of the hearing, the Special Commissioners give their decision in the form of an order (known as a deciding order) which must be signed and served on the parties. These orders fall into two basic categories—those which set out to the last

detail the tax effects of the order and those which still require partial or total negotiation discussion or review between the D.G. and the appellant. In the latter case the provisions of section 101 regarding review and agreement etc. apply and the case may well go through the whole cycle again if the parties cannot agree on the details. Yet there is an over-riding provision which can prevent the appeal from coming back, and that is where any one of the parties requires the Special Commissioners to state a case on any point of law, to the High Court.

(x) Vexatious and Frivolous Appeals

Any appellant who in the opinion of the Special Commissioners has made an appeal which is vexatious and frivolous will not of course have had his assessment discharged or amended, but, in addition he may be ordered to pay to the Special Commissioners a sum not exceeding \$5,000/- as costs. Such sum is payable within seven days of the order being served on the appellant, but the appellant may within twenty one days make oral or written representation to the Special Commissioners stating why, such order should not have been made, or the costs showed be reduced, and if the Special Commissioners are satisfied, they may remit the costs ordered wholly or partly. No costs and fees are payable in respect of an appeal to the Special Commissioners except as specifically provided in Schedule 5 of the Act.

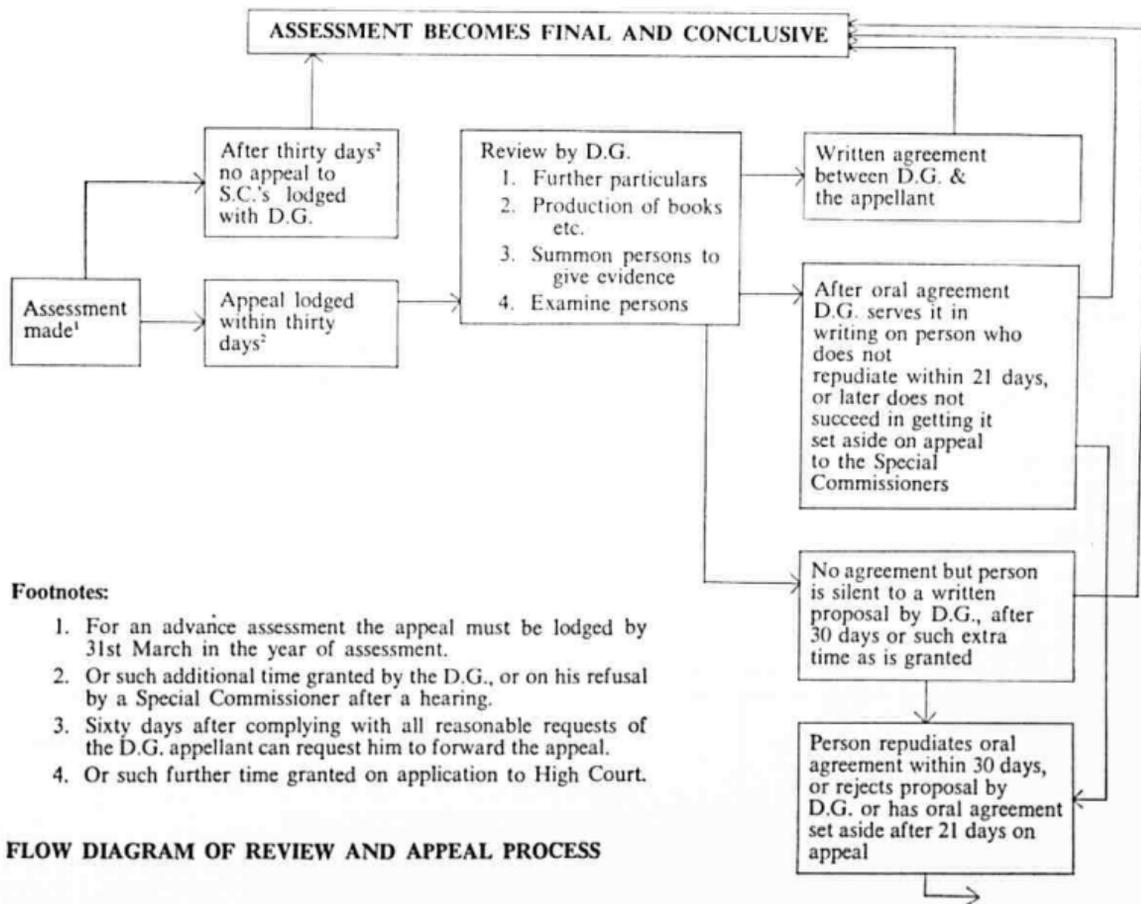
(xi) Case Stated

Either party can appeal against a deciding order on a question of law by, writing to the Special Commissioners within 21 days of the service of the order requiring the Special Commissioners to state a case to the High Court and paying the Clerk the fee prescribed by the Minister. The period of 21 days may be extended on application to the High Court by an intending applicant.

A case stated by the Special Commissioners must set forth the facts as found by them, and the deciding order, being signed by those Special Commissioners who heard the appeal (but where by reasons of death illness, absence or other cause, any of them cannot sign, the signature of those who can, will suffice), but the appellant is required to pay the prescribed cost of preparing the case and may in addition be required to deposit with the clerk the cost of preparing copies of the case stated, and on failure to make such deposit the Special Commissioners may refrain from transmitting the case stated to the High Court.

(xii) High Court

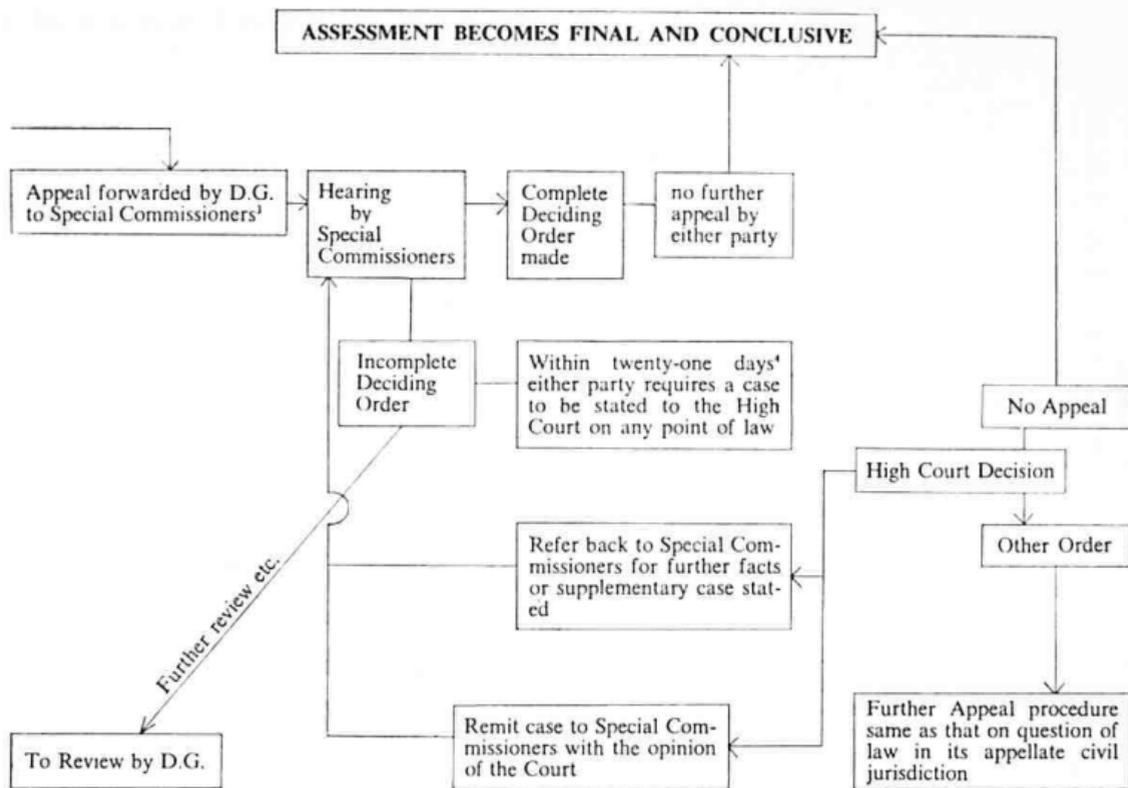
The High Court will hear and determine any question of law in a case stated as above but before such determination it can have the case sent back to the Special Commissioners for amendment or require them to find further facts and state a supplementary case. The right to further appeal from a decision of the High Court is the same as it is in respect of its decisions in questions of law in its appellate civil jurisdiction.



Footnotes:

1. For an advance assessment the appeal must be lodged by 31st March in the year of assessment.
2. Or such additional time granted by the D.G., or on his refusal by a Special Commissioner after a hearing.
3. Sixty days after complying with all reasonable requests of the D.G. appellant can request him to forward the appeal.
4. Or such further time granted on application to High Court.

FLOW DIAGRAM OF REVIEW AND APPEAL PROCESS



(xiii) **Hearings in Camera and Publication**

Proceedings of appeals are held in camera before the Special Commissioners, the High Court, or the Federal Court unless at the request of the appellant (but not the D.G.), the Special Commissioners or the court direct otherwise.

However, the facts of the case, the arguments and the decision may be published by or with the authority of the Special Commissioners or the Court where in their opinion these ought to be reported, without identifying the party other than the D.G. Such publications may be obtained from the Special Commissioners or the Court on payment of the prescribed fee. (para. 43).

7. SUMMARY

As the provisions for the appeal procedure are rather complex we summarize these in the form of a diagram on pages 23 and 24.

COLLECTION, RECOVERY AND PAYMENT OF TAX

1. COLLECTION

(i) Thirty Days to Pay or Penalty—Section 103

Regardless of the fact that an appeal has been made against an assessment, when a notice of assessment or composite assessment has been served, the tax payable must be paid, at the place specified in such notice within thirty days of such service, but the D.G. may give extra time for payment. The D.G. may also allow payment by instalments. However if at the end of the thirty days (or extra time) any amount is still unpaid, then a penalty of 10% automatically becomes payable in addition to the tax. Even where tax is allowed to be paid by instalments, default in the payment of any instalment on due date, makes the whole balance due and payable on that date, and automatically a penalty of 10% of the outstanding amount becomes payable in addition to it.

Illustration

Enche Adam is served with a notice of assessment on 31.3.1971 and the tax payable is \$270/-.

Suppose:

(a) By 30.4.71 he has not paid anything.

Tax due is now:	\$
Tax as assessed	270
+ 10% penalty	27
	<hr/>
Tax now due	297
	<hr/>

(b) He has asked for another 14 days extension and the D.G. has allowed this. By 14.5.71 he has not paid anything.

Tax with penalty as above	297
	<hr/>

- (c) He has asked to pay by instalments and the D.G. has agreed to receive the money through a banker's order at \$30 per month beginning 31.3.71. The money is paid for March, April, and May but due to insufficient funds the June 30th instalment is not paid. The Tax now due is as follows:

Tax as above	270
Less paid 3 × 30	90
	<hr/>
Balance	180
Penalty on 30.6.1971	18
	<hr/>
Due on 30.6.1971	198
	<hr/>

However when the overdue instalment is subsequently paid, the D.G. may treat it as paid on the due date, so that the penalty etc. do not attach. Similarly where the penalty has attached to tax payable, but good cause has been shown to the D.G. he may in his discretion remit the whole or part of it, or where it has been paid, repay the same. [Section 103 (5) & (6).]

The penalty also attaches to amounts which become due and payable from companies under section 108 (5) or (7) or from tax to be deducted from interest paid to non-residents under section 109 (2). [Section 103 (7).]

(ii) **Collection from Any Wife—Section 103 (8) & (9)**

Under section 45 (2) the income of a wife or wives is aggregated as the income of an individual. (That "wives" does not include the "secondary wives" of Chinese taxpayers had been decided in *Comptroller of Income Tax, States of Malaya v. H.K.V.*, [1968] 2M.L.J. 260 but the definition of "wife" in the Income Tax Act 1967 (Act 53) has included all Chinese secondary wives for purposes of income tax). In the normal course of events the individual is served with a notice of assessment, but the Act provides that the portion of tax attributable to the income of any wife may be collected directly from that wife, in spite of the fact that no assessment has been served on her. This has the effect of making such wife liable to pay tax within thirty days and also liable for penalty etc. as indicated in (i) above. However this does not confer the right of appeal on the wife. [Section 103 (8).]

The portion of tax attributable to the wife by section 103 (8) is calculated proportionately to her share of the aggregate total income of the husband. Eg. If her share of income is $\frac{1}{4}$ of such aggregate than the portion of tax attributable to her is also $\frac{1}{4}$ of the tax charged. This is so even where an individual's aggregate income is made up of the income of two or more wives. [Section 103 (9).]

(iii) **Deduction of Tax from Emoluments etc.—Section 107**

The D.G. can direct that from any employment income, pension, annuity or periodical payment under section 4 (e), to any individual who has to pay tax or may have to

pay tax, the person paying shall deduct tax. The amounts and time of deduction will be at the direction of the D.G. (subject to rules under section 154) and the deductions must be made whether the tax has been assessed or not. However this provision for deductions does not prevent the D.G. from serving an assessment on any person in the ordinary way, or prevent him from enforcing payment of any tax under section 106. [Section 107 (1) (2) & (3).]

An employer who does not comply with section 83 (5) by holding back money due to an employee leaving Malaysia, or who does not comply with a direction to deduct tax is himself liable—to the tax lost in the former case and the tax not deducted in the latter case. The D.G. is however required to apply such recovery to the tax due and the employer can reimburse himself from the employee. Similar provisions apply to a person paying pensions, annuity or other periodical payments, and where such person does not comply with a direction to deduct tax he is also liable as above for the tax not deducted. He also has the right to reimbursement. [Section 107 (4) & (5).]

2. RECOVERY

(i) Prevention of Taxpayer Leaving Malaysia—Section 104

Where the D.G. feels that a person is about to leave Malaysia without paying all the tax payable by him under the Act he may requisition the help of the police or immigration authority to prevent such person from leaving without paying the tax, or without giving satisfactory security for such tax. The D.G. does this by issuing a certificate containing particulars of the tax due, and directing that such person be prevented from leaving. Subject however to a banishment or ejection order made under any written law, the police and the immigration authority can do anything that is necessary to prevent such person leaving, including the use of reasonable force and the taking away of travel papers, and no official can be sued for lawfully doing anything as above. Simultaneously with the issue of the certificate the person will also be notified but non-receipt by him does not invalidate anything done as above.

(ii) Departure After Payment or Security

The person so prevented from leaving Malaysia can leave only if he either pays the tax to the D.G. or furnishes suitable security, obtaining a statement signed after the date of the certificate, by the D.G. or an authorized officer. Alternatively he can pay the tax to the officer in charge of a police station or to an immigration officer.

(iii) Refusal of Custom Clearance to Ship or Aircraft

The D.G. can issue a similar certificate to the custom authority to refuse clearance to a ship or aircraft owned, partly owned, or chartered by a person who being in the business of transporting cargo and passengers by sea or air has not paid the tax assessed on him, for a period of three months. However the permission of the Minister is required before the issue of such a certificate. The Act provides immunity from proceedings against any public officer for such an action, and lays down that harbour or other charges for the period of detention are still payable, during the period of detention.

Recovery by Suit

Tax due and payable can be recovered by the D.G. or any authorised officer, by civil proceedings, and the court is required not to entertain any plea that the tax is excessive, incorrectly assessed, under appeal, or that a penalty has been wrongly calculated. [Section 106.]

In such a suit, a certificate signed by the D.G. giving particulars of the defendant and the tax due, is sufficient evidence of the fact and sufficient authority for the court to give judgement for that amount. Even in criminal or civil proceedings, a statement purporting to be signed by the D.G. or an authorized officer, supporting the action, shall be evidence of the facts, until the contrary is proved. However, such a statement is not sufficient to prove the intent of the defendant and cannot be relied on in proceedings for an offence punishable by imprisonment.

3. DEDUCTION OF TAX FROM DIVIDENDS ETC.

(i) Tax to be Deducted from Dividends Paid or Credited—Section 108

Where a company (other than a co-operative society *as per* paragraph 12 of Part I schedule 6), pays or credits shareholders with a dividend derived (by virtue of section 14) from Malaysia the company is entitled to deduct tax at the rate applicable to the company for the year of assessment in which the dividend is paid or credited.

Where a company pays or credits a dividend as above without deducting tax, then the Act provides (section 108 (2)) that such a dividend shall be deemed to have been deducted.

Note: Section 14 (4) provides inter alia that a dividend "other than money" is to be considered as dividend equal to the amount of the market value of such property. The above provisions for deduction of tax apply therefore to such dividends also.

(ii) Certificate of Deduction to each Shareholder

Shareholders are to be supplied with a certificate setting out the gross dividend and the tax deducted or deemed to be deducted and they can use this certificate to claim an offset against tax payable by each of them.

(iii) Statement of "TOTAL AMOUNT" Deducted to D.G.

Where a company has been resident for a basis year (say 1970) for the year of assessment 1971 it must within three months of the beginning of the year of assessment, by 1.4.1971, submit to the D.G. a statement in the prescribed form setting out the total amount of tax deducted or deemed to be deducted, from dividends paid or credited to shareholders in that basis year (1970).

(iv) Comparison by D.G. with "TOTAL AGGREGATE"

The D.G. if he accepts this total compares this total amount (say \$200,000/-) with an aggregate calculated as follows:

The tax payable by the company in that year of assessment (at 40% on adjusted profit of say \$0.5 million) is:	\$200,000
Less any reliefs for double-taxation under section 132 or 133 say: ..	10,000
	<hr/>
	\$190,000
Plus any credit carried forward under section 108 (6) from the previous year (1970) say:	50,000
	<hr/>
Total Aggregate (for year of assessment 1971)	\$240,000

The "total amount" of tax deducted from dividends is \$200,000/- and this is compared with the total aggregate \$240,000/-.

(v) Credit after Comparison to be Carried Forward

This situation where the "total aggregate" exceeds the "total amount" means that the difference of \$40,000/- is carried forward as a credit to the next year of assessment. We will continue the example to illustrate what happens if the reverse happens.

(vi) Debit Payable to D.G. Forthwith

During the next year of assessment—1972—the following situation arises (perhaps because the company distributes a realized capital profit). The company in the basis year 1971 withholds tax on dividends to a total amount of \$180,000/- but the total aggregate is only \$160,000/- as follows:

The tax payable by the company for the year of assessment (40% of say \$0.3 million)	\$120,000
Less any reliefs under section 132 or section 133 say	NIL
	<hr/>
	\$120,000
Plus credit carried forward under section 108 (6) from previous year (\$240,000 — \$200,000)	40,000
	<hr/>
Total Aggregate	\$160,000

Now the "total amount" of tax withheld (\$180,000/-) *exceeds* the "total aggregate" (\$160,000) by \$20,000/- i.e. the company has deducted \$20,000/- more tax from dividends than the amount paid or payable to the D.G. This has an unpleasant result—for the \$20,000/- becomes immediately payable to the D.G.!

As mistakes in the application of section 108 have been and still can be, very expensive, we repeat the argument in slightly different words.

(vii) Summary and Examples of Application of Section 108

Every company assessable to tax in Malaysia is required to pay tax on its chargeable income at 40%. This tax is to be paid in every year of assessment based on the income of the company for that year of assessment. This income is calculated on the profits of the company during the basis period. This basis period is usually the preceding calendar year but where the company prepares its accounts for a period ending on a date other than 31st December i.e. say on 30th September in the basis year, that period may be and usually is, accepted as the basis period by the D.G. The tax so paid or payable by a company is kept track of in the D.G.'s office for the purpose of section 108 which entitles a company to deduct tax at 40% on the dividends which it pays or credits to shareholders. The purpose of keeping track of the tax paid or payable on profits is that if the company should deduct or be deemed to have deducted a total amount of tax greater than the aggregate of:

- (i) the amount of tax (if any) chargeable on the company for that year of assessment, less any unilateral or double-taxation relief given the company for that year of assessment; and
- (ii) the amount of balance (if any) carried forward from the immediately previous year of assessment. This "balance" is defined in section 108 (6), and is the excess of the "compared aggregate" over the "compared total".

Two examples will clarify:

Example 1. *X Co. Ltd.*, commenced business on 1.7.1970 and for the year ended 30.6.1971 its adjusted profit was \$1,000,000 (Income Tax @ 40% will be \$400,000)

Gross dividends paid on 31.7.71	\$900,000
Tax deducted from dividends	360,000

Note: Here the year of assessment for which the tax is payable is y/A 1972.

Basis year for y/A 1972	is	1971
Basis period for y/A 1972	is	1.7.1970 to 30.6.1971

The "compared total" is composed of tax deducted or deemed to be deducted in the basis year and not the basis period, hence the deduction of tax on 31.7.1971 in this case is still within the basis year 1971 (although it falls for this company in the basis period for the y/a 1972).

Tax paid/payable for the y/A 1972 and the tax deducted from the dividends in the basis year 1971 are compared as follows.

		Section 108 (4) Credit a/c			
B/y 1971	Tax deducted	\$360,000	y/A 1972 Tax paid/payable	\$400,000	
	Balance c/d	40,000			
		\$400,000			\$400,000
			y/A 1973 Bal. b/d		40,000

Note: If however *X Co.* had paid this dividend (perhaps as an interim dividend) on or before 31.12.1970 it would have suffered the serious consequence of section 108 (5) i.e. the 360,000 tax deducted would have no credit in the account above and will become payable to the D.G. and also in y/a 1972 further tax of \$400,000 is payable to the D.G.

Here the credit allowed to be carried forward is \$40,000.

Example 2. The above *X Co. Ltd.*, has the following facts for the 2nd year. Adjusted profit for the year ended 30.6.1972 = \$700,000 (Income Tax @ 40% will be \$280,000)

Gross dividend paid on 31.5.1972	\$1,000,000
Tax deducted from dividends	\$ 400,000

Here the year of assessment for which the tax is payable is Y/A 1973

Basis year for y/A 1973 is 1972

Basis period for y/A 1973 is 1.7.1971 to 30.6.1972

Tax paid/payable for the y/A 1973 and the tax deducted from the dividends in the basis year 1972 are compared as follows:

Sec. 108 (4) Credit account

B/y 1972 Tax deducted		y/A 1973 Bal. b/d.	\$ 40,000
from dividends	\$400,000	y/A 1973 Tax paid/payable	280,000
		Balance	80,000
			<hr/>
	\$400,000		\$400,000
			<hr/>
Bal. b/d.	80,000		

The amount of \$80,000 will not be allowed to be carried forward to y/A 1974 and must be paid to the D.G. in 1973 when he serves a requisition under Sec. 108 (5).

(viii) Section 108 in Accountants' Language

As section 108 causes a lot of difficulty even to students of accountancy we will describe the effects again in terms of book-keeping. Whenever a company makes a profit the Act provides that tax is payable on it at 40%. This tax becomes payable in any year of assessment (1st January to 31st December) based on the preceding year's profits. A company's accounts drawn up at any date during the preceding year are usually acceptable to the D.G. When tax becomes payable under the Act we can imagine an account being credited in the books with the tax payable. When a dividend is paid or credited, tax is deducted under section 108 and this tax deducted is debited to the same account to which the credit is made. The D.G. requires from the company an account of tax withheld on dividends during a basis year to be submitted by 31st March of the next year, and then compares this with the total of any tax payable by the company plus any credit balance carried forward before under section 108 (6). If this comparison shows that the tax deducted on dividends is greater than the above total it becomes payable to the D.G. forthwith. In our second example above *XY* company has deducted \$80,000 of tax in

excess of the total credit and this \$80,000 is "a debt due from the company to the government" payable on a requisition being served on the company by the D.G. Incidentally it should be noted that the total adjusted profit of this company for the two years of assessment is \$1,700,000, while gross dividends paid total \$1,900,000, so that in this case the problem arose because of a payment of dividends in excess of adjusted profit of \$200,000 on which tax of \$80,000 became due.

To put this in another way where a firm had made no revenue profits at all it could have no "credit" for tax payable. If it has made a capital profit of \$1 million and distributes it or credits it to shareholders as a dividend it must still deduct 40% on this under section 108 and this will be payable to the D.G. under section 108 (5). Thus in effect the capital profits of such a firm which has no revenue profits, are still taxed when they are distributed as dividends.

(ix) Debit Balance Payable on Requisition

If and when a debit balance arises as above the D.G. will serve a requisition on the company in the prescribed form, asking them to pay the amount, which becomes a debt owed by the company to the Government.

(x) Additional Requisition

The situation may arise where after such a requisition has been served to pay a debit balance (brought about by comparison of "total amount" and "total aggregate") that, due to a repayment of tax for that or a previous year of assessment, after the date of such requisition, the "total aggregate" is reduced. (The reader should recall that the debit was the result of the "total amount" being greater than the "total aggregate"). In such case the additional debit so arising will also become a debt due from the company to the Government. [Section 108 (7).]

(xi) Adjustment and Repayment

Since changes can occur in the components of either of the two totals, used for comparison, the Act provides also that the D.G. may make such revisions and such repayments of tax, or debt paid under subsections (5) or (7) and the requisitions, "as appear to him to be appropriate in the circumstances". [Section 108 (8).] These provisions ensure that the running balance is subject to such adjustments as become necessary, and the resulting overpayment by the company if any can also be repaid to it. [Section 108 (8).]

(xii) Date of Payment of Dividend for Purposes of Section 108

As in deciding a question under section 108 the date of payment of a dividend may become most crucial, section 23 (b) specifically provides that, the date is that date on which the cheque etc. is posted or delivered by the payer, or the distributor in the case of dividends in kind. However section 108 also includes dividends which are only credited, so it is provided that where section 108 has been applied to a dividend so credited, it shall not apply again to the same dividend when it is paid. [Section 108 (9).]

(xiii) Presumptive Debit under Section 108 (10)

Where a company although not entitled to deduct tax under section 108 from a dividend paid or credited still issues to any *one* of its shareholders, a certificate purporting to show that such deduction has been made, then an amount equal to the total amount of tax which would have been deducted, if section 108 (1) and (2) had been applicable, from the gross amount of the dividend (ascertained as per (2)) paid credited or distributed to *all* its shareholders, shall be a debt due to the Government, and the D.G. will serve a requisition which the company must pay. [Section 108 (10).]

An example will clarify this:

Illustration

TRIX Co. Ltd., is not entitled to deduct tax from a dividend paid, under section 108, but it issues a certificate to 'M' *one* of its ten equal shareholders for \$40,000/- as tax deducted on an apparent 'dividend' of \$100,000/-. It is ascertained in accordance with section 108 (2) that a total dividend deemed to be \$1,000,000/- was paid, credited or distributed to *all* the shareholders (including 'M'). The debt which becomes due is:

$$40\% \text{ of } \$1 \text{ million} = \$400,000$$

It should be noted that there is in this case no provision for comparison etc., and the tax deemed to be deducted from the dividends of *all* the shareholders becomes a debt due even where a purported certificate is issued to only *one* of them.

The Act provides however that where the company can prove to the satisfaction of the D.G. that such certificates were issued only to particular shareholders, that debt shall be reduced proportionately.

4. DEDUCTION OF TAX FROM INTEREST—SECTION 109 & SECTION 6

Where a person is liable to pay any form of interest whatever, derived in Malaysia, to another company, partnership, or body of persons, who are not known to him to have a place of business in Malaysia at time of payment, he must deduct tax at the rate applicable i.e. normally 40% but 15% on "approved loans". This must also be done if interest is paid to an individual not known to him to be in Malaysia at time of payment.

Whether or not such tax on the interest has been deducted, the amount of tax must be paid to the D.G. within one month.

However the D.G. may write to the payer to use another rate or to pay without deduction, in which case these instructions must be followed.

Where the payer may not have deducted tax as required, but has paid the tax to the D.G. he has the right to recover the amount from the person to whom the interest was paid without the proper deduction.

Tax Set-Off

A set-off against tax payable is allowed where the gross income of a person includes dividends or interest from which tax has been deducted at source under section 108 or 109.

Illustration

X's chargeable income for the year of assessment 1972 is \$30,000/- which includes dividend (Gross) \$1,000/-.

Income tax deducted at source is \$400/-.

Income Tax on first \$25,000 (see scale of rates)	..	..	\$4,450
Income Tax on the next \$5,000 @ 30%	..	..	1,500
			<hr/>
Income Tax payable	..	..	\$5,950
Less Tax Set-off in respect of dividends—section 110	..		400
			<hr/>
Tax payable	..	..	\$5,550
			<hr/>

In the case of a business where accounts have been made up for a period longer than 12 months the D.G. may apportion the adjusted income in any way he thinks fit for two years of assessments (section 21 and section 41) basing such apportionment on those accounts. Any income from dividends or interest, from which tax has been deducted at source and which has been included in the gross income of the business accounts stated above, should also be deemed to be apportioned in the same manner as the adjusted profit, i.e. a set-off for the income tax deducted at source from dividends or interest will also be apportioned on the same basis as the adjusted profit. [Section 110 (2).]

Illustration

Z Ltd., made up its accounts for 18 months to 30.9.1970. The adjusted profit including a gross dividend of \$3,600 from a Malaysian company was \$18,000. The D.G. had decided to tax \$6,000 for the year of assessment 1970 and \$12,000 for the year of assessment 1971. The set-off for tax deducted at source would be as follows:

	Year of Assessment	Year of Assessment
	1970	1971
Chargeable Income	\$6,000	\$12,000
<hr/>		
Income Tax @ 40%	\$2,400	\$ 4,800
Less set-off for income tax deducted at source from dividends	480*	960*
<hr/>		
Income Tax payable	\$1,920	\$ 3,840
<hr/>		

$$*40\% \times \$3,600 = \$1,440$$

$$\$1,440 \times \frac{\$6,000}{\$18,000} = \$480$$

$$\$1,440 \times \frac{\$12,000}{\$18,000} = \$960$$

OFFENCES AND PENALTIES

1. OMISSION OR COMMISSION

Any person who contravenes, or fails to comply with any provision of the Act is guilty of an offence. This means that an offence can be committed by doing something against the Act, as well as by failing to do something as required by the Act. The penalties for the various offences are set out below.

2. PROCEDURE AND EVIDENCE

(i) D.G.'s Statement Evidence of Fact

In criminal and civil proceedings under the Act, a statement signed by the D.G. or an authorized officer which is attached to "the information, complaint, or statement of claim shall until the contrary is proved, be evidence of any fact stated therein". However the above procedure cannot be used to prove the intent of the defendant, and it cannot be used at all in any proceedings for an offence punishable by imprisonment. [Section 142 (2).]

(ii) Certified Transcript Admissible as Proof

In relation to particulars of tax contained in any return or other document, a transcript certified by the D.G. or any authorized officer to be a true copy, shall be admissible as proof of those particulars. [Section 143 (3).]

(iii) Documents and Statements Induced by Lawful Promise Admissible

Even where a person proves that he made a statement or produced documents because of an inducement or promise lawfully made by the D.G. or an authorized officer, these can be still used in evidence against him. The mere fact of the inducement or promise alone does not render such statement or document inadmissible. E.g. an investigator promises a person who has evaded tax that if he makes a full confession the D.G. will compound the offence under section 113 (2) where a penalty equal only to the tax evaded is payable. The tax evader is induced by this promise to produce a well hidden set of books which reveal that an extensive elaborate and systematic scheme has been in operation to evade tax. It would appear that this set of books can be used as evidence to prosecute under section 114 which carries a penalty of three times the tax evaded, a fine up

to ten thousand dollars and imprisonment up to three years or both fine and imprisonment. However, this does not mean that this set of books will not be ruled out on some grounds other than the inducement.

It would appear that a promise to compound an offence is lawful as the Act in section 124, empowers such a compounding. Any statement made by a person or any document produced by him as a result of such a lawful promise can also be used against him in legal proceedings under any section and also to recover money due by way of tax or penalty.

(iv) Act Not to Affect Certain Provisions of "Evidence Act" Section 142 (5) (a)

The part of the Evidence Act 1950 (Act 56) not to be affected by the Income Tax Act is Chapter IX of Part III. We give below an outline of only the important provisions:

(a) Witnesses

All competent witnesses may testify.

(b) Testimony of Accused

In criminal proceedings the accused may testify in his own behalf, but the cross-examination relating to his credit, shall be limited to the extent thought proper by the Court.

(c) Marriage Partner can be Silent

A husband or wife cannot be forced to disclose a communication made during the marriage.

(d) Sources Secret

Judges, Police and Revenue Officers are not required to disclose the source of their information about the commission of offences.

(e) Privileged Communications of Advocates, Solicitors, and their Employees

These persons are not permitted to disclose any communication made to them by the client or on the client's behalf in the course of employment. This restriction extends also to advice given to the client. But this privilege may be breached by the client's express permission. However any communication made in the furtherance of an illegal purpose is not protected.

Also any fact observed by the solicitor or advocate showing that any crime or fraud has been committed since the commencement of his employment is not protected from disclosure. This is so even where it comes to his attention inadvertently.

The above protection extends to the servants and clerks of advocates and solicitors and also to interpreters.

(f) Witness to Answer Questions Even if Answer Incriminates Him

No witness can be excused from answering a question relevant to the matter at hand, on the grounds that it might incriminate him or make him liable to a civil suit, but where he is compelled to answer, such answer cannot be used to "subject him to any arrest or prosecution, or be proved against him in any criminal proceeding, except a prosecution for giving false evidence by such answer".

(v) Documents etc. Protected by Evidence Act Chapter IX of Part III

Those documents, things or information, which a lawyer, solicitor, banker, government official or other person would not be required to produce to a court by virtue of protection under Chapter IX of Part III of the Evidence Ordinance, cannot because of any provision of the Income Tax Act be contrived to be required to be produced to the D.G., Special Commissioners, or any other person. [Section 142 (5) (b).]

3. FAILURE TO FURNISH RETURN OR GIVE NOTICE OF CHARGEABILITY—SECTION 112

A person who without reasonable excuse fails to furnish a return under section 77 (1), or does not give a notice of chargeability under section 77 (2) or (3), shall be guilty of an offence and is liable to a fine up to one thousand dollars or imprisonment up to six months or both. In such a proceeding the burden of proof that a return was in fact made shall be upon the accused person.

Where a person, though guilty of this offence, has not been prosecuted as above, "the D.G. may require that person to pay a penalty equal to treble the amount of the tax which, before any set-off, repayment or relief under this Act, is payable for that year". The use of the word "relief" above raises certain questions bearing on the calculation of the amount of the penalty e.g. Mr. Adam has a total income of \$15,000 for y/a 1971 on which he has committed an offence by not furnishing a return. As he is married and has children and insurance he would normally be allowed a reduction (of say \$5,000) from this figure before tax is charged on chargeable income. While on the one hand the words quoted would appear to mean that he must pay a penalty, three times the tax payable on the \$15,000, on the other hand it could be argued that the penalty should be three times the tax due on \$10,000 for the Act calls these and other reductions "deductions", (e.g. in sections 46 to 51) and, it could be argued that on a strict construction "relief" is not "deductions". Another point in favour of this argument is that "the amount of the tax, which . . . is payable for that year" refers normally to the tax calculated upon the chargeable income which in section 45 (1) is referred to as the total income less any deductions allowed by Chapter VII of Part III of the Act.

On close consideration of the Act however it is clear that since "set-off" refers to the recoupment of tax deducted at source on dividends (Section 110), and "repayment or relief" refers to non-resident relief under section 130, and double-taxation or unilateral relief under sections 132 & 133 respectively, "deductions" (i.e. the \$5,000 in Mr. Adam's case) are not prohibited by section 112. Hence the penalty would be as follows.

Total Income	..	..	..	..	..	\$15,000
Less "deductions"	..	..	..	..	..	5,000
						<hr/>
Chargeable Income	..	..	..	..	..	\$10,000
*Tax payable on Chargeable Income	..	..	..	..	..	1,050
						× 3
						<hr/>
Maximum Penalty	..	..	..	..	..	\$ 3,150
						<hr/>

*As per Schedule I of the Act.

Payment of the penalty frees the person of liability to be charged for this offence. Under section 124 (3) the D.G. may remit or abate a penalty imposed before a conviction. As this is such a penalty, where it is so reduced the payment of such lower penalty also discharges the liability to prosecution for this offence. [Section 112 (3) (b).]

4. INCORRECT RETURN OR INFORMATION—SECTION 113

(i) Not in "Good Faith"

Where, a person on his own or another's behalf makes an incorrect return, he is guilty of an offence under the Act unless he can satisfy the court that he did this in good faith. On conviction he is liable to a fine up to five thousand dollars and it is provided that he shall pay a special penalty of double the tax undercharged as a consequence of such an incorrect return.

An incorrect return or the giving of incorrect information can lead to income being omitted or under-stated but if the act is done innocently, with no intention to evade tax, in other words with an absence of bad faith, and the person charged under section 113 (1) can satisfy the court of this, then he will not be convicted. This may well be a difficult task.

(ii) Simple Error

In the absence of a prosecution under section 113 (1) the D.G. may require that person to pay a penalty equal to the tax undercharged as a result of the incorrect return

or incorrect information, and the payment of such penalty, (or a penalty reduced under section 124 (3)) renders that person not liable to be charged on the same facts with an offence under section 113 (1). [Section 113 (2).]

5. EVASION

(i) Actions and Penalties

The most serious penalties are provided for "any person who wilfully and with intent to evade or assist any other person to evade tax" does any of the following:—

- (a) Omits income from returns.
- (b) Makes a false statement or entry in a return.
- (c) Gives a false answer (orally or in writing,) to questions or requests for information. It should be noted that such questions or requests must be lawfully asked or made under the Act. Of course persons protected from answering by the Evidence Act (see paragraph 3 above) can refuse to answer.
- (d) Prepares or authorizes the maintenance of false account books and records.
- (e) Falsifies, or authorizes the falsification of, existing books and records.
- (f) Makes use or authorizes the use of any fraud, art or contrivance.

On conviction such a person is liable to pay a fine up to \$10,000 or be imprisoned up to three years or both. In addition such person "shall pay a special penalty of treble the amount of tax which has been undercharged in consequence of the offence". Section 114 (1).

(ii) Presumption that False Entry Act of Person

Where false entries or statements are proved to exist in returns made on a person's behalf, the person himself shall be presumed to have done these acts until the contrary is proved. Thus where an illiterate businessman has his returns prepared by some other person but has put his thumbprint on it, and such return has been proved to be false in proceedings under section 114, it is presumed that the false return was his act. Before this businessman can disavow the act he must rebut the above presumption. This provision prevents a person charged from easily claiming that his employee or accountant is responsible. For the onus of proving this is on the person. Standard practice even where professionals, or part-timers prepare accounts and returns etc., is to always ask the client to sign or make his mark as the case may be. Yet where a person can prove that he had no knowledge of the contents (admittedly a difficult task) and where the contents represent perhaps, a systematic attempt to evade tax, the person who prepared the return could be liable to the severe penalties provided by section 114, for this section extends to persons who "assist any other person to evade tax". [Section 114 (2).]

6. THREE DEGREES

(i) Offences and Penalties

It should be noted that basically, the Act provides three degrees of penalties for three degrees of offences.

The first degree is for making an incorrect return or giving incorrect information leading to tax being undercharged, otherwise than in good faith, (fine \$5,000, no imprisonment, special penalty of double the tax undercharged).

The second degree is for failing to make a return, or giving notice of chargeability (fine \$1,000, imprisonment 6 months, penalty of treble the amount of tax before relief), while the third degree (fine \$10,000, imprisonment 3 years, special penalty of treble the tax undercharged) is for wilful evasion. This last is applicable where a deliberate and systematic attempt, demonstrating an intent to evade, has been proved.

(ii) Different Procedure

In the first degree of offence, not carrying a penalty of imprisonment, a statement about the facts of the case signed by the D.G. or an authorized officer is evidence of such facts. [Section 142 (2).] The other two degrees, carrying a penalty of imprisonment, cannot be proved by this expedient manner. While in an appeal before the Special Commissioners the onus of proof is on the appellant (but this is "no higher than proof on a preponderance of probability . . . (and it is) not necessary for the taxpayer to attend in order to discharge the burden". *P.Q.R. v. C.I.T. Singapore* [1961] 27 *M.L.J.* 273, *C.A.*), in proceedings before the courts there is a distinction laid down in section 142 by which charges carrying a penalty of imprisonment have to be proved by ordinary means of adducing evidence in court.

7. DEPARTURE FROM MALAYSIA AN OFFENCE—SECTION 115

Any person, who while knowing that a certificate under section 104 has been issued against him (see Chapter V, paragraph 2 above) leaves or attempts to leave Malaysia, without paying the tax or giving security, shall on conviction be liable to a fine up to one thousand dollars or imprisonment up to six months or both. Also a police officer or immigration officer may arrest without warrant any person who he reasonably suspects is trying to leave as above.

8. OBSTRUCTION OF OFFICERS

Any person obstructing or hindering the D.G. or an authorized officer in the exercise of duties under the Act, is liable on conviction to a fine up to two thousand dollars or imprisonment up to one year or both. The following actions of obstructions are specifically listed in section 116.

- (a) refusing entry into any land, building or place as permitted by section 80;

- (b) obstructing exercise of function under Act (this seems to be a "catch-all" provision);
- (c) refusal to produce books, documents etc.;
- (d) failure to give reasonable assistance for any of the purposes of the Act;
- (e) refusing to answer any question, relating to the purposes of the Act, lawfully asked.

9. SECRECY IN TAX MATTERS—SECTIONS 117, 138

One universal feature of Income Tax Acts in most countries is the requirement of secrecy from all those who are concerned with the information obtained in the administration of Income Tax. The need to prevent business competitors from getting valuable information and the ordinary right to privacy of the citizen have no doubt been important factors.

The following persons known as "classified persons" must keep confidential, tax matters known as "classified material" (see below) except as permitted by the Act. Classified persons are:

- (a) Officials having an official duty under the Act.
- (b) Auditor-General and public officers under his direction and control.
- (c) Any person advising or acting for a person chargeable to tax e.g. an accountant, or tax consultant. The employee of such accountant etc. is also included.

Any such classified person who, in contravention of the permitted exceptions in section 138, communicates classified material (any return or other document made for purposes of the Act, and other information coming to the attention of a classified person in his capacity as such) to another person, is guilty of an offence, and on conviction is liable to a fine up to two thousand dollars or imprisonment up to one year or both. Giving another person access to classified material carries a similar penalty. [Section 117.]

This means *inter alia* that accountants and even their most junior clerks are not permitted to gossip over lunch about the "five figure income of 'so and so'".

However this requirement to keep tax matters confidential is qualified and in the following circumstances the information can be disclosed:—

- (a) for purposes of this Act or another tax law i.e. any written law relating to estate duty, film hire duty, payroll or turnover tax, and any other written law declared by the Minister to be "another tax law" for the purposes of this section);
- (b) in order to facilitate a prosecution under this Act, or for tax or duty under another tax law;

- (c) with written authority of Minister, or the person or partnership to whose affairs it relates;
- (d) to the Auditor-General or his officers;
- (e) the Auditor-General can use the classified material in the proper exercise of his office.

All officials only, dealing with classified material, are also required to make a declaration to keep this confidential but the other classified persons are bound by the Act to do the same.

10. OFFENCES BY OFFICIALS—SECTION 118

(i) Acts which are Offences

Any person having an official function under the Act who does any of the following is guilty of an offence and on conviction is liable to a fine up to ten thousand dollars or to imprisonment up to three years or to both.

The acts are:

- (a) Demanding money in excess of tax or penalties due under the Act (otherwise than in good faith).
- (b) Withholding money from tax or penalty collected.
- (c) Makes a false report accounting from such tax or penalty, otherwise than in good faith.
- (d) "Defrauds any person, embezzles any money, or otherwise uses his position to deal wrongfully with the D.G. or any other person".

(ii) Unauthorized "Tax Collectors"

An unauthorized person who collects or tries to collect tax or penalty is liable on conviction to the same penalties as above.

11. MISCELLANEOUS

(i) Other Offences—Section 120

For the following offences without reasonable excuse a person on conviction is liable to a fine up to one thousand dollars or imprisonment up to six months or both.

- (a) Failure to comply with a notice given by the D.G. to:—
 - make a specific returns or personally produce books (section 78);
 - give particulars of banking accounts, assets, sources and other facts bearing on chargeability to tax (section 79);
 - give the D.G. a set of books, records, and accounts translated into the National Language (section 80 (3));

- give the D.G. all information about his own or another person's income, assets or liabilities (section 81). (This would not apply to advocates, solicitors and bankers under certain circumstances. See Chapter V, paragraph 3).
 - keep records and issue receipts and retain duplicates in a form and manner laid down by the D.G. (section 82 (3));
 - supply the D.G. with particulars of the income of a person chargeable to tax, represented by money or property under his control (section 84 (1));
 - supply particulars of the landlord or owner, and the rent (section 85);
 - give fuller or further returns (section 87);
- (b) Failure to comply with statutory order made by the D.G. to:—
- keep records, and issue receipts and retain duplicates, in a form and manner laid down by the D.G. (section 82 (3));
 - prepare, keep and deliver to the D.G. for the employees specified, a return giving the names and addresses, and full amount of gross income under section 13 (section 83 (1));
- (c) Fails to give a notice to the D.G. that:—
- he has commenced to employ a person who is or will be chargeable to tax on his employment income (section 83 (2));
 - he has, or is about to, cease to employ a person chargeable to tax on his employment income (section 83 (3));
 - to his knowledge an employee of his, chargeable to tax on his employment income is leaving Malaysia for a period exceeding three months (section 83 (4));
- (d) Contravenes:—
- duty to keep sufficient books and records (section 82 (1));
 - duty to make appropriate entries in above within sixty days of each transaction (section 82 (6));
 - duty by a person selling goods in Malaysia on behalf of a non-resident person such sales being in the course of a carrying on a (Malaysian) business of the non-resident (section 84 (2));
 - duty of "precedent partner" to make a return when requested by the D.G., or within three months on his own volition (section 86 (1));
 - duty of person who has given a Malaysian address to the D.G. to inform him in writing within three months of a change to another Malaysian address (section 89);
 - the requirement even while holding himself out as an accountant, tax adviser, or tax consultant to be qualified as an accountant under paragraph 15 of Schedule 5 before acting on behalf of any person for any of the purposes of the Act (section 153 (1)).

[But where a company, body of persons or partnership, holds itself out to be accountants, tax advisers, or consultants, it is sufficient if at least one such qualified member, employee or partner, is present in Malaysia for a total of more than 182 days during that year. Such days need not be consecutive and the person need not be the same person. Also no solicitor or advocate is restricted in the lawful practice of his profession by this section.]

(ii) Statute-Barred Offences; Aiding Abetting and Inciting—Section 121

Twelve years after any of the following offences have been committed no proceedings can be instituted.

- (a) Incorrect Return or Information (section 113).
- (b) Leaving Malaysia while knowing certificate of detention under section 104 exists (section 115).
- (c) Obstructing tax officers in the course of their duty (section 116).
- (d) Offences by tax officers (section 118).
- (e) Any "other offence"—see (i) above (section 120).

Any person who aids, abets or incites any other person to commit any of the offences (a) to (d) above is deemed to have committed the same offence and be liable to the same penalty.

(iii) Tax Payable in Addition to Penalty—Section 122

It should be stressed that even where proceedings are instituted or a penalty fine or imprisonment imposed, the tax is still payable. In effect, suppose on conviction tax undercharged is found to be \$200,000 and further it has been held to be wilful evasion. Then in law the following can happen:

Penalty	\$600,000
Fine	10,000
Tax Payable	200,000
	\$810,000

and the evader can be sent to jail for up to three years. Further, of the \$810,000 paid \$610,000 cannot be used to claim say double-taxation relief and the whole \$810,000 is not an allowable expense.

Additionally such person is still liable for the payment of any debt or the making of a return under the Act.

(iv) Court—Section 126

Any subordinate court, (as defined in schedule 5) is empowered to try any offence under the Act and on conviction to impose the full penalty notwithstanding any other written law.

(v) Recovery of Fines and Penalties

Special penalties imposed for making incorrect returns, giving incorrect information or wilful evasion are recoverable in the same way as fines imposed on conviction.

Other penalties under section 112 (3) and 113 (2) may be recovered according to sections 103 to 106, being treated as tax payable only so far as these sections apply.

(vi) Sanction for Prosecution—Section 123

Subject to Article 145 (3) of the Federal Constitution, prosecutions under the Act for the offences set out in sections 113 to 119 may only be instituted with the sanction of the Public Prosecutor, while all other offences can be prosecuted with the sanction of the D.G. The D.G.'s power to compound any offence at any time before conviction however is discussed below.

12. COMPOUNDING—SECTION 124**(i) Need for Compounding**

Most modern nations use the taxation of income as a just and equitable means of redistributing wealth, using the money obtained to run the services which government provides for its citizens. The stress of the Act is on the expeditious collection of tax, hence provision for the compounding of offences is universal. Again the resources of the investigation and anti-evasion section are limited and have to be devoted to that activity which will give the best return. This means that on the initial discovery of tax evasion on a large scale it may be expedient all around to compound the offence for such compounding achieves nearly all the aims of society, by recovering tax evaded, punishing the offender and warning other like-minded citizens. In recent years the authorities have recovered several million dollars by this process. The statutory provisions for compounding are set out below.

(ii) Procedure

Before the point of conviction the D.G. may compound any offence whatever under the Act. On such a compounding the D.G. may order the offender to pay a sum of money not exceeding the maximum fine plus any special penalty which would have been payable on conviction e.g. in the case above where the tax undercharged was \$200,000 and the person was charged for wilful evasion the maximum amount, such a person could be ordered to pay on compounding would be \$610,000 (fine \$10,000 plus special penalty \$600,000). The tax undercharged would also be due.

However, the D.G. is only authorized to exercise his power to compound if the person, admits in writing that he has committed the offence and requests the D.G. to compound it.

(iii) Order and Consequences of Compounding

Where an offence is compounded as above the D.G. is required to make an order in writing, with the person's admission of the offence and request for compounding,

attached. Such order must give particulars of the offence committed, the sum of money to be paid and the method of payment i.e. instalments if any. Such order prevents any further or subsequent prosecution for that offence, and being final is not subject to appeal. The sum of money shown on an order can be recovered as if it were a judgement of a subordinate court, e.g. if person fails to pay, his property etc. can be seized and auctioned off.

The D.G. is also empowered to abate or remit any penalty imposed under the Act, except a penalty imposed by a court on conviction. [Section 124 (3).]

INCOME AND RESIDENCE

1. WHAT IS INCOME?

We feel it best to approach the problem of defining "income" and other connected terms through some discussion of semantics. This will also throw light on the interpretation of statutes and the bearing of case law with respect to "*ratio decidendi*" and "*obiter dicta*" etc., on the working of the apparatus of taxation.

2. SEMANTICS

Semantics is the study of the meaning of meaning. It is related to philosophy in this way—philosophers have to conduct their discourse by the use of language and it is now commonly held that most of the philosophical problems that have engaged some of the finest minds within recorded history were essentially linguistic and semantic problems.

Unfortunately it takes time for new ideas to affect other disciplines so we feel it will be useful if we illustrate some linguistic traps by using the title of paragraph 1: "*What is Income*"?

The way in which the above question is written contains a linguistic trap which leads to a maze of confusion. The trap is this—the arrangement of the three words in the question almost demands an answer in the form:—

"Income is....." The linguistic form of the question exerts a moulding pressure on the form of the answer. There are more subtle aspects of the trap e.g., the question assumes that there IS something which is essentially in itself that identical THING and it is also implied that we just have to search very hard until we find this mysterious essence.

3. CONSENSUS

Instead of asking "What is Income" and falling into the trap we should ask, "What is it that we should agree to call 'income'?" Thus definitions are a matter of consensus. If language is defined as a social activity the definition of a term like "Income" is on one view only a matter of agreement among the businessmen, government officials, and other citizens who have an interest in the matter. Such a consensus can be embodied in the form of a definition in a Statute to become the law of Malaysia. However, if subsequent

events make it necessary to expand or restrict the term "Income", the Statute can be amended.

4. CASE LAW

The semantic aspect does have a bearing on Case Law. Lawyers and text-book writers make an apparent distinction between "*ratio decidendi*" and "*obiter dicta*". They say that case law can create a binding precedent where a superior judge (superior in the hierarchy of the courts) makes a decision on the facts of a case. They say that this decision can be divided into that part which is binding—"ratio decidendi" i.e. that part related to the basic similarities of the facts of the case; and "*obiter dicta*" being those parts of the judgement which are learned remarks in passing on the surrounding area. This distinction is used by some to justify the statement that legal decisions are arrived at by a purely rational and logical process. But one of the great games of the legal profession is that called, "distinguishing a case". This is a process of shaving a "ratio-deciding" to make it fit slightly different facts. In the context of an absolute claim to logic in legal decisions a close study of such distinctions sometimes arouses considerable doubt. Yet for the want of a better substitute, the existing legal system has to serve the purposes of society.

5. STATUTORY LAW

For these and other reasons recent Statutes carry more weight than case law except that Statutes themselves being written in words, come within the ambit of the legal system whose help is invoked when a dispute arises about the interpretation of Statutes. In such a dispute, case law on the interpretation of Statutes has a bearing on the Statute. Again Statutes often embody provisions designed to avoid the "laws delays" by substituting administrative procedures to replace, or at least try to reduce the load on, the judicial processes (e.g. the Special Commissioners appointed under the Act cut down the volume of cases which would otherwise go to court). Modern states often find it necessary to seek an expeditious procedure say for the acquisition of private land by the state. The term "judge-proof legislation," is used to describe the attempted objective but in most functioning democracies the courts normally do have an over-riding authority and even if all else fails writs of "mandamus" or "certiorari" can be used where applicable; to exercise that function of the law claiming to act as the bulwark for the individual threatened by the abuse of administrative power. Some countries use an Ombudsman to perform a similar or supplementary function.

6. INTERPRETATION OF STATUTES

Case law on the Interpretation of Taxing Statutes has led to the following general rules:

- (a) Words used shall have their plain and ordinary meaning unless otherwise stated in the statute. Thus "person" normally refers to any human being but in the Act it "includes a company, body of persons and a corporation sole".

- (b) Where two equally possible results can arise from the ambiguity of the wording of an Act that result which is favourable to the taxpayer will hold.
- (c) The fact that a particular interpretation may have an unfair or inequitable result is not relevant, for it is not the function of the Courts to pass judgement on the intention of the legislators. Only the words of the Act are to be considered, and other materials like speeches in Parliament during the debate on the Act would be inadmissible.
- (d) Where an Act contains a list of terms followed by a catch-all clause, the meaning of the clause is restricted to the same class of terms e.g. in the phrase "road-signs, signals, lines, notices, and other indicators," the last part "and other indicators" is a catch-all clause and its meaning is restricted to include the same class of notices as that of road-signs etc. Thus the blowing of a whistle by a policeman will not constitute an indicator in the phrase "and other indicators." This is known as the "*ejusdem generis*" rule, and it serves to make legislation more precise by preventing the interpretation of such catch-all phrases by both officials and citizens to extend the scope of Acts without fresh legislative authority.

[Readers interested in pursuing this matter further should consult—Maxwell, Peter Benson "*Maxwell on the Interpretation of Statutes*" 12th edition, London, Sweet & Maxwell, 1969.]

7. DISTINCTION OF CAPITAL AND REVENUE

(i) No Statutory Definition

Although in 3 above we have commented upon the advantages of a statutory definition of "Income," there is in fact no such definition in the Act, and we shall have to rely heavily on case law in making the fundamental distinction between capital and revenue, i.e. between capital and income. There is no tax at present on capital, but as regards income, section 3 in part reads:

"Subject to and in accordance with this Act, a tax to be known as income tax shall be charged for each year of assessment upon his income"

(ii) It Must Be INCOME

Since the tax is on INCOME this is the first prior condition to be satisfied, to bring an item into the ambit of the Act. At this stage we shall only outline some preliminary tests, but we shall keep coming back to this crucial distinction in later chapters. As we have indicated there is little difficulty in deciding on which side of a line the largest number of "occurrences" lie, so the distinctions in the occurrences not covered by the statute have to be based on cases, decisions on which have helped to define the boundaries or lines of demarcation. Yet each case has to be considered on its own attendant circumstances.

- (a) **Circulating or Fixed Capital:** Any incoming from circulating capital is revenue or income and from fixed capital, capital. The legal meaning of "capital" is different from the meaning put upon the word by accountants in phrases like "capital account". Legally "capital" includes what accountants call assets. Accountancy bodies define fixed assets as those which in the normal course of business will not be realized (turned into cash or debtors) during one year, while current assets are normally realized within one year.

Viscount Haldane in "*Smith John & Son v. Moore*", (12 T.C. 266) said "...fixed capital (is) what the owner turns to profit by keeping it in his own possession, circulating capital (is) what he makes a profit of by parting with it and letting it change masters."

- (b) **Not Necessarily Physical:** The actual nature of the object is not the only criterion, for while a motor-car is circulating capital for a dealer in motor-cars, it is fixed capital for a taxi-driver. There may be no physical object involved at all. The giving up of a dealership or certain rights like sole agency may lead to the receipt of money and it may well be necessary to decide whether this is fixed or circulating capital, for tax purposes.

- (c) **Source and Income:** If it involves the liquidation of a source of income it is fixed capital.

If the receipt is a substitute for the income itself it is circulating capital and hence is income. E.g. (1) tea-money received by a landlord for the transfer of the tenancy of rent-controlled premises is income, being considered as a receipt of rent in advance, yet the person paying the tea-money cannot claim this as an allowable deduction and it is treated as capital expenditure. Hence the fact that an item is income or capital in the hands of the receiver does not in itself decide its nature in the hands of the payer.

E.g. (2) If the passenger in a taxi dies or is permanently disabled as a result of an accident and he or his heirs receive a lump-sum in compensation, such a sum is not income, being a replacement for a source—his life or his earning capacity. Yet if he is disabled only for six months and receives compensation for this period, this is income, being merely a substitute for his lost earnings alone.

E.g. (3) A company engaged in rubber planting obtains a lease on forest land. It gives out contracts to cut and remove trees, receiving large sums for giving out these contracts. These sums will of course be liable for the supplementary "Timber Profits Tax" under Part IV of the Supplementary Income Tax Act 1967, (from 1969 onwards) but the question of income or

capital was decided as *income* in a similar case in India—*Pullangode Rubber & Produce Co. Ltd. v. C.I.T.* (Ker.) [(1971) 79 I.T.R. 738] on the reasoning that trees were sold and not a right to cut trees. Were the trees to form a part of the capital of such company however, the sale may well be classed as not income.

(d) Capital Profit not Income

The mere fact of buying something and selling it at a profit does not constitute income. In *Tebrau (Johore) Rubber Syndicate Ltd. v. Farmer (Surveyor of Taxes)* ((1910) 5 T.C. 658) a company bought a rubber estate with the idea of developing it for its rubber. Subsequently not having enough capital to continue they sold the estate at a higher price. The Commissioners' decision to uphold the assessment was over-ruled on the grounds that the main business of the company was to produce rubber and the profit on the sale of land was incidental to the main purpose and therefore not income.

8. IT MUST BE THE INCOME OF A PERSON

Besides being income, it must also belong to a person (see definition in Chapter I) for, our system of taxation, taxes a person on his income. Additionally the persons chargeable to such tax must be persons who are within the jurisdiction of our laws. Of the persons within our jurisdiction some may differ in their intentions as to where their permanent homes are, and those who have the intention to make their permanent homes here are taxed on their income no matter from where it is derived. But persons who do not so intend are taxed only upon their income derived from Malaysia.

Now it is an impossible task, to read an intention from a person's thoughts so the Act provides a test of such intentions, by considering the question of residence as an indicator of intention as follows:—

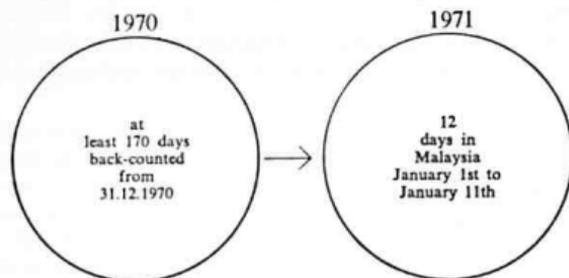
"3. Subject to and in accordance with this Act, a tax to be known as income tax shall be charged for each year of assessment—

- (a) in the case of a person ordinarily resident for the basis year for the year of assessment, upon his income from wherever derived; and
- (b) in the case of every other person, upon his income derived from Malaysia."

9. RESIDENCE

(i) Individual

In the case of an individual, residence is primarily measured by counting the number of days such individual is physically present in Malaysia, but a part of a day, is counted as a full day. Section 7 (1A).

Diagram VII-3: Residence by back-counting at least 182 consecutive days.

Result: Resident in basis years 1970 and 1971.

- (b) i. Even where the qualifying period of 182 consecutive days, (forward or back-counted) is broken "for such temporary absences as the D.G. may in his discretion allow to be taken to form part of that qualifying period" an individual is resident for the basis year for a year of assessment.

This provision ensures that where a temporary absence or absences (e.g. a ten-day course in Bangkok) interrupt the period of 182 consecutive days, and the D.G. chooses to exercise his discretion, then such broken period can still be taken to be a qualifying period. The plain and ordinary meaning of the words in section 7 (1) (b) (i) quoted above appears to indicate that the period of absence can be included in the counting of the 182 days.

It should be realised that in most cases residence confers a tax-advantage in that residents are allowed personal deductions and are taxed at scale rates as per Schedule I while non-residents (with some exceptions) enjoy no deductions and are taxed at 40%. This explains to some extent the discretion given to the D.G. by the exercise of which he can allow a person to be "resident", as above, in spite of temporary absence.

- ii. Even where an individual is in Malaysia, during a basis year (say 1971) for less than 182 days (say 120 days), and such period of 120 days in 1971 would have formed part of a consecutive 182-day qualifying period, but for unforeseen circumstances e.g. he may have had to leave suddenly on January 31st, 1972 for medical treatment in China returning only on 1st June 1973, with the result that the normal 182 consecutive day qualifying period was cut-off suddenly on 31st January 1972 on its 152nd day, the individual could be considered resident in the basis year 1971 if the D.G. exercises his discretion under section 7 (1) (b) (ii).

Another example will clarify that the 182 days (less the absence) may be entirely within one basis year:

e.g. In Malaysia from 1.4.71 to 29.9.71 i.e. 182 days.

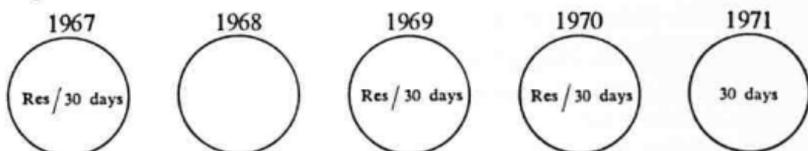
Left Malaysia for a week (1.7.71 to 7.7.71) but such absence treated by D.G. as a temporary absence under section 7(1) (b).

Result: Resident in basis year 1971.

If the D.G. refuses to exercise his discretion in any of the above two instances, his refusal cannot be a ground for appeal against any assessment, or against a refusal by the D.G. of a claim for repayment of tax or any other kind of relief. [Section 7 (2).]

- (c) (i) An individual is also considered to be a resident for a basis year if in that basis year he has been in Malaysia for a total period of at least 30 days and he has, in at least any three of the immediately four preceding years, been a "resident" under any provision or been present for a total period of at least 30 days. (Section 7(1) (c) (i) & (ii).)

Diagram VII—4: Residence under Section 7(1) (c) (i) & (ii)

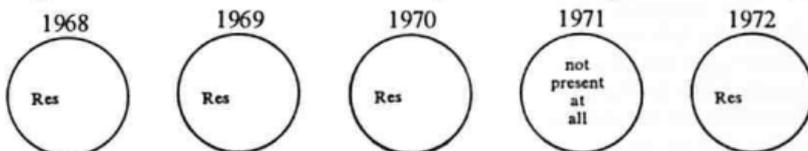


Result: Resident in basis year 1971.

Two points should be noted. Firstly—any three years from the four years 1967, 1968, 1969, 1970 would qualify and secondly—"residence" may be by any provision of the act or even mere presence for a total period of 30 days in any three of these four years.

- (d) For readers who may be thinking that 30 days presence for residence is a bit easy there is a further surprise. It is possible to be considered a resident for a basis year without being in Malaysia for even a single day during the basis year if one is resident in the year after and the three years before that basis year. [Section 7 (1) (d).]

Diagram VII—5: Individual resident in basis year without being present in Malaysia



Result: Resident in basis year 1971.

The "residence" in basis years 1968, 1969, 1970 and 1972, may be under any provision of the Act.

(ii) Business run by a Company or Body of Persons—Section 8 (1) (b)

Any one of these is resident in a basis year in Malaysia if at any time during that basis year management and control of the business is exercised in Malaysia, e.g. (1) *X* Co. runs a business of hauling goods to and from Malaysia and Singapore. It has an office in Kuala Lumpur, which collects and delivers goods for the trucks but no other management or control is exercised in Malaysia. *X* company is *not* resident. E.g. (2) *Y* Co. has two businesses one in Singapore and one in Kuala Lumpur. *Y* Co. is incorporated in Singapore but the directors who control and manage the Kuala Lumpur business have their meetings only in Singapore. *Y* Co. is not resident.

As a general proposition we can say that control and management of a corporation is normally exercised at the place where the directors hold their meetings.

(iii) Any other Company or Body of Persons (i.e. not having a business)—Section 8 (1) (c)

Any such company or body of persons is resident if its management and control are exercised in Malaysia by its directors or other controlling person.

(iv) Hindu Joint Family—Section 8 (1) (a)

A "Hindu joint family" is not included in "body of persons" in (ii) and (iii) above, (but it is so in the definition in Chapter I *q.v.*) Such a unit is resident in a basis year if its *Karta* is resident for that basis year.

Note: Company once established as resident is presumed to continue to be so.

Where it is established that a company or body of persons have by agreement with the D.G. been treated as resident for the basis year for any year of assessment it shall be presumed until the contrary is proved that it is resident for every subsequent year of assessment. [Section 8 (2).]

(v) Ordinary Residence—Section 9

With the two exceptions given below every person *resident* for a basis year (in any of the ways outlined above) is also *ordinarily resident* for that basis year e.g. a company, individual, or a body of persons (this is the definition of "person") each resident for basis year 1970 is also ordinarily resident unless it also falls under section 10.

The exceptions are firstly that an individual who is resident under section 7, but who also falls under any provision of section 10, (which makes him "not ordinarily resident"—see below) is to be considered as "resident but not ordinarily resident". Secondly where the *Karta* of a Hindu joint family falls into a similar category such unit is also "resident but not ordinarily resident". Before we discuss section 10, we should mention that the main tax effect of this is that an individual or a Hindu Joint Family

ordinarily resident is chargeable to tax on world income but where they are not ordinarily resident (or are non resident) they are chargeable to tax only on their income which is derived in Malaysia.

10. INDIVIDUALS NOT ORDINARILY RESIDENT (N.O.R.)—SECTION 10

Note: Since individuals ordinarily resident are chargeable to tax on their income on a world-wide basis, individuals who may wish to come to Malaysia on a short-term basis, may well be discouraged by this. Hence the Act provides that although such individuals may be resident under section 7 (1) (a), (b) and (d) (but not 7 (1) (c)), if they are in fact "short-term residents" who do not intend to make their permanent homes in Malaysia, they will be termed "resident but not ordinarily resident", with the effect that their income derived from outside Malaysia is not affected by the Act. Once again the question of intention is decided by a series of tests laid down in the Act as follows:

(i) Definition of "Short Term Resident"

Any individual, resident in the basis year except an individual who is resident under section 7 (1) (c) (described in paragraph 9 (i) (c) (i) & (ii) and illustrated in Diagrams VII—4 above) who was not resident for any of the basis years for the five immediately preceding years of assessment is termed a "short-term resident". This means that a person who has been in Malaysia, off and on, for at least 30 days in four out of five years cannot qualify, for he falls under section 7(1) (c) and such residents are excluded from being considered as "short term residents".

For an example which does qualify we shall take Mr. Kana who is resident because say he was in Malaysia for at least 182 days in the basis year 1970 (it could also be by any of the other ways except section 7 (1) (c) (i) & (ii)). If additionally Mr. Kana was not resident for the five years before 1970 i.e. in 1969, 1968, 1967, 1966 and 1965, he is a "short-term resident". The Act refers in our example to year of assessment 1971 as the "first year" and to 1972, 1973, 1974, 1975 and 1976 as the "second, third, fourth, fifth and sixth year" respectively. We will follow this through using the data from the example above. [The reader is reminded that the "basis year" is the year which precedes the "year of assessment".]

(ii) The "First Year" and the "Second Year"—Section 10(2)

Mr. Kana coming under the definition of "short term resident" is by virtue of section 10(2) treated as:

- (a) N.O.R. in the first year; and
- (b) if he is resident in the second year, as N.O.R. in the second year.

Assuming that he has an income of \$100,000 p.a. from a tax haven, he does not have to worry about paying tax on this in Malaysia—yet.

(iii) The "Third Year"—Section 10(3)—First Way

One way to gain N.O.R. status in the "third year" i.e. basis year 1972, for Mr. Kana is to either satisfy the D.G. during 1972 that he is not likely to be resident in both the "fourth year" and the "fifth year", or that he will not be resident in the "fourth year" (otherwise than by section 7(1) (b)—explained in Diagram VII above) and, that he will not be resident in the "fifth year". To summarize in tabular form:

Condition 1	+ Condition 2A	Result
"Short Term Resident" Resident in "third year" satisfies D.G. in that year	that he is not likely to be resident in "fourth year" and "fifth year"	N.O.R. in "third year"

Condition 1	+ Condition 2B	Result
(as above)	that he is not likely to be resident in "fourth year" (otherwise than by section 7(1) (b) and not resident in "fifth year"	N.O.R. in "third year"

Note 1: Condition 2B is actually a "breach" of 2A. Although Section 10(3) only lays down condition 2B, we have put in 2A to illustrate the point that non-residence i.e. 2A also satisfies the second condition 2B. This is also true in the cases considered below.

Note 2: If Mr. Kana had stayed in Malaysia for only 29 days in 1972, he would not be a resident at all and he, not satisfying condition 1 above would not come under section 10(3). His tax haven income would still be safe however as non-residents are taxed on only their Malaysian income.

If Mr. Kana does at first gain N.O.R. status for 1972 but then breaches condition 2B in any way, his position will be as if section 10(3) had never had any effect at all i.e. he would lose his N.O.R. status for 1972, unless he gains it as explained in the next subparagraph.

(iv) The "Third Year"—Section 10(4)—Second Way

Another way to gain N.O.R. status in the "third year" (and also for the "fourth year"—see below) is for Mr. Kana to satisfy the D.G. that he is not likely to be resident (except perhaps under 7(1) (b)) in the "fifth year" and not likely to be resident under any provision whatever in the "sixth year". It should be noted that under section 10(4) Mr. Kana does not have to satisfy the D.G. about non residence in the "fourth year", for in fact the section assumes that he *will* be resident in the fourth year for N.O.R. status is only applicable to residents. The examples given further below will help to clarify.

Subsequent breach of any condition will revert Mr. Kana to a position as if section 10(4) had never had any effect at all.

(v) The "Fourth Year"—Section 10(5)

Note: At this point it should be stated that once an individual has qualified under the definition of "short term resident" he is treated as such for the purposes of section 10 throughout. Assuming Mr. Kana has been a "short term resident" who was resident for 1970, 1971, 1972, and 1973, we cannot say in 1973 that he is not a short term resident as he does not come under the definition in 1973. The fact is that by first arriving in 1970 without having been in Malaysia in the five preceding years Mr. Kana qualifies as a short term resident in 1973.

If Mr. Kana is resident in the "fourth year" (1973) and he can satisfy the D.G. that he is not likely to be resident (except perhaps under section 7(1) (b)) in the "fifth year", and not likely to be resident under any provision whatever in the "sixth year" (this is identical to sub-paragraph (iv) above) he will be considered as N.O.R. for that "fourth year".

Note: If Mr. Kana had gained during the "third year" N.O.R. status for the "third year" and for the "fourth year" under the previous section (sub-paragraph (iv) above), he would not have to satisfy the D.G. again under this section. However if he had qualified for N.O.R. status only for the "third year" because he so qualified under section 10(3) (sub-paragraph (iii) above) then he would have to give the assurance under section 10(5). Once again breach of any condition would have the effect of section 10(5) never having had any effect.

(vi) Individual not Resident for Three Preceding Basis Years—Section 10 (6)

An individual who is resident for the basis year for any particular year of assessment (otherwise than by section 7 (1) (c) (at least 30 days in basis year and in three of four previous years etc.) but who was not resident for the basis years for the three immediately preceding years of assessment and who is also not a short term resident to whom section 10 (2) applies, shall be treated as not ordinarily resident for the basis year for that year of assessment.

Example

Mr. X stays at least 182 days in 1970 (or for a shorter period which is part of a qualifying period of 182 days, or deemed to so qualify at the D.G.'s discretion). He is hence resident for year of assessment 1971. If he was not resident in basis year 1969, 1968, 1967, and does not qualify for exception as a short term resident under section 7 (2) (perhaps because he was resident in basis year 1966, the reader should recall that a short term resident must *not* have been resident for five years before arrival) then he shall be treated as not ordinarily resident in the basis year 1970. This category provides for persons who do not qualify as "short-term residents", for while section 10 (2), (3), (4) & (5) all use the phrase "short term resident" this subsection (6) refers only to "an individual".

**(vii) Resident Individual Leaving and not likely to be Resident for Five Following Years—
Section 10 (7)**

Where any individual who is being treated as an ordinarily resident person for a basis year satisfies the D.G. that he is not likely to be resident for the next five basis years, he shall be treated as not ordinarily resident for that basis year.

But if subsequently he in fact is resident in any of the five basis years he will be treated as if this subsection had never had any effect in the basis year in which he leaves. Thus if say in basis year 1976 Mr. Kana is being treated as ordinarily resident, but he satisfies the D.G. that he is migrating to Canada and does not intend to be resident till 1982 then in the year he leaves (i.e. basis year 1976) his income of \$100,000 from the tax haven will not be taxed. But if he should turn up as a resident in any basis year between 1977 to 1981, then he may be retrospectively taxed for basis year 1976 on his income from outside Malaysia.

11. SUMMARY OF INDIVIDUALS NOT ORDINARILY RESIDENT

Individuals who do not intend to stay permanently are considered as resident but not ordinarily resident. The effect of this is that their income from outside Malaysia is not taxed here. Firstly we have considered people who not having been resident for 5 preceding years, arrive for a "short term residence". Since intentions cast no shadow that can be easily measured, residence by such "short term residents" over longer periods than one or two years together with a process by which the D.G. is to be satisfied, as to the likelihood of residence in later years, has been enacted. The process ensures that an individual who changes his mind e.g. by staying a further year may still be considered as not ordinarily resident by a different subsection but this can go on not longer than four full basis year and 29 days in the "fifth year" (see below and the exercises for examples). An individual who was not resident for only three preceding years is not a "short-term resident", but in his year of arrival he is treated as not ordinarily resident. Lastly any individual in the year of departure can be treated as not ordinarily resident if he can satisfy the D.G. that he is not likely to be resident for the following five years.

We have now established that in order to be chargeable to tax an item must firstly be INCOME and secondly it must be the income either of an ordinarily resident person no matter where derived, or income of any person derived in Malaysia. We shall now discuss the classes of income which are chargeable to tax and the law applicable to each class of income.

12. INCOME CLASSES

Before, it was necessary that income fall into a statutory class in order to be chargeable to tax but the inclusion of a "catch-all" class ((f) below) has removed this condition. The Act sets out the following classes:—

"4. Subject to this Act, the income upon which tax is chargeable under this Act is income in respect of—

- (a) gains or profits from a business, for whatever period of time carried on;
- (b) gains or profits from an employment;
- (c) dividends, interest or discounts;
- (d) rents, royalties or premiums;
- (e) pensions, annuities or other periodical payments not falling under any of the foregoing paragraphs;
- (f) gains or profits not falling under any of the foregoing paragraphs."

13. EXAMPLES

Preliminary Note

The subject of residence appears to be very complex, but the reader who follows through the attached examples should have little difficulty. The reader is reminded again that unless the context indicates otherwise we use "basis year" to mean "basis year for year of assessment". This is done in the reader's interest for we have found from experience that a constant flitting back and forth between basis year and year of assessment in textual exposition imposes a severe strain, which is an unnecessary burden in this case—for the chargeability of a person in the year of assessment depends on his residence status in the basis year, and a discussion confined to the basis years alone is hence completely relevant, and all the reader has to bear in mind is the relationship between basis year and year of assessment—i.e. that the basis year is the calendar year preceding the year of assessment. It is also worth repeating that the question of O.R. or N.O.R. only arises if the person is firstly resident.

COMPARATIVE EXAMPLES ON RESIDENCE

Basic Year	E.G. I			E.G. II			E.G. III			E.G. IV			E.G. V			E.G. VI									
	Days in Malaysia	Applicable Sections of the Act		Status	Days in Malaysia	Applicable Sections of the Act		Status	Days in Malaysia	Applicable Sections of the Act		Status	Days in Malaysia	Applicable Sections of the Act		Status	Days in Malaysia	Applicable Sections of the Act		Status					
		Res	O.R./N.O.R.			Res	O.R./N.O.R.			Res	O.R./N.O.R.			Res	O.R./N.O.R.			Res	O.R./N.O.R.		Res	O.R./N.O.R.			
1965	NIL			N.R.	NIL			N.R.	NIL			NIL	—	—	N.R.	NIL			365	7(1)(a)		O.R.			
1966	NIL			N.R.	NIL			N.R.	NIL			NIL	—	—	N.R.	NIL			365	7(1)(a)		O.R.			
1967	NIL			N.R.	NIL			N.R.	181			365	7(1)(a)	—	F.N. 1, O.R.	NIL			365	7(1)(a)		O.R.			
1968	NIL			N.R.	NIL			N.R.	30			NIL	—	—	N.R.	NIL			365	7(1)(a)		O.R.			
1969	NIL			N.R.	NIL			N.R.	NIL			NIL	—	—	N.R.	NIL			365	7(1)(a)		O.R.			
"7th year" 1970	365	7(1)(a)	10(1) 10(2)	N.O.R.	365	7(1)(a)	10(1) 10(2)	N.O.R.	30	F.N. 1, 7(1)(b)	10(1) 10(2)	N.O.R.	NIL	—	—	N.R.	365	7(1)(a)	10(1) 10(2)	N.O.R.	365	7(1)(a)	10(7)	N.O.R.	
"2nd year" 1971	365	7(1)(a)	10(2)	N.O.R.	365	7(1)(a)	10(2)	N.O.R.	30	7(1)(c)	10(2)	N.O.R.	185	7(1)(a)	10(6)	N.O.R.	187	7(1)(a)	10(2)	N.O.R.	NIL	—	—	N.R.	
"3rd year" 1972	366	7(1)(a)	10(4)	F.N. 1, N.O.R.	366	7(1)(a)	10(4)	F.N. 1, O.R.	30	7(1)(c)	10(3) or 10(4)	N.O.R.	365	7(1)(a)	—	O.R.	NIL	F.N. 1, 7(1)(b)	10(4)	N.O.R.	NIL	—	—	N.R.	
"4th year" 1973	365	7(1)(a)	10(4)	N.O.R.	365	7(1)(a)	10(4)	F.N. 2, O.R.	30	7(1)(c)	10(5)	N.O.R.	365	7(1)(a)	10(7)	N.O.R.	365	7(1)(a)	10(4)	N.O.R.	30	—	—	N.R.	
"5th year" 1974	29	7(1)(b)	10(7)	N.O.R.	30	7(1)(c)	10(4) proviso	O.R.	29	7(1)(b)	10(7)	F.N. 2, O.R.	NIL	—	—	N.R.	29	—	—	F.N. 2, N.R.	30	—	—	N.R.	
"6th year" 1975	<30			N.R.	<30	7(1)(d)		O.R.	10	—	—	N.R.	NIL	—	—	N.R.	NIL				N.R.	181	—	—	N.R.
1976	<30			N.R.	<182	7(1)(c)		O.R.	<30	—	—	N.R.	NIL	—	—	N.R.	NIL				N.R.	29	—	—	N.R.
1977	<30			N.R.	<30	7(1)(d)		O.R.	<182	—	—	N.R.	<182	—	—	N.R.	NIL				N.R.	29	—	—	N.R.
1978	<182			N.R.	<182	7(1)(c)		O.R.	182	7(1)(a)	10(7) proviso, F.N. 2	N.O.R.	NIL	—	—	N.R.	NIL				N.R.	181	—	—	N.R.
1979	NIL			N.R.	NIL	F.N. 3		F.N. 3																	

Notes

E.G. I
F.N. 1. In "third year" he satisfies D.G. that:
(a) he is not likely to be resident in "fifth year" except under 7(1)(b); and
(b) not likely to be resident in "sixth year"

E.G. II
F.N. 1, & 2. The N.O.R. status for 1972 & 1973 is retrospectively lost because he overstayed in 1974, by only one day c.f. E.U.1.
F.N. 3. Would depend on 1980 status.

E.G. III
F.N. 1. Assumed that the D.G. has exercised his discretion under section 7(1)(b)(i). Otherwise he would not be a resident for a short term resident.
F.N. 2. In 1979, he contravenes section 10(7) giving effect to the proviso in that section, i.e. he retrospectively loses his N.O.R. status in 1974 but he is N.O.R. for 1979 by 10(6).
N.B. If he stayed 30 days in 1974, he would be resident under 7(1)(c), and would then lose his N.O.R. status for 1972 & 1973 because he would have contravened 10(4) and 10(5) giving effect to the proviso in these subsections.

E.G. IV
F.N. 1. If he had obtained N.O.R. status under 10(7) he would have lost it retrospectively in 1971 being resident in contravention of 10(7)

E.G. V
F.N. 1. The assumption is that the D.G. has exercised his discretion and treated this as a temporary absence.
F.N. 2. The assumption is that the D.G. has not exercised his discretion under section 7(1)(b). The effect is that not being a resident he cannot claim N.O.R. status.
This does not affect his tax have income, but his Malaysian income is taxed at non-resident rates.

ALLOWABLE DEDUCTIONS—GENERAL AND BUSINESS SOURCE

Preliminary Note

Because this and the two following chapters are crucial to the subject of Income Tax they are of vital concern to practitioner and student alike, so we give an overview at this point.

We begin by warning the reader (and ourselves) about the low applicability of U.K. case-law, specially when it relates to deduction from an employment source and explain why this is so. We then give a definition of "Allowable Deductions"; "Income"; and "Gains and Profits". This is followed by an exploration of section 33 (1) which is the general authority for allowable deductions. The case law we use in this exploration is mainly on business-source deductions because this is more closely applicable than the case law on employment-source deductions for reasons explained at the beginning of the chapter. We give extracts of the statutory provisions on deductions from other countries at the end of this chapter for comparison.

The two chapters following this one are concerned with allowable deductions from non-business sources, and specific statutory provisions allowing or prohibiting certain deductions. A certain degree of repetition of important distinctions is a built-in feature to stress and review these distinctions.

1. PITFALLS IN APPLYING U.K. AND AUSTRALIAN CASE LAW

We have set out at the end of this chapter extracts from the statutes of the United Kingdom, New Zealand, Australia, the United States of America and the Republic of Singapore for the purpose of comparing them with section 33 (1) of the Act which is given below:

"Chapter 4—Adjusted income and adjusted loss

33 (1) Subject to this Act, the adjusted income of a person from a source for the basis period for a year of assessment shall be an amount ascertained by deducting from the gross income of that person from that source for that period all outgoings and expenses wholly and exclusively incurred during that period by that person in the production of the gross income from that source, including . . ."

(i) Some Differences

The rules for deduction in the United Kingdom for example used to and in some cases still do, differ from the Act on the following points:

- (a) Different rules apply to different sources e.g. Schedule D, Case I & II and Schedule E.
- (b) The rules for deductions from a trade source are worded in the negative.
- (c) The rule for deductions from any employment source (Ninth Schedule) are most restrictive with the word "necessarily" used twice and "necessary" once.
- (d) The Ninth Schedule used the example of a horse as an example of a necessary travelling expense.

In the U.K. the rules for deductions vary depending on the source of income but in Malaysia the one rule (given above) applies generally to all the different sources (except a section 11 source—a source arising from the occupation of premises—for which the deductions are set out in section 37), and some differences in actual tax payable result, from other specific provisions in the Act e.g. the carrying forward of losses is allowed only when incurred from a trade source. The above differences pose serious obstacles to the application of the decided U.K. cases to points at dispute in Malaysia. No one can deny that it is the borderline case in U.K. that ends up in court and is appealed and reappealed until it reaches the highest tribunal available. Here erudite legal minds apply themselves to deciding on which side of the line a particular point in a case falls. The debate is conducted and the decisions are made on or near the outer limits of these boundaries. To our mind the logical effect of a different wording in one statute therefore, is, that the decisions (as such), based on another statute with different wording, become extremely poor guides to interpretation. Yet an extremely careful and intensive study of the reasoning of judges, as embodied in their delivered judgements, may give some guidance to us. The quality of guidance of a particular case will depend primarily on the near identity or otherwise of the two statutes at that point and subsequently the decision on the facts is relevant only if the above primary condition is fulfilled and the facts are similar e.g. U.K. case law on allowable deductions for business sources will thus be more persuasive than case law on the allowable deductions from employment sources.

(ii) Warning to Avoid Facile Generalisations

We have set the above down so that the reader will avoid making facile generalisations from cases and specially so from cases on allowable deductions from an employment source. We could also remind the reader that "Similar is not SAME". Conditions of training, and the educational background of the person, may unconsciously bias

a person in his judgement, and the pressure of work may often prevent the exercise of the critical faculty in spite of high professional standards. Last of all we have set these points down as a caution to ourselves not to take the easy way out.

2. CAPITAL OR REVENUE

We have discussed the difference between capital and revenue in Chapter VI. There it was necessary to distinguish these two because only revenue items are considered as sources for the purposes of the Act. This being so the deductions from these sources must also mainly be of a revenue nature in order to ascertain income for tax purposes. The case law is far more voluminous on deductions than on any other point so we shall state a few definitions before we proceed.

(i) Three Definitions

- (a) **Allowable Deductions** are those deductions which are ruled as allowable by Part III, Chapter IV of the Act and are not statutorily prohibited. These may be variously called: "outgoings, expenses, disbursements, costs, losses, expenditures, gratuities, indemnities, contributions", etc.
- (b) **Source of Income and Income.** When we discuss section 4 we sometimes refer to "Income From Employment" or "Income From Rents" etc. Strictly speaking these are sources from which allowable deductions can be made to ascertain "The Income". Thus gross rent received or receivable is *not* income in the above strict sense; it is a source to which the Act refers as "gross income". Only after you have deducted the cost of repairs, the interest paid on money borrowed to buy the house, the assessment paid etc. do you have "The Income" which is taxable and the Act refers to this as chargeable income. We can now answer the philosophical question we asked before in a non-philosophical way.

Question: "What is Income?"

Answer: "From the sources (gross income) as set out in section 4 deduct the items allowed by Part III, Chapter IV of the Act and what is left is Income". [See Act section 5 (1) for the statutory formula.]

Logically Income as defined above may be a minus quantity. What to do with this we will explain in subsequent chapters. For now we outline the problem of defining allowable deductions in Malaysia.

- (c) **Gains and Profits.** If you look closely at section 4 you find the phrase "gains and profits" used for "Business", "Employment" and the catch-all provision in paragraphs 4 (a), (b) & (f) respectively. The question is "How does one arrive at this "gain and profit?" We know that accountants prepare profit and loss accounts according to accountancy principles. Although similar principles are applicable in the ascertainment of income the fact is that the results

almost always differ. We give examples of the conversion required in later chapters but here we will outline the legal concepts involved in arriving at a "gain or profit" for tax purposes.

(ii) Special Commissioners are Judge of Fact

The Act lays down what must be deducted and what must not be deducted but where we have a controversial item it is a matter of fact to be decided whether this item can or cannot be allowed. The Special Commissioners have the authority to decide on the facts of every disputed case, and the High Court will generally not upset its decision on fact but where it is a mixed question it may have a further say. Admittedly it is sometimes hard to say where the fact begins and the law ends.

3. EXPLORATION OF SECTION 33 (1)

We repeat that we are here usually considering items which on the circumstances of the case are neither allowed nor prohibited by the Act. The tests to be applied are therefore based on an interpretation of section 33 (1) which we intend to discuss in three parts:—

- (i) "... all outgoing and expenses . . . incurred".
- (ii) "... wholly and exclusively . . ."
- (iii) "... in the production of gross income from that source".

4. ALL OUTGOINGS AND EXPENSES . . . INCURRED

(i) What is an Outgoing?

Where the item is not covered specifically by the Act the ordinary practices of merchants will have persuasive force:

"... I know of no standard for making the vital, but often delicate, distinction between a revenue charge appropriate to form a deduction from trading receipts and a capital which ought not to enter into the ascertainment of trading profits, except the standard set up by the prudence and experience of merchants . . ." (Lord President (Clyde) in *Roebank Printing Co. Ltd. v. I.R. Comrs.* 13 T.C. 864).

The circulating or fixed capital distinction mentioned before is also a useful test here, but it must be related to the circumstances of the case.

(ii) Incurred

The question of when an item is incurred is often of great importance. The time of payment is of minor relevance for it includes:—

"Outgoings to which the taxpayer is definitely committed in the year of income although there has been no actual disbursement". (*F.C. of T. v. James Flood Pty. Limited* 88 C.L.R. 492; 5 A.I.T.R. 597).

A loss impending, threatened or expected is usually included by accountants as a provision if they know the amount and it is more or less certain; or as a contingent liability if the amount is unknown and the liability uncertain, but such an item will not generally be allowed as a deduction:

When a dispute was submitted to arbitration in an earlier year and the award given in a later year—held: the item was an outgoing of the later period. (*Stockvis v. F.C. of T.* 1930).

In these borderline areas, at first there may be uncertainty about the existence of the liability as well as about the amount. Only if the first is definitely settled and the second known with some reasonable degree of certainty, can the item be said to be incurred.

(iii) Period of Incurring Expense and Period of Income

In Malaysia the *source* of income becomes of vital importance when heavy expense (of a revenue nature) is incurred earlier and the income is produced later. Where a business source (4 (a)) already in operation incurs such an expense in a certain period, such expense being more than the incomings in that period, a loss (negative income) results. However, the person who is chargeable to tax can offset this loss *in that year only* against all other sources he may have. Even if there is still a business loss, he can carry it forward to offset against his share of profits only from a *business* source. This carrying forward or even offsetting against other sources in the same period cannot be done where outgoings and expenses on a *non-business source* exceed the incomings.

5. WHOLLY AND EXCLUSIVELY

This does not mean that if an expense is incurred say partly for a private purpose and partly for a business purpose, it cannot be allowed.

For where it is possible to distinguish a part of the expense that can be said to be wholly and exclusively for an income producing purpose, then that is an allowable deduction e.g. a doctor uses his car for domestic as well as professional purposes. If his chauffeur keeps a log of the mileage covered on the two purposes and such a log is acceptable to the D.G., being accurately and reasonably kept in his opinion, then that portion of the expenses pertaining to the professional purpose is an allowable deduction. That portion of the capital cost of the car may also be allowed as a capital allowance.

The difficulty is born out of the high uncertainty factor in certain cases. As we have said, initially the D.G., and finally the Special Commissioners are the judges of fact and where the records kept enable the fact to be ascertained with a reasonable degree of reliability a portion will be allowed.

The corollary that follows of course is that in some cases where it is not possible to separate the allowable part, then the expense is not allowable, because almost by definition, the item is not wholly and exclusively incurred in the production of income. This in practice boils down to the quantum of the proportions. Where such "dual-purpose" expenditure has only a small non-allowable component it will be allowed.

6. IN THE PRODUCTION OF INCOME

It stands to reason that even where an expense satisfies every criterion required by law to be classed as an "allowable deduction" *except* that it happens to be not in the production of income, it fails to be allowable.

(i) Capital or Revenue

Thus one of the distinctions between capital and revenue is that: that part of the expenditure devoted to creating a source of income is capital and that part devoted to further operate the source in the production of income is revenue. The latter is an allowable deduction. We could put this in another way and say that expenditure incurred in acquiring, expanding and improving a source is capital expenditure and expenditure incurred in operating, maintaining and preserving the source is revenue expenditure.

(ii) Examples

- (a) A new hotel is opening in Kuala Lumpur and a big free dinner is given *before* the doors are opened to the public. The expenses for this big dinner are not allowable. If the dinner is given after the doors are opened they will be allowable as a part of the advertising costs.
- (b) Land etc. is purchased, levelled, drained etc. and rubber trees are planted on it. Further expenses are incurred to bring the estate to stage where rubber can be sold. These further expenses are allowable as a special case (*Vallambrosa Rubber Co. Ltd. v. Farmer (Surveyor of Taxes)*, (5 T.C. 529).

(iii) Initial Repairs are Capital?

On the acquisition of a second-hand asset e.g. a ship, the initial repairs required to put it into a reasonable state were not allowed as deductions. ("*Law Shipping Co. Ltd. v. I.R. Comrs.*" (1923) 12 T.C. 621).

After renting new shops, additional money spent to repair and decorate them was not allowed. (The case of "*S. Limited*" (Singapore Board of Review VII (1) 1953).

Expenditure representing an accumulation of repairs on initial occupation as tenant was held to be capital expenditure. (*Jackson v. Laskers Home Furnishers* (1956) 37 T.C. 69).

Expenditure to repair damage and neglect during the Japanese Occupation was allowed. The fact of the Occupation as an abnormal circumstance may have been relevant. ("*U Limited S.B. IV* (1951)).

However the recent decision in *Odeon Associated Theatres Ltd. v. Jones The Times November 13th 1970*. (1970), T.R. 299, that expenditure correctly chargeable to revenue in accordance with sound commercial accounting principles was also deductible for tax purposes, modifies the "Law Shipping" principle and initial repairs of a similar nature should now be allowed.

(iv) Repair or Improvement

A great number of cases are argued on the difference between repair and improvement. Generally, expenditure to restore to the original state is a repair, and to a state better than the original is an improvement to the extent that the new state is better than the original state. Yet as always, the surrounding circumstances affect the decision.

Example:

- (a) Where a new chimney was built but it was a small part of the entire factory it was allowed. (*Jones & Co., Ltd. v. I.R. Comrs.* (32 T.C. 513). But where it was a large part of another firm it, being considered almost an entirety in itself, was not allowed. (*O' Grady v. Bullcroft Main Collieries Ltd.* (1932) 17 T.C. 93).
- (b) The replacement of a watergate on a rubber estate was considered as a part of a larger entirety—the whole irrigation system and allowed. (*C.I.T. Federation v. Straits Rubber Co. Ltd.* [(1961) M.L.J. 191]).
- (c) Where instead of dredging a channel a new wharf was built making the dredging unnecessary it was not allowed. (*Cunsworth v. Vickers Limited* (6 T.C. 671), but the clearing of wrecks sunk during the war to make a harbour safe was allowed. (*Whelan v. Dover Harbour Board*, 18 T.C. 555 C.A.).

(v) Intangible Advantage

Where a firm incurs an expense and obtains some intangible advantage it is necessary to distinguish whether such advantage does in fact create a source of income or whether the expense is merely expenditure in the production of income from an existing source. In the former case it is capital and not allowable; in the latter case it is an allowable deduction.

Examples:

- (a) Where the new owner of a business in accordance with the terms of the take-over arrangement, paid a lump-sum to an employee of the old firm, it was held to be capital. (*Royal Insurance Company v. Watson* 3. T.C. 500 H.L.).
- (b) But where an existing employee, in lieu of a pension he was already entitled to, was given an annuity purchased from an insurance Company for a lump-sum, this was allowed. (*General Reversionary and Investment Company Limited v. Hancock*, 7 T.C. 358).

The former was held to be a part of the cost of acquiring a new business while the latter was the payment of an allowable deduction (the pension) in a lump-sum commuted form, bringing no asset into existence and not affecting any of the firm's capital.

(vi) **Insurance Payments**

Insurance payments by a firm that create a right which definitely accrues only to the employee, or his heirs on certain definite eventualities, are generally allowable, in so far as they do not bring into existence any tangible or ascertainable asset which would brand them as capital of the firm.

Examples:

(a) The Company paid out a large sum to purchase annuities for its employees in lieu of pensions but these were payable to the company first, which would then pay them to the employee. The employee had no absolute right to the pension, which could be withdrawn under certain circumstances. Held: the payment was not an allowable deduction. (*Morgan Crucible Co. Ltd. v. I.R. Comrs.* 17 T.C. 311). This is different from the previous example (*Hancock*) in that the transaction brought about an asset, available to the company in certain circumstances.

(b) (i) Where premiums were paid on a director's life, with the proceeds payable to the firm it was held not allowable.

(ii) As in (a) but proceeds payable absolutely to the director or employee—allowable.

(*Atherton (Inspector of Taxes) v. British Insulated and Helsby Cables Ltd.* 10 T.C. 155) was distinguished from the "*Hancock*" case by deciding that an asset had been created i.e. an enduring benefit of a contented staff. The facts in brief: The firm paid a large sum calculated accurately into a trust fund for the absolute benefit of employees. There were two essential differences from "*Hancock*".

(i) The Company paid the sum voluntarily and not out of necessity.

(ii) An enduring asset (contented employees) was brought into existence by the payment.

(vii) **Preservation of a Source**

Sums expended either in a lump-sum or otherwise in the preservation of a source of income were held allowable.

Examples:

(a) Where a relatively large sum was paid to retire an unsatisfactory director, without injuring the firm's goodwill by using an alternative available cheaper method, it was held that this was allowable. (*Mitchell (Inspector of Taxes) v. Noble Limited* (1927) 11 T.C. 372).

- (b) The Company paid a large sum to their agents in Persia, in order to do the operations themselves. The Commissioners decided it was capital but the Courts ruled that it was an allowable expense. The argument that they had bought out their agents to create a more viable company was rejected on the grounds that the agent is only an extension of the principal, the transaction being an internal arrangement for better functioning. (*Anglo-Persian Oil Co. Ltd. v. Dale* (1934) 16 T.C. 253).
- (c) Where the amount was paid in instalments to close down a competitor it was held to be capital and hence not allowable. *C.f.* "*Anglo-Persian*" and (*United Steel Co's, Ltd. v. Cullington (Inspector of Taxes)* (1940) 23 T.C. 91).
- (d) The expenditure of a sum of money to defend an existing good title to income earning property was held to be an allowable deduction. (*Southern (Inspector of Taxes) v. Borax Consolidated, Ltd.* (1940) 23 T.C. 597). See also House of Lords case of *Morgan (Inspector of Taxes) v. Tait and Lyle Ltd.* (1955) A.C. 21.
- (e) But money spent in the prevention of competition by retiring directors by contractually binding them was held to be capital bringing into existence a new right. (*Associated Portland Cement Manufacturers Limited v. Kerr (Inspector of Taxes)* (1945) 27 T.C. 103).

(viii) Loans Lost

Sums of money loaned out and lost where the lending out of such sums though incidental is held to be *in the normal course of business* are a allowable deductions, (except in the case of a money-lending business where bad debts are considered allowable only as losses of the trade merchandise i.e. loss of circulating capital—hence of a revenue nature).

Examples:

- (a) Money lent out to many tenants of a brewer's public-houses (bars) when lost was held to be allowable. The lending out of the money was found to be an example of a loaning out of "circulating capital" which when lost is allowable. (*Reid's Brewery Co. Ltd. v. Male (Surveyor of Taxes)* (1891) 3 T.C. 279).
- (b) But money paid in advance to secure raw materials, when lost, was not allowed in the following two cases:
 (*English Crown Spelter Co. Ltd. v. Baker (Surveyor of Taxes)* (5 T.C. 327).
 (*Marsden and Sons Ltd. v. I.R. Comrs.* 12 T.C. 217).

(ix) Non-Trading Expenses

Where expenses are incurred *not in the capacity of a trader* they are not allowable as they are not wholly and exclusively incurred in the production of income for the trade.

Examples.

- (i) The Company broke the law and paid a penalty. Held—breaking the law is not for the purpose of trade and hence the penalty was not allowable. (*C.I.T. v. Alexander and Company Limited*) (12 T.C. 232).
- (ii) A businessman fined for speeding even where he was driving a client in a hurry to the airport will probably not have the fine allowed as a deduction. It is no part of his business to break the law. A fine is not a trading transaction and even the legal expenses concerned would not be allowable.
- (iii) Where no law is broken and a sum of money is expended in the normal course of business, say to prevent a legal dispute from going to court, the amount would be allowable.
- (iv) **Payments to Accountants** to prepare the accounts of a business are allowable but the fees of a tax consultant to ascertain tax liability, or to fight an appeal, are not allowable. (*Smith's Potato Estates Limited v. Bollard (Inspector of Taxes)*) (30 T.C. 267). A fine for a tax offence is of course not allowable.

Note: In practice limited companies are often allowed the tax consultant's fees in preparing tax returns, as a concession.

(x) Theft, Fraud, Robbery and War-Losses

We can pull together the strands of the general principles of allowable deductions by considering losses arising from theft, fraud, robbery and war.

Whether such a loss is allowable or not depends on:—

- (i) The essential nature of the thing lost—e.g. whether it represents fixed or circulating capital.
- (ii) The circumstances surrounding its loss—whether it was in the normal course of the operations resulting in an income.

The principle stated first is logically also the first one that needs to be considered for if loss is of a capital nature the matter is settled and there is no need to go any further:—

Example:

Where enemy action destroyed the spare parts of an air-transport firm it was held that this was a capital loss. Kitto *J. inter-alia* distinguished this from money held by a bank which is stock-in-trade, and an appreciation of which is assessable income.

(*Guinea Airways Limited v. F. C. of T* (1950) 83, C.L.R. 584).

(*Punjab Co-operative Bank Limited Amritsar v. I.T.C. Lahore* (1940 A.C. 1055).

But the attendant circumstances are also important to decide if the loss was in the course of some operation normal to the trade.

Examples:

- (a) A bookmaker lost some money at a race course—held allowable (*C.T.B.R. 13 Case 12*).
- (b) Retail store employees robbed on way to bank—allowable. (*Charles Moore & Company (W.A.) Pty. Limited v. F. C. of T.* (1956), 6 A.I.T.R. 379).
- (c) One of the accountants employed to keep books by a partnership, persuaded taxpayer to sign a cheque leaving the figure blank to ascertain later for payroll tax. He filled in £301 payable to himself and disappeared with the money—not allowable as held to be a loss of capital. (*C.T.B.R. 4 (N.S.) Case 68*).
- (d) £8,835, was lost when a burglar stole bonds partly received from customers as payment of accounts and partly held to hand over to employers who had bought them through a payroll deduction plan—held: bonds not capital of taxpayer and hence allowable. (*Weidman Brothers Limited v. Minister of National Revenue.* (1950) 2, Can. Tax A.B.C. 223).

N.B. Where any amount of any allowable loss is recoverable under any insurance such amount lost can be allowed as a deduction, but the sum recoverable must be included as the gross income of the person (section 22 (2)).

A loss of trading stock, or undetected cash pilferage, is in most cases automatically "allowed", in the sense that in the first case closing stock will be at a lower figure reducing the profit or increasing the loss as the case may be, in the second case the lower figure for sales will have a like result.

Note: 1. The last word in section 33 (1).

"Including"—has been held (*cf. M.N.O. v. C.I.T.* [1961] M.L.J. 223) to extend the scope of section 33 (1). This means that even if an item is not allowed under section 33 (1), but it comes under any subsequent paragraph, then it is allowed. We cover this in Chapter IX.

2. The revision questions of this chapter are at the end of the next chapter.

EXTRACTS FROM COMPARATIVE PROVISIONS IN THE INCOME TAX LAW OF THE U.K., AUSTRALIA, CANADA, U.S.A. AND THE REPUBLIC OF SINGAPORE

New Zealand

Land and Income Tax Act, 1954 (Reprinted in 1970)

110. Except as expressly provided in this Act, no deduction shall be made in respect of any expenditure or loss of any kind for the purpose of calculating the assessable income of any taxpayer.
111. In calculating the assessable income of any tax payer any expenditure or loss to the extent to which it—
- (a) Is incurred in gaining or producing the assessable income for any income year; or
 - (b) Is necessarily incurred in carrying on a business for the purpose of gaining or producing the assessable income for any income year—
- May, except as otherwise provided in this Act, be deducted from the total income derived by the tax payer in the income year in which the expenditure is incurred.

(2) In calculating the assessable income of any person deriving assessable income from two or more sources, any expenditure or loss exclusively incurred in the production of assessable income for any income year may, except as otherwise provided in this Act, be deducted from the total income derived by the taxpayer for that year from all such sources as aforesaid."

Australia

Income Tax and Social Services Contribution Assessment Act 1936-1969

- "Section 51 (1) All losses and outgoings to the extent to which they are incurred in gaining or producing the assessable income, or are necessarily incurred in carrying on a business for the purpose of gaining or producing such income, shall be allowable deductions except to the extent to which they are losses or outgoings of capital, or of a capital, private or domestic nature, or are incurred in relation to the gaining or production of exempt income.
- (2) Expenditure incurred or deemed to have been incurred in the purchase of stock used by the taxpayer as trading stock shall be deemed not to be an outgoing of capital or of a capital nature".

This section 51 in 1936 replaced, section 23 (1) (a) of the Income Tax Assessment Act, 1922-34 which permitted a deduction of "all losses and outgoings . . . incurred in gaining or producing the assessable income", and section 25 (e) of the same Act prevented a deduction of "money not wholly and exclusively laid out or expended in the production of assessable income."

United States of America

Internal Revenue Code of 1954

Section 162—Trade or Business Expenses

- (a) In general: There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including:
- (1) a reasonable allowance for salaries or other compensation for personal services actually rendered;
 - (2) travelling expenses (including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances) while away from home in the pursuit of a trade or business; and
 - (3) rentals or other payments required to be made as a condition to the continued use or possession, for the purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

Section 165—Losses

- (a) General rule: There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.
- (c) Limitation on losses of individuals: In the case of an individual, the deduction under sub-section (a) shall be limited to:
- (i) losses incurred in a trade or business;
 - (ii) losses incurred in any transaction entered into for profit, though not connected with a trade or business; and
 - (iii) losses of property not connected with a trade or business, if such losses arise from fire, storm, shipwreck, or other casualty, or from theft.
- (d) Wagering losses: Losses from wagering transactions shall be allowed only to the extent of the gains from such transactions.
- (e) Theft losses: For purposes of sub-section (a) any loss arising from theft shall be treated as sustained during the taxable year in which the taxpayer discovers such loss.
- (f) Capital losses: Losses from sales or exchanges of capital asset shall be allowed only to the extent allowed in sections 1211 and 1212.

Section 262—Personal, living and family expenses

Except as otherwise expressly provided in this chapter, no deduction shall be allowed for personal, living, or family expenses.

Section 263—Capital Expenditures

(a) General rule: No deduction shall be allowed for:

- (1) Any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate . . .
- (2) Any amount expended in restoring property or in making good the exhaustion thereof for which an allowance is or has been made.

United Kingdom

Income and Corporation Taxes Act 1970, Section 130

"Section 130—General rules as to deductions not allowable:—

Subject to the provisions of the Tax Acts in computing the amount of the profits or gains to be charged under Case I or Case II of Schedule D, no sum shall be deducted in respect of:—

- (a) any disbursements or expenses, not being money wholly and exclusively laid out or expended for the purposes of the trade, profession or vocation;
- (b) any disbursements or expenses of maintenance of the parties, their families or establishments or any sums expended for any other domestic or private purposes distinct from the purposes of the trade, profession or vocation;
- (c) the rent of any dwelling house . . . except such part thereof as is used for the purposes of trade or profession . . . ;
- (d) any sum expended for repairs of premises occupied, or for the supply, repairs or alterations of any implements, utensils, or articles employed for the purposes of the trade, profession or vocation, beyond the sum actually expended for those purposes;
- (e) any loss not connected with or arising out of the trade, profession or vocation;
- (f) any capital withdrawn from, or any sum employed or intended to be employed as capital in, the trade profession or vocation. . . .
- (g) any capital employed in improvements of premises occupied for the purposes of the trade, profession or vocation . . . "

INCOME TAX ACT 1952

Ninth Schedule

Rules Applicable to Schedule E

7. If the holder of an office or employment of profit is necessarily obliged to incur and defray out of the emoluments thereof the expenses of travelling in the performance of the duties of the office or employment, or of keeping and maintaining a horse to enable him to perform the same, or otherwise to expend money wholly, exclusively and necessarily in the performance of the said duties, there may be deducted from the emoluments to be assessed the expenses so necessarily incurred and defrayed . . .

Republic of Singapore

Income Tax Act, (Part IV, Chapter 141) Section 14

- (1) For the purpose of ascertaining the income of any person for any period from any source chargeable with tax under this Act (in this Part referred to as "the income") there shall be deducted all outgoings and expenses wholly and exclusively incurred during that period by that person in the production of the income, including:—
 - (a) except as hereinafter provided, any sum payable by way of interest upon any money borrowed by that person where the Comptroller is satisfied that the interest was payable on capital employed in acquiring the income;
 - (b) rent payable by any person in respect of any land or building or part thereof occupied by him for the purpose of acquiring the income;
 - (c) any expenses incurred for repair of premises, plant, machinery or fixtures employed in acquiring the income or for the renewal, repair or alteration of any implement, utensil or article so employed:

Provided that no deduction shall be made for the cost of renewal of any plant, machinery or fixture, which is the subject of an allowance under section 19 of this Act; or for the cost of reconstruction or rebuilding of any premises, buildings, structures or works of a permanent nature;

- (d) bad debts incurred in any trade, business, profession or vocation, which have become bad during the period for which the income is being ascertained, and doubtful debts to the extent that they are respectively estimated, to the satisfaction of the Comptroller, to have become bad during that period, notwithstanding that those bad or doubtful debts were due and payable before the commencement of that period:

Provided that:

- (i) all sums recovered during that period on account of amounts previously written off or allowed in respect of bad or doubtful debts, other than debts incurred before the commencement of the basis period for the first year of assessment under this Act, shall for the purposes of this Act be treated as receipts of the trade, business, profession or vocation for that period;
 - (ii) the debts in respect of which a deduction is claimed were included as a trading receipt in the income of the year within which they were incurred;
 - (iii) no deduction shall be allowed in respect of any debt incurred before the commencement of the basis period for the first year of assessment under this Act;
- (e) any sum contributed by an employer to an approved pension or provident fund or society in respect of any of his employees engaged in activities relating to the production of the income of the employer, the contribution of which sum by the employer was obligatory by reason of any contract of employment or of any provision in the rules or constitution of the fund or society:

Provided that:

- (i) a deduction in respect of any such contribution by an employer in respect of an employee for any period shall not exceed fifteen per cent of the remuneration paid by the employer to the employee for that period; and in this proviso, the word "remuneration" means that part of an employee's emoluments by reference to which his employer's contributions are calculated;
 - (ii) where any such fund or society is first established and a special contribution is made thereto by the employer whereby persons in his employment whose employment commenced prior to the establishment of the fund or society may qualify for the benefits there under in respect of such prior employment, the Comptroller may, when approving the fund or society, authorise such deductions in respect of that special contribution as he thinks fit;
- (f) zakat, fitrah, or any religious dues, payment of which is made under any written law;
- (g) where the income is derived from the working of a mine or other source of mineral deposits of a wasting nature, such deductions in respect of capital expenditure as may be prescribed in rules made under section 7.

(2) Notwithstanding the provisions of sub-section (1) payments made by way of salary, wages or similar emoluments, to an employee who is the husband, wife or child of an employer, shall be allowed as deductions only to the extent to which, in the opinion of the Comptroller, they are reasonable in amount having regard to the services performed by that employee.

IMPORTANT NOTE: Persons wishing to obtain information on the law of other countries should consult the most up-to-date version available. These extracts are included by us only to illustrate the points made in the text. However the extracts from the laws of the Republic of Singapore are the current legislation as at Nov. 1972.

ALLOWABLE DEDUCTIONS—EMPLOYMENT AND OTHER NON-BUSINESS SOURCES

Preliminary Note

The application of Section 33 (1) to the other sources of income will now be considered. We repeat that as a general proposition the U.K. case law on allowable deductions from an employment source is not helpful to us because of the more restrictive wording of the rule in the United Kingdom (see end of previous chapter). Indeed section 51 (1) of the Australian statute is more relevant for our purposes because of its greater similarity to our Act so we quote it here again.

(i) Section 51 of the Australian Act

"Section 51—Losses and Outgoings. (1) All losses and outgoings to the extent to which they are incurred in gaining or producing the assessable income, or are necessarily incurred in carrying on a business for the purpose of gaining or producing such income, shall be allowable deductions except to the extent to which they are losses or outgoings of capital, or of a capital, private or domestic nature, or are incurred in relation to the gaining or production of exempt income".

The following points should be noted:—

The expenses ("losses and outgoings") of *business* must be necessarily incurred, while the expenses of other activities are allowed "to the extent to which they are incurred". In the case of Malaysia the latter provision is nearer to the rule for *all* sources of income. The phrase "to the extent . . ." is a refinement of the "wholly and exclusively . . ." condition. As we have stated the latter does not mean that composite expenses will be disallowed in their entirety for where the proportions can be ascertained, those incurred for the income earning purpose will be allowed. The use of "to the extent . . ." is a statutory authorisation of the apportioning practice carried on even under the "wholly and exclusively . . ." condition.

1. ALLOWABLE DEDUCTIONS FROM AN EMPLOYMENT SOURCE

(i) Capital and Revenue

The basic principle of capital and revenue holds and any outgoing on capital account is not allowable. The following have been *not allowed*:

Legal costs of defending taxpayer from a charge of padding his travelling expenses and not obeying an order. (*C.T.B.R. 8 (N.S.) Case 117*).

The cost of several appeals for promotion by a police officer (*C.T.B.R. 10 (N.S.) Case 102*).

The question of whether they were allowable was decided on the grounds that these were capital. Another example of a capital expense is payment to an agency which helps a person to find a job. This is not allowable, because it only helps a person to reach the income-earning stage, but is not a part of the occasional, incidental, or main operation of the income-earning activity. (*Shortt v. McIlgorm (Inspector of Taxes)* (1945) 26 T.C. 262).

A government employed architect travelled to England and Europe with a view to further his knowledge of architecture, and it was found as a fact that the trip was in fact devoted solely to this purpose. It was held in the High Court that the cost of the tour was deductible as "losses and outgoing . . . incurred in gaining or providing assessable income". (*F.C. of T. v. Finn* (1961) 8 A.I.T.R.). This is a new trend in the attitude of the Special Commissioner (in Australia and New Zealand at least) for hitherto the cost of securing qualifications has been held to be capital analogous to the acquisition of an additional fruit-bearing tree, whereas in some new cases the view that an additional course of study is like a recurrent cost of fertilizing a tree has been accepted (*11 C.T.B.R. (N.S.) Case 51*) see also *Tout v. Inland Revenue Commissioner*: (N.Z.) ((1970) 1 A.T.R. 705) where the expenses for education, books and travelling, on a university course of lectures in psychology and sociology by an Inspector of the Inland Revenue were held allowable. In this case however, Justice Moller of the Supreme Court of New Zealand, ended his judgement with this final comment:—

"This must be understood to be a decision on what I consider to be the somewhat special and unusual facts of this particular case, and not one of general application".

(ii) Travelling Expenses

The decided U.K. cases on this are not strictly relevant to Malaysia in view of the highly restrictive rule in the U.K. Act. Thus where a person is carrying on employment at one place and letting premises at another and during the course of the day he goes from his home to place *A*, place *B*, and then to his home, only the expenses from his home to place *A* and from place *B* to his home are disallowed. To put it in another way the expenses of reaching his first place of earning from his home and the expenses of reaching home from his last place of work are not allowable.

In the case of travel overseas on business or employment we can assume that the allowable expense begins from the time he leaves either his home or his office depending on where he left from. If a wife accompanies a husband on a business trip whether her expenses are allowable is a question of fact to be decided with reference to the circumstances, and if they are such that her presence is in the course of her husband's

business activities or partly so, the appropriate part of her expenses could be allowable. (c.f. *Maclean (Inspector of Taxes) v. Trembath* (1956) 36 T.C. 653)

The expenses of maintaining a car and telephone in the circumstances of (*Nolder v. Walter* (1930) 15 T.C. 380) would probably be allowable in Malaysia, as would the travelling expenses of the solicitor in (*Cook v. Knott* (1887) 2 T.C. 246) who travelled to another town to act as clerk to the Justices.

A barrister practicing in London who held an appointment in Portsmouth had his claim for travelling expenses to Portsmouth rejected, and also his hotel expenses rejected for deduction. In Malaysia his travelling expenses should definitely be allowed and also that part of his hotel expenses incurred above his normal living expenses should also be allowable (*Ricketts v. Colquhoun* (1926) 10 T.C. 118).

It bears repeating that the onus of proving that such expenses of a certain amount were of an allowable nature is on the person claiming them to be so:—

“Something more is required of a taxpayer than to give a ‘rough computation’ or a ‘pretty good idea’ or a ‘rough estimate’, when he is claiming a precise amount as outgoings incurred in the earning of his assessable income.” (10 *C.T.B.R. Case 47*).

If income-earning activity can be shown to have begun between a person's house and his place of work e.g. an employee-manager of a film company uses his car only for checking and selling purpose, the expenses of the journey from his house to the first theatre visited can also be allowed.

“In the case, the fact that the car is garaged at taxpayer's home does not appear to have any particular significance. From the time that taxpayer takes his car out of his garage and proceeds to his first call, he is no doubt engaged upon the business of his employer. He is on duty. He is using the car for business purposes. The case is thus different from one where a car issued to transport a man from his home to his place of business where, upon arrival, his working day commences and he starts to perform the duties for which he is paid”. (13 *C.T.B.R. Case 15*)

(iii) Employment “Loss”

In the rare event of the allowable expenses of employment exceeding the income from the employment source, such “loss” cannot be offset against the income from any other source in the basis period. Also not being a loss from a business source it cannot be carried forward to another period for setting-off.

(iv) Entertainment Expenses

Where the lunch-hour is devoted to furthering income-earning objectives and this can be proved by the person, the luncheon expenses are allowable, and even the fact that he would have to eat anyway to support life (such being not allowable), can probably be ignored.

Examples:

(a) (*Bentleys, Stokes and Lowless v. Beeson (Inspector of Taxes) (1952) 33 T.C. 491*). Solicitors had business luncheons, because they were so busy during office hours that they were forced to use the lunch hour—a situation reminiscent of the hustle and bustle of Kuala Lumpur. Held allowable.

(b) The entire hotel expenses of an actress were allowed, despite the contention that she would have had to eat anyway.

“I am not satisfied that it would be correct to make a finding incorporating a principle of general application that subsistence expenses are of a private or domestic nature irrespective of the circumstances under which the expenses are incurred.” (*1 C.T.B.R. (N.S.) Case 53*).

(v) **Nature of Employment Vital**

The nature of the employment of course is vital in making a decision.

A travelling salesman has a much better case for having his full living expenses away from home allowed than a person in another occupation not requiring travelling as a part of the employment.

An insurance salesman has a better chance to claim expenses and even heavy entertainment expenses in the pursuit of a wealthy prospect; and where his prospect is moving about and he has to accompany him; such expenses can also be claimed.

(vi) **Repairs and Renewals of Assets used in Employment (See pages 86 & 105)**

2. ALLOWABLE DEDUCTIONS FOR DIVIDENDS, INTEREST, RENTS AND OTHER INCOME

The General rule applies here *i.e.* all the outgoings and expenses wholly and exclusively incurred in the production of income are allowed. Hence any interest paid on money borrowed to buy shares or houses, which generates income is allowed and so are the other expenses incurred. In the case of interest and dividend incomes, bank commissions and charges are not allowed on the ground that these expenses are incurred not in the production of income but are incurred after the income has been produced. It is submitted that bank charges and commissions in respect of foreign dividends at least should be allowed as the expenses incurred are in the production of income. In reality a person cannot get the income from such dividends etc. into his possession unless he first incurs these expenses. To import some mystical idea of a fruition of such income prior to its receipt in the hands of a person is to inject a metaphysical line of reasoning into a practical situation. In our opinion the real question here is the nexus between the expense and the income—the foreign dividends would not have been received without the incurring of bank charges and commission.

3. REVISION QUESTIONS (Answers are on next page)

1. Set out the details of three legal decisions on travelling expenses in the United Kingdom, which would probably have been differently decided under the Malaysian Act.
2. Give an illustrative example to bring out the tax advantages of setting up a business of renting out premises instead of being a passive rentier? What changes are required to the latter operation to make it of the former type?
3. From personal observation and enquiry list at least five "articles" which would qualify for a renewals allowance in spite of being used in an employment source.
4. If expenses must be "wholly and exclusively" incurred in order to qualify for deduction, why are deductions allowed for a part of a doctor's car used in his work? What alternative phrasing would meet the situation?
5. Quote a part of a judgement given in any case you know, stressing the need for proper records to support a claim for deductions.
6. State whether the following expenses are deductible for income tax purposes. Give reasons for your answer.
 - (a) Cost of removal from one place of residence to another, on a change of employment.
 - (b) Interest paid on borrowed money used in trade or business.
 - (c) Employment agency charges for obtaining a post.
 - (d) Expenses incurred by an employee in travelling from residence to place of work.
 - (e) Fee paid for preparing income tax returns.
 - (f) Company formation expenses.
 - (g) Income Tax paid by employer on employee's remuneration.
 - (h) Contractual gratuity of \$12,000/- paid to employee who has worked 11 years as compensation for loss of office.
 - (i) Expenses incurred abroad to purchase trading stocks.
 - (j) Legal costs in connection with an income tax appeal.
 - (k) Initial repairs to machinery just purchased, such repairs being charged to revenue according to "sound accountancy principles".
 - (l) Cost of employing a domestic servant so that wife can go out to work.
 - (m) Legal charges incurred in defending an action concerning the title to properties abroad used in the business, such title being in fact a good title.
 - (n) Expenditure on installation of machinery.
 - (o) Fee paid for renewal of trademarks.
 - (p) Costs of acquiring lease incurred by a general goods dealer, on his business premises.
 - (q) Expenses incurred in an increase of share capital.
 - (r) Costs in an action to compel customers to take delivery of goods.
 - (s) Refresher course expenses by professional man, which do not "enlarge the profit-earning subject".
 - (t) Parking and speeding fines.

- (u) Provision for contingent service liability in the case of a motor-trader who sells cars under a guarantee of service for a certain period of time.
- (v) Architect's fees in connection with erection of new factory premises by manufacturer.
- (w) Lease costs incurred by a property owner who lets his property.
- (x) Expenses incurred by a property owner who lets his property.
- (y) Lunch expenses of \$120/- incurred by an insurance salesman for three prospects and himself. None of the prospects in fact took out a policy.

ANSWERS

1. See (1) *Nolder v. Walters*; (2) *Cook v. Knot*; (3) *Ricketts v. Colquhoun*.
2. (a) Wear and Tear allowance in respect of Plant and Machinery may be claimed.
 - (b) Losses if any can be set off against other income in the same year of assessment and also losses can be carried forward to the set off against the income of business sources.
3. (1) Car used by a salesman. (2) Books bought by a lecturer. (3) Tape-recorders used by T.V. and Radio Announcers.
4. See paragraph 5, Chapter XV; expenses incurred to the extent . . .
5. 10. C.T.B.R. Case 47.
6. (a) No—incurred to put the tax payer in a position to earn income and not in the production of income.
 - (b) Yes—see 33 (a).
 - (c) No—same as (a).
 - (d) No—same as (a)—employment starts after he reaches the place of work.
 - (e) No—expense incurred after the production of income.
 - (f) No—expense incurred before the production of income.
 - (g) Yes—if paid as extra allowance. No—if it is to be recovered from the employee.
 - (h) Yes—expense incurred in the course of business by the employer.
 - (i) Yes—expense incurred in the course of business by the employer.
 - (j) No—expenses incurred after the production of income.
 - (k) Yes—see *Odeon Associated Theatres Ltd. v. Jones* (1970) T.R. 299.
 - (l) No—same as (a).
 - (m) Yes—incurred in the maintenance of fixed asset—see *Southern v. Borax Consol Ltd.* 23 T.C. 597.
 - (n) No—capital expenditure.
 - (o) Yes—in the course of business.
 - (p) First time—no, renewal—yes; same as (a).
 - (q) No—capital expenditure.
 - (r) Yes—in the course of business.
 - (s) No—same as (a) also see *Tout v. Inland Revenue Commissioner, Supreme Court (N.Z.)* ((1970) 1 A.T.R. 705).
 - (t) No—not in the production of income.
 - (u) No—provisions not allowed.
 - (v) No—Capital expenditure.
 - (w) Yes—in the course of business.
 - (x) Yes—in the course of business.
 - (y) Yes—in the course of business.

CHAPTER IX

SPECIFIC DEDUCTIONS STATUTORILY ALLOWED OR PROHIBITED

Preliminary Note

In addition to the general provision for allowable deductions set out in section 33 (1) the Act extends the scope of this rule in the three following paragraphs modified by subsection (2). Also section 34 provides for the additional specific deductions from a business source followed by section 35 which deals with stock in trade. The only deductions allowed for a section 11 source on income as calculated by section 31 are given in section 37 and we end the discussion of specific deductions with section 38 dealing with additional specific deductions from an employment source. The chapter ends with a discussion of deductions statutorily prohibited by section 39.

1. SPECIFIC DEDUCTIONS ALLOWED

(i) List

We list these and follow them with a discussion of each.

From all sources—section 33 (1)—(except a source arising from occupation of premises (see sections 11, 31 and 37))

- (a) net interest incurred on money borrowed and employed in earning income;
- (b) rent incurred on property used to earn income;
- (c) repair of large assets and repair, renewal and alteration of small implements etc.

Additional Specific Deductions from a Business Source—section 34 and 35

- (a) business debts written off;
- (b) obligatory contributions to an approved scheme for employees engaged in producing income;
- (c) mine capital expenditure as per schedule 2;
- (d) payroll and turnover tax;
- (e) improvements to replanting of a plantation;
- (f) expenses incurred in scientific research;
- (g) adjustments in stock in trade.

(ii) **Net Interest Incurred on Money Borrowed and Employed in Earning Income—Section 33 (1) (a)**

If you borrow money to build a house and then rent it out but you are not in the business of renting out houses, the interest you pay can be deducted from the rent you earn, the balance (surplus) only being assessable to tax. When the interest you pay on money borrowed to buy the house above or any other capital employed to earn income (except interest borrowed to carry-on a business) is more than the income earned you cannot offset this against other income. You cannot even carry it forward to deduct from next year's income from the same source e.g. If interest on money borrowed to buy a house comes to \$3,000 in 1 year while the net rent is only \$2,000 you have a loss of \$1,000. You cannot offset this loss against a gain from other sources. Even if in the following year you make a gain of \$2,000 from the same house you cannot deduct your previous year's loss. If the interest is on money borrowed to run a business etc. as defined in section 4 (a) then such a loss can be set-off and carried forward.

It is possible that a person carrying on a business of his and using borrowed money may in fact lend the whole or part of the borrowed sum out in order to earn some interest or buy an investment with it. In such circumstances section 33 (2) provides that except in the case of loans given for the purpose of producing the gross income (e.g. by money lenders) where it appears to the D.G. that the borrowed money has partly or wholly been so used then the deduction allowable for the interest incurred must be proportionately reduced. An example will clarify:

Mr. X in the course of his business has borrowed \$100,000/- on 1.2.1971 from a bank at 1% interest per calendar month. In the opinion of the D.G. he has used this sum to purchase shares worth \$30,000/- and lent out \$60,000/- to his brother interest-free.

The deduction allowed will be:

$$\begin{array}{r} \text{Interest Accumulated on} \\ \text{Borrowed Sum} \quad \text{Less} \end{array} \left\{ \begin{array}{l} \text{Interest Accumulated} \\ \text{on Borrowed Sum} \end{array} \times \frac{\text{Loan + Cost of} \\ \text{Investment}}{\text{Borrowed Sum}} \right\}$$

$$\begin{array}{r} \$1,000 \quad - \quad \{ \$1,000 \quad \times \quad \frac{60,000 + 30,000}{100,000} \} \\ \$1,000 - \$900 = \$100 \end{array}$$

Only \$100 will be allowed as deduction against the business profits instead of \$1,000. If the result leads to a minus figure then the deduction is zero. 33 (2) (c).

The Act now provides that the above calculation can be done in an alternative way if the D.G. is of the opinion that this alternative is just and reasonable in all the circumstances. The above calculation or the alternative is to be done every calendar month and the total deduction is to be the aggregate. "Calendar month" has the usual meaning but in addition section 33 (3) provides that a part of a month is to be taken as a calendar month.

Illustration

P borrowed \$100,000 from a bank at 12% p.a. to be used in his business. Out of this money he bought shares in *TR Ltd.* for \$30,000 and lend out \$40,000 to *Q* a friend free of interest. From the following information, calculate the interest which will be allowed to *P* against his gross income from business.

Month Ended	Amount of the Loan from the Bank	Interest Paid to Bank	Cost of Shares in <i>TR Ltd.</i> and Loan to <i>Q</i>
31.1.1971	\$100,000	\$1,000	\$70,000
28.2.1971	90,000	900	70,000
31.3.1971	80,000	800	70,000
30.4.1971	70,000	700	70,000
31.5.1971	60,000	600	70,000
30.6.1971	50,000	500	60,000
31.7.1971	40,000	400	60,000
31.8.1971	30,000	300	30,000
30.9.1971	20,000	200	30,000
31.10.1971	20,000	200	30,000
30.11.1971	20,000	200	NIL
31.12.1971	20,000	200	—

Solution

Date	Interest Paid to Bank		Interest Allowed as Deduction
31.1.1971	\$1,000	$[\$500 - (\$500 \times \frac{70000}{100000})]$	$= \$500 - \$350 = \$150$
28.2.1971	900	$[\$500 - (\$500 \times \frac{70000}{90000})]$	$= \$500 - \$389 = \$111$
31.3.1971	800	$[\$500 - (\$500 \times \frac{70000}{80000})]$	$= \$500 - \$438 = \$62$
30.4.1971	700	$[\$500 - (\$500 \times \frac{70000}{70000})]$	$= \$500 - \$500 = \text{Nil}$
31.5.1971	600	$[\$500 - (\$500 \times \frac{60000}{70000})]$	$= \$500 - \$583 = \text{Nil}$
30.6.1971	500	$[\$500 - (\$500 \times \frac{60000}{60000})]$	$= \$500 - \$600 = \text{Nil}$
31.7.1971	400	$[\$500 - (\$500 \times \frac{60000}{50000})]$	$= \$500 - \$750 = \text{Nil}$
31.8.1971	300	$[\$500 - (\$500 \times \frac{40000}{50000})]$	$= \$500 - \$750 = \text{Nil}$
30.9.1971	200	$[\$500 - (\$500 \times \frac{30000}{50000})]$	$= \$500 - \$750 = \text{Nil}$
31.10.1971	200	$[\$500 - (\$500 \times \frac{30000}{40000})]$	$= \$500 - \$750 = \text{Nil}$
30.11.1971	200	$[\$500 - (\$500 \times \frac{\text{Nil}}{20000})]$	$= \$500 - \$000 = \$500$
31.12.1970	200	$[\$500 - (\$500 \times \frac{\text{Nil}}{20000})]$	$= \$500 - \$000 = \$500$
	<u>\$6,000</u>		<u>\$1,323</u>

Note: Section 33 (2) (a) provides that interest accrues evenly over the months. As such the interest for the year \$6,000 is divided equally for each month regardless of the actual amount paid in each month.

(iii) **Rent Incurred on Land or Building used for Producing Income—Section 33 (1) (b)**

One point to note is that statutory authority is given to the principle of apportionment as opposed to the "wholly and exclusively" restrictions, at least in the specific case of rent. This is done by the words "... respect of any land or building or part thereof . . ."

Thus where even a part of a rented palatial residence is used in the acquiring of income, a reasonable part of the rent can be claimed as a deduction.

Also the use of the premises or land must be "by that person for the purpose of producing the gross income from that source". Thus rent incurred on premises used to produce income from source *A* cannot be deducted from gross income from source *B*. Also the deduction is only available to the relevant person chargeable to tax on that particular income produced by that particular rental expense. This may seem to be stating the obvious but we include it here because we wish to make a point about our Act which written in simple language has been often amended to make such refinements e.g. the requirement "from that source" was added by Act A13. This painstaking attitude is to be admired and commended although it may be a source of irritation to some practitioners.

(iv) **Repair of Large Assets and Repair, Renewal and Alteration of Small Implement or Article—Section 33 (1) (c)**

The question firstly is as to what kind of asset comes under this. "Capital Allowances" on certain industrial buildings, plant and machinery, used in only a business activity are allowed to be written off under schedule 3. Some of these same assets if used in other income earning activities (i.e. not a business source under section 4 (a)) can only be claimed when a new asset is acquired to replace an old one already expended in the activity. The authority for this is contained in section 33 (1) (c). In this section the following are mentioned for repairs only—premises, plant, machinery or fixtures—but in the case of any implement, utensil or article, renewal, repair or alteration are allowable.

This to our mind means that almost every material object (except those prohibited specifically) used in the acquiring of income is allowed on a renewal basis. In the case of assets specifically not allowed to be written-off, repairs are still allowed. This has the following applications in practice. The reason why one does not actually encounter such cases in real life is that most such persons are not chargeable to tax due to their small income, but the familiar scene can provide us with ample illustrations of principles.

Example 1

EMPLOYED LAWYER'S LIBRARY

A person employed as a lawyer has built up an extensive law library in his study in a part of his private residence. Which of his expenses are allowable?

Answer

1. The net annual value or rent on the portion represented by the law-library.
2. New editions of books to replace previous editions outdated or worn out.
3. The salary of a librarian or secretary working here.
4. A portion of the light, water and other charges.
5. The cost of an air-conditioner to replace the old one that is beyond repair.
6. The cost of any chemicals used to protect the books.
7. The repair, painting and renewal of shelves and other library equipment.

Assumption

We have assumed that the library as such is an essential "implement, utensil or article" employed in acquiring an income. (Also see later under Capital Allowances for assets employed in a trade business profession or vocation).

*Example 2***GENERAL ALLOWABLE EXPENSES****(i) Lecturers**

Repair of a typewriter or tape-recorder, salary of a typist preparing his notes, lectures, etc., reasonable cost of journals connected with his subject. (Section 33 (1)).

(ii) T.V. Malaysia Part-Time Announcer

Travelling expenses to the studio from his office and vice versa. Renewal and repair of special uniform (if any), tape-recorder, tapes.

(iii) Night Watchman

Cost of a new raincoat or torchlight to replace one worn out. Cost of batteries in his torchlight.

(iv) Social Escort

Renewal of special dresses used only in work, cost of cosmetics and perfumes necessary due to the nature of the work.

Assumption

We have assumed that the relevant circumstances are such that they do not rule out the classification of these as allowable deductions. Also that these do not fit into the category of those specifically prohibited under the Act (see below).

The last part of paragraph (c) and the bracketed qualifications are designed to prevent double deduction of items which are entitled to capital allowances and the deduction of capital expenditure on "any premises, buildings, structures or works of a permanent nature."

(v) Business Debts Written Off

N.B. Section 34 (2) is specifically for debts in respect of a business—section 4 (a)—source, and hence is not available for bad debts arising say from a non-business renting out of houses. The debt to which section 34 (2) applies is statutorily defined in section 34 (3) as a debt arising in respect of section 24 (1) or (5) which consist of debt arising from:

- (a) stock in trade sold in the course of a business;
- (b) services rendered at any time in the carrying on of a business;
- (c) the use or enjoyment of any property at any time in the carrying on of a business;
- (d) any interest which first becomes receivable in respect of a debenture, mortgage or other source of interest provided that such interest bearing investments etc. formed the stock in trade of a business;
- (e) any interest which becomes receivable in respect of a loan given in the course of a money lending business.

The Act provides that where an item falls to be a debt under more than one head it shall be counted as such only once.

Those debts which have been included in calculating the income for any taxable period are allowed as deductions if they cannot be recovered. Thus bad debts of a time prior to the basis period for the first year of assessment, when the law was enforced, cannot be allowed as deductions because they were never included in any taxable income i.e. debts incurred before 1.1.1947. These debts (of a period before 1.1.1947), even if recovered, need not be included as income. However, in case any bad debts which have been allowed as deductions, are recovered, these must be included as the income of the period in which they are received. A bad debt is one which cannot be recovered because of the customer's bankruptcy, death, or leaving the country etc. Sometimes when things have not yet reached this stage but something has happened to cast doubts on the possibility of recovering the debt, a specific provision can be charged as an allowable deduction provided it has been a trading receipt. However, the common accounting practice of charging a certain percentage of all debts as a general provision will not be allowed; for the provision to be allowed for tax purposes it must be on specific accounts. The period in which the debt was contracted is not important except as indicated as above, that debts contracted prior to the first basis period cannot be allowed and do not have to be included as incomings when recovered. The first basis period in this context also means the first basis period of the business e.g. if XYZ & Company is taken over by XYZ & Company Limited on 1.1.1971; for XYZ & Company Limited the first basis period for the year of assessment 1972 is 1.1.1971 to 31.12.1971. Any debts incurred prior to 1.1.1971 and written off after 1.1.1971 will not be allowed.

It is to be noted that the bad debts of money-lending concerns arising on the loans lost are *not* allowable deductions under this section but the tax effect is the same because they can be charged as a loss of circulating capital. Debts represent the stock-in-trade of these firms and in this respect are different from the debts mentioned in 33 (1) (c).

As stated above only business bad debts are allowable. We give an example of a non-allowable bad debt.

Example

X is a person (not in the business of renting out houses) who has included \$6,000/- as rental income from a house. This figure represents rent from 1.1.1969 to 31.12.1969 at \$500/- p.m. After deducting \$1,500/- being interest paid on money borrowed to buy the house, assessment, repairs etc. \$4,500/- is declared on 31.3.1970 as net income from this source, and tax has been paid. However in 1969 the November and December rent had not been paid and it now appears that it cannot be recovered. This "Bad Debt" is not a bad debt under section 33 (1) (c). The loss would appear to be unclaimable unless relief under section 131 (error and mistake) is successfully claimed.

In the event that the person claiming a deduction for bad debts is not ordinarily resident for the basis year for a year of assessment the Act provides that section 34 (2) shall apply as if section 12 (1) (other than paragraph (b) (ii)) had been applicable to all the previous basis years. The effect of section 12 (1) (q.v.) is to apportion gross income when it is necessary to find the portion derived from Malaysia. Thus a not ordinarily resident person cannot claim a deduction on bad debts which may have arisen on a portion of his business which has not been brought to charge to tax in Malaysia.

(vi) Contributions to an Approved Scheme for Employees Engaged in Producing Income

Contributions made by an employer on behalf of his employee to an approved scheme ("any pension or provident fund, scheme or society approved by the D.G. under section 150") up to a maximum of 15% of the remuneration are an allowable deduction. However this deduction is allowable only to the extent that the employees remuneration has been allowed as a deduction.

Example

Dr. *X* employs a chauffeur at a monthly salary of \$400/- p.m. but the D.G. allows only \$300/- p.m. of this as a deduction from the business income. If Dr. *X* contributes at 10% to E.P.F. i.e. \$40/- the amount allowed will be:

$$\$40 \times \frac{300}{400} = \$30$$

A special contribution to a new fund to enable employees to back-date the benefits with respect to their past employment may be allowed by the D.G. when he approves such fund. The amount allowed, will be decided by the D.G. In practice such back-dating will not be allowed for more than six years or so, but the decision will depend on the circumstances. [Section 34 (5).]

(vii) Payroll and Turnover Tax

Sums paid for these are allowed as a deduction.

(viii) Mine Capital Expenditure Allowable Pursuant to Schedule 2—Section 34 (6) (c)

Where any part of the gross income is from the working of a mine then a deduction calculated according to the provision set out in Schedule 2 of the Act is allowed. Very briefly Schedule 2 provides for the treatment of a mine as a wasting asset and the residual value of a mine is divided by the expected life to give a figure for deduction from the gross income of the mine.

(ix) Improvements to and Replanting of a Plantation—Section 34 (6) (d)

From the relevant gross income obtained from the working of any plantation there may be deducted the expenses incurred in replanting or improving the plantation. It should be noted that the allowing of deductions for improvements and replanting is a rather exceptional one. The line of reasoning on which this is based is well stated in *Vallambrosa Rubber Co. Ltd. v. Farmer (Surveyor of Taxes)* (5 T.C. 529).

However the following are NOT allowed to be deducted:

(a) Expense which would be classed as qualifying expenditure or qualifying plantation expenditure for the purpose of Schedule 3. (Schedule 3 deals with capital allowances and charges, and since such capital expenditure will be allowed under that Schedule, it is not allowed as a deduction).

(b) Expense incurred in the acquisition of land or on anything growing thereon.

(x) Expense Incurred in Scientific Research—Section 34 (7)

Expense incurred in scientific research is an allowable deduction if:

(a) it is not of a capital nature; and,

(b) the research is related to the business; and,

(c) it is directly undertaken by the person or on his behalf; and,

(d) it is by the relevant person during the relevant period.

Where any sum is paid to a scientific association, approved by the Minister for this section as undertaking research related to the business, this is allowed.

Also a sum paid to a university, college or research institution approved by the Minister as above is allowed.

However there is no double-deduction allowed and where a deduction has been allowed under section 34 it cannot also be allowed under section 33, e.g. if expenditure on scientific research has been allowed under section 34 (7) (a), it cannot also be claimed as a deduction under section 33. Section 34 (8).

(xi) Adjustments in Stock in Trade—Section 35

Income from a business is brought to tax on its gains or profits. In the determination of these gains or profits however the stock in trade plays a most vital part. The Act provides how this is to be treated in section 35.

The problem boils down to how the stock is to be valued at the beginning and at the end of the basis period and the Act provides that this shall be the market value, unless the person elects that this should be cost and the item is a physically tangible one. Given this condition, cost is defined as the total cost of acquisition to the person including the cost of any materials used in its manufacture, preparation or construction and the cost of bringing it to its condition and location at that time.

The value at the beginning of any basis period (except for a new business) shall be the value at the end of the immediately preceding basis period such value being determined as above but from the year of assessment 1968, where at the end of the relevant period stock consists of immovable properties, stocks, shares or marketable securities, the value to be placed must be cost to the person or market value at that time whichever is *lower*. Where an accounting period other than the normal basis year is being used by the exercise of section 41, then the reference to the basis period in the previous sentence extends to such basis periods as construed under section 41 i.e. the closing stock value of an immediately preceding basis period will be used as opening stock value for the next period arising by application of section 41.

Any increase in the value of the stock during the basis period (found by comparing the value at the beginning and at the end) is to be deducted from the sum of the allowable deductions in sections 33 and 34 and any decrease is to be added to such sum. However if the person is not ordinarily resident in the basis period, he is chargeable only on his income derived from Malaysia, so only the stock which relates to his income so derived from Malaysia is to be included as above.

If on the permanent cessation of a business, trading stock is sold for valuable consideration to a person who is or will be carrying on a business of such a nature that the cost of the stock would be a deductible item for tax purposes, then such stock is valued at the amount of the price paid or the valuable consideration given and this is the value of the stock at the end of the period. (Section 35 (5) (a)).

Firstly it must be realized that what is or is not trading stock depends on the nature of the business. Thus land is the trading stock of a land-developing company but it is certainly not the trading stock of a manufacturer of plastic toys. Hence if the former ceases business and sells the land for \$X to the latter, \$X will not necessarily be considered as the value of the trading stock sold by the land company because the plastic toy manufacturer cannot deduct the cost of the land in calculating his profits.

What then will be the value placed on this land?

The answer is that in such a case the open market value on the date of the discontinuance of the business shall be the value of such trading stock.

The effects of this provision become clear if we consider the following situation:

X Co. an export-import firm holds some land for investment purposes. It sets up a wholly owned subsidiary, *XY* Land Developing Co. to which it transfers this land. *XY* develops the land and sells part of it, but the overall results are losses every year. *XY* is now liquidated and the rest of its land which was purchased at \$1 million from *X* is to be 'sold' to *X* at \$1 million, although the open market value is now \$10 million. The value placed on this stock in calculating the profit of *XY* for its last year will be \$10 million.

If *XY* sold the land to another land dealing company it would not matter so much if the value placed were \$1 million. For when the next company sold this land for \$10 million it would have to show a profit of about \$9 million less expenses on this transaction.

Similarly a disposal of motor cars by a car dealer in liquidation to other car dealers could be at any price but where these are sold to other types of firms a market price has to be used to prevent tax avoidance.

Where the stock in trade is sold or transferred together with other assets to another person to whom it also forms stock in trade (i.e. as per section 35 (5) (a)) and where the consideration may be partly in cash and partly otherwise then the Act provides in 35 (5) (c) that the value to be placed on the stock shall be such an apportioned amount as is just and reasonable. The value placed on that stock in the hands of a purchaser is to be the same value as calculated above. (We could just note here that in a winding-up the final accounts of the firm for tax purposes are prepared to record all revenue sales and revenue expenses and fixed capital sales are not taken in unless a balancing charge or allowance falls due on industrial building or plant and machinery, used in the business.)

2. DEDUCTIONS NOT ALLOWED BY THE ACT—SECTION 39

Deductions are firstly allowable under the general provision of section 33 (1) and this general provision is expanded by the specific examples given above. Subject to these allowable deductions, and other provisions for relief, exemption etc. in the other parts of the Act the items below are not allowed as deductions. This means that where for example a domestic expense like educating a child overseas is allowed as a deduction then a provision like section 39 (1) (a) prohibiting "domestic or private expenses" shall be of no effect to the extent that such expense is allowed as a deduction by another part of the Act. (Section 48 (3)). (This example illustrates the meaning of the phrase "Subject to" in the statute). (See however section 39 (2) for a qualification).

(i) Domestic or Private Expenses

These are not allowed.

(ii) Money not "Wholly and Exclusively" Spent for Earning Gross Income

This will in effect perhaps prohibit "Dual Purpose Expenditure". Where money is expended and at the same time, a say private and domestic purpose as well as a business purpose is served we *could* term this as not wholly and exclusively for the purpose of earning income. Where taxpayer could prove either that the whole expenditure was for an income earning purpose or where there was a dual purpose but he could document the proportion of the expenditure pertaining to the income earning purpose, he would be allowed such proportion.

(iii) Capital

The drawings of the owners of a firm are capital withdrawn, regardless of the fact that they are from the revenue surplus of the firm; and as such, they cannot be allowed as deductions.

Any sums expended by a firm to bring about an enduring benefit to the firm are capital expenditures and are not allowed as deductions.

Even where such are withdrawn with the intention of using them as capital although they may not yet be so used they are not allowable.

(iv) Unapproved Funds or Schemes

Payments to pension, provident, savings, widows and orphans funds etc. where such are not approved by the D.G. are not an allowable deduction. Of course there is nothing to prevent the employer from actually adding such sums to the remuneration of the employees, in which case the enhanced portion of the remuneration will be an allowable deduction together with the previous remuneration.

There would then of course be no contribution by the employer to an unapproved fund, and whether to save or spend will be at the employee's own discretion.

(v) Qualifying Expenditure

Any business expenditure which is a qualifying expenditure under Schedule 2 (qualifying mining expenditure), or Schedule 3 (qualifying expenditure, qualifying plantation expenditure or qualifying forest expenditure), or Schedule 4 (qualifying prospecting expenditure) which would be allowable but for section 39 (1) (e) is not allowed. These expenditures are required to be written off in a specific way set out in these schedules.

(vii) Interest Paid to Persons not Known to be in Malaysia—Section 39 (1) (f)

Such interest paid without deduction of tax and the payment of such deduction to the D.G. as required under section 109, is not allowed. Thus if X Co. borrows \$1 million from a Hong Kong financier at 10% p.a., it is required to deduct \$40,000 from the interest payable to him, if he is "an individual not known . . . to be in Malaysia at

the time of payment". If they do not so deduct and pay the \$40,000 to the C.G. then the \$100,000 interest will not be allowed as a deduction, increasing their profit or reducing the loss as the case may be, for tax purposes.

(viii) **Timber Royalties**

Any money payable for the use of a licence or permit to extract timber (otherwise than to a State Government) is not allowable no matter by what name such sum is called.

3. REVISION QUESTIONS (Answers are on page 97)

1. Mr. Lim owns the following houses:

Houses	A	B	C	D
Defined Value	\$5,000	\$5,000	\$4,500	\$4,000
Rent received	Nil	5,000	4,500	4,000
	(owner occupied)			
	_____	_____	_____	_____

Expenses:

Assessments	1,800	1,080	900	900
Repair and Maintenance	1,000	1,500	2,000	2,500

Fire Insurance:

House	100	60	50	50
Contents	50	30	25	25
Mortgage Interest	1,000	1,500	1,300	1,000
	_____	_____	_____	_____
	\$3,950	\$4,170	\$4,275	\$4,475

Compute Mr. Lim's Income for tax purposes in such a way that he has to pay the minimum tax.

- What do you understand by "Initial Repairs"? Are they allowable for tax purposes? Quote a case in support of your answer.
- The following properties have been occupied by Mr. Lim for purposes of residence since 1964:—
 - 105 Jalan Hippy
(Cost \$100,000/-) D.V. \$7,200/- Assessment at 36%
 - 307 Jalan Hippy
(Cost \$50,000/-) D.V. \$3,480/- Assessment at 27%
 - 109 Pasir Panjang Road
(Cost \$12,000/-) D.V. \$900/- Assessment at 23%

The properties have been insured against fire and details of the premiums paid are as follows:—

	1970	1971	1972	1973
No. 105	\$250	\$260	\$270	\$270
No. 307	120	120	120	120
No. 109	36	36	30	30

The following expenses were also incurred:—

	1970	1971	1972	1973
Mortgage Interest				
No. 105	\$585	\$425	\$360	\$300
No. 109	800	200	—	—
Installation of Air-conditioners				
No. 105	—	180	—	—
No. 307	—	80	—	—
Quit Rent				
No. 307	35	35	35	35
No. 109	9	9	9	9
White-washing and Painting				
No. 105	600	Nil	500	Nil
No. 109	Nil	300	Nil	250
Cost of Construction of Road				
No. 105	100	50	150	—
No. 109	100	50	30	—

Ascertain the Adjusted profit from the properties assessable under section 4 (d) for each of the years of assessment 1972, 1973, and 1974.

4. (a) *A*'s accounts for the year ended 31.12.1970 show a net profit of \$15,000/- after charging the following:—

Bad debts written off	..	..	..	..	\$1,000
Provision for doubtful debts	..	..	..	..	5,000

Bad debts are all trading debts. Compute adjusted profit for tax purposes.

- (b) *B*'s accounts for the year ended 31.12.1970, show a profit of \$20,000/- after charging and crediting the following. Compute adjusted profit for tax purposes.

Charges

Bad debts written off	..	..	..	..	\$3,000
Provision for doubtful debts	..	..	..	..	6,000

Bad debts written off consisted of the following:

Personal Loan to Moota an uncle of <i>B</i>	..	..	..	..	\$ 500
Toka a customer to whom goods were supplied	..	..	..	..	1,500
An advance to Manium an employee of <i>B</i> . (Manium left the employment without paying the advance.)	..	..	..	..	1,000

\$3,000

Credits

Cash received from *P* a customer \$ 800

In 1969 *P* had become bankrupt and a debt of \$8,500
had been written off as bad.

- (c) *R*'s profit and loss account for the year ended 31.12.1970 shows a loss of \$25,000 after charging \$30,000 as bad debts. This amount of \$30,000 is made up of the following:—

Bad debts written off (all trade debts)	\$10,000
Provision for specific bad debts (<i>A</i> , <i>B</i> and <i>C</i> each of them owe \$5,000)	15,000
Provision for doubtful debts (10% on the balance of the debtors after the above specific provision)	6,000
	<hr/>
	\$31,000
Less: Bad debts recovered (these trade debts were written off in 1968)	1,000
	<hr/>
	\$30,000

Compute adjusted profit/loss for tax purposes.

- (d) *T* Ltd. was formed on 1st January, 1969, to take over the assets and liabilities of Leong & Partners. During the year ended 31st December, 1970, *T* Ltd.'s profit and loss account shows a net profit of \$35,000 after writing off debts of \$20,000. This amount of \$20,000/- was in respect of the following:—

Debts taken over from Leong & Partners	\$10,000
Debts incurred by <i>T</i> Ltd. after 1.1.1969	10,000
	<hr/>
	\$20,000

(All the above debts were trade debts).

Compute adjusted profit for tax purposes.

- (e) The bad debts charged in the profit and loss account of *P.G.* Ltd., amount to \$940/-, made up as follows:—

Bad debts written off		\$1,090
Deduct: Bad debts recovered	\$30	
Transfer from bad debts provision account:		
General	\$50	
Specific	70	120
	<hr/>	<hr/>
		\$ 940

You are required to make the necessary adjustments in respect of this account for income tax purposes.

5. State whether the following expenses are deductible for income tax purposes. Give reason for your answer.
- Cost of new books to a lawyer, for his library.
 - Cost of a jacket worn only on duty by a T.V. Malaysia announcer.
 - Cost of a torchlight to a night watchman replacing his old torchlight.

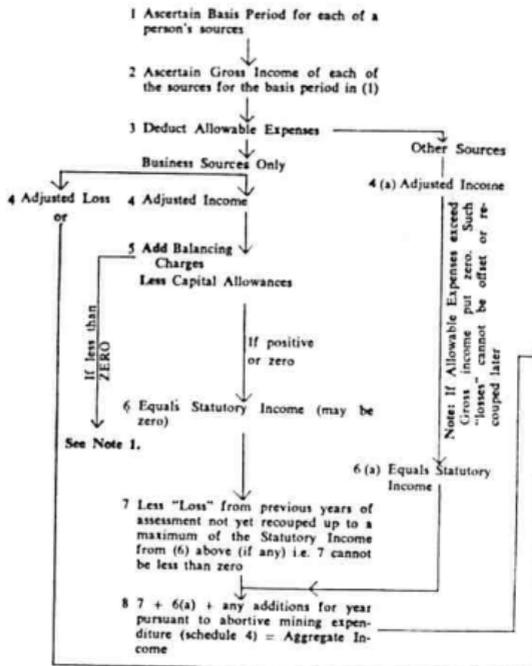
ANSWERS

- By grouping the properties adjusted income is \$660—insurance on contents not allowed.
- See 'Law Shipping Co. Ltd. v. I.R. Comrs.' ((1923) 12. T.C. 621) and Odeon Associated Theatres v. Jones The Times, November 13, 1970 (1970) T.W. 299.

3.	Y/A 1972	Y/A 1973	Y/A 1974
No. 105	\$3,923	\$3,478	\$4,038
Exemption may be claimed in respect of this house.			
No. 307	\$2,385	\$2,385	\$2,385
No. 109	148	654	404
Total for the Y/A	<u>\$2,533</u>	<u>\$3,039</u>	<u>\$2,789</u>

- \$20,000
 - \$27,500
 - \$19,000 (loss)
 - \$45,000
 - Total charge for bad debts in the profit and loss account should be \$990 (or additional \$50).
- No—Capital expenditure.
 - Yes—only on replacing the first one.
 - Yes—replacements.

FLOW DIAGRAM SHOWING PROCESS OF ASCERTAINING CHARGEABLE INCOME



NOTE 1. This represents an excess of Capital Allowances, which can only be offset against the adjusted income (if any) of that particular business in the following year or years.

REFERENCE

No.	Topic
1	Basis
2	Gross income
3	Allowable Expense
4	Adjusted Income/Loss for business source
4(a)	Adjusted Income
5	Balancing Charges and Capital Allowances
6	Statutory Income of business sources
6(a)	Statutory Income of a non business source
7	Unrecouped losses of previous years
8	Aggregate Income
9	Total Income
10	Chargeable Income

- 9 Aggregate Income Less
- Adjusted Loss for current year from (4) up to a maximum of the Aggregate Income.
 - Abortive mining Expenditure (schedule 4)
 - Approved Donation = Total Income
- Note:** Total Income cannot be less than zero and any adjusted loss not deducted here can be offset in future years against the Statutory Income from Business sources only
- Donations in excess of available Aggregate Income cannot be carried forward.
- Total Income Less Deductions for:
- self
 - earned income
 - wife, or former wife
 - wife's earned income
 - children
 - insurance premiums and obligatory contributions to an approved provident or pension fund.
- = Chargeable Income

CHAPTER X

PERSONAL INCOME TAX

1. PERSONAL

No matter *what* the source of income may be, and in the case of ordinarily resident individuals no matter *where* the source of income may be, some PERSON must pay the income tax on it. So we have written this chapter in a very special way. We shall assume almost no previous knowledge and will try to be clear and precise. If at the same time we are not comprehensive our more learned readers can get some pleasure out of pointing out what we have left out. We also have the more serious purpose of summarizing the material of this book, from the view-point of the individual taxpayer.

You are a taxpayer, or about to become one, otherwise you won't be reading this. If you are an average human being you probably want to know how not to pay tax even with a high income. We regret that we cannot tell you this. It would be ILLEGAL for us to do so. It could be CRIMINAL even. And we could go to gaol for three years and pay a fine of Ten Thousand Dollars and YOU could join us in the gaol and in paying the fine. In addition you may have to pay TREBLE the tax we helped you evade and also the tax. AND you cannot write off all this money you pay as penalty in your accounts as an expense of business. And as for claiming as deduction the travelling expenses to and from the gaol or the lawyer's fees etc.—that is unthinkable.

However do not give up reading this book yet. Although we cannot help you to EVADE tax which the law requires you to pay, we can and will help you by guiding you through the maze so that you can get all the benefits and rights that the law allows you.

In other words we will help you to do your duty as a citizen of Malaysia by paying your tax correctly, promptly and as painlessly as possible. At the same time we will try to teach you to look after the most important person—yourself.

2. TREES AND FRUITS

It is useful to think of the various sources from where you get gains or profits, benefit or money, as *trees*, and the actual gains you get as the fruits. The source is the tree and the gain is the fruit.

- Your job is a tree. —Your pay is a fruit.
 Your housing allowance is a fruit.
 Your overtime is a fruit.
 Your bonus is a fruit.
 Your 'ang pow' from the boss is a fruit.
 Your free lunch is a fruit.
 Your free home is a fruit.
 Your free transport provided by the firm is a fruit.
- Your business whether partnership or sole-proprietorship is a tree. —Your share of the adjusted profits is a fruit.
- Your portfolio of shares is a tree. —The dividends are a fruit. But not Bonus Shares and Rights Issues.
- Your fixed deposit in a bank is a tree. —The interest earned is a fruit.
- Your house rented out is a tree. —The net rent is a fruit.
- Occupation of premises for non-business purposes is a tree. —The net annual value or economic rent is a fruit.

You must reveal the value of *all* the fruits from your job etc. to the D.G.

You have to do this whether he asks you or not, and you cannot get out of your responsibility by saying things like, "I never got a form."

In fact if you arrive in Malaysia, and are chargeable to tax in the year of arrival you have to write to the D.G. within one month of your arrival and tell him that you are now in Malaysia and earning income, and in any other case you have to inform him by 14th April.

3. FORM "B"

This form is accompanied by a set of very clear explanatory notes which you should read most carefully. You may ask why you should read this chapter we have written, if those notes are very clear. Well we hope to explain them in a greater detail but even more important we intend to give some clarification so that you become aware of your full rights under the Act, and if you care to, you can exercise these rights. We intend to try and explain also the effects of certain decisions you can take, on your tax position, so that this subject which misleads most people becomes familiar to you, and you can make decisions having all the tax-facts in mind.

This Form B is the device by which you give the D.G. information about the fruits you obtain from the various trees. You are required to give accurate information about your income on this Form B, so that the D.G. can assess you on your income

and tax you on it. There are penalties for making even simple mistakes in filling-up the form, and there are very severe penalties for deliberately making false entries to try and evade tax. If you make a mistake by which you pay more tax than you are liable for, there is no certainty that the D.G. will find out your mistake and correct it. This is specially true when you yourself not knowing the law, do not even give him enough information by which he could detect your error.

We have come across a man, who used to ask his clerk to prepare his income-tax return as he himself was very busy. He said he felt he was paying too much tax and did some checking up. To his horror he found that *all* the rent from his properties had been included as income without any deductions for the interest he was paying on the money borrowed to finance the buildings, and without any deductions for the assessments he had paid. Luckily for him he discovered his mistake within 6 years and was able to ask for the mistake to be corrected. This right (under section 131) was explained to him over a casual lunch, and he is now an avid student of income-tax.

So make yourself more aware of your rights by reading and discussion. Even if you cannot save much money yourself, you can still be an informed guide to your friends. Finally you may even become intellectually involved and enjoy it as a serious pursuit.

4. NINE SOURCES

We will discuss first the nine sources of income you are required to put down in Form B.

If you are reading the notes at the same time you will soon find out why you should read this chapter as well. (A reader with no interest in any one source should skip to the next one.)

5. SOURCE ONE AND TWO—PROFITS OF TRADE, BUSINESS, PROFESSION OR VOCATION, SOLE TRADER AND PARTNERSHIP

For full details on how to calculate these read Chapters XI and XII. For now we will assume that you have available the business accounts which tell you what this figure is. Before writing down the figures you have been given into Form B (A1 and A2) check over the following points:

- (a) If you personally borrowed money to put into the business check if the interest on this money has been deducted. If not on a separate sheet of paper deduct this. In this as in every other case you should try and give the full details to the D.G. and give him copies of any receipt, contract or other document so that he can confirm any matter without further correspondence.

- (b) If you have a private car or other equipment which is used for the business purpose even some of the time, (if it is used wholly for the business it should be charged in the business accounts) you can deduct a proportion of the cost of repairs, road tax, insurance, renewal and a capital allowance from the profit of the business, *to the extent* that you can prove that these were wholly and exclusively for the business purpose.

This is not as crazy as it sounds. A part of a whole *can* be, and has been said to be, wholly and exclusively used for a purpose, if such part can be ascertained with a reasonable degree of certainty.

In the case of a car for instance you should keep a record of your use of the car on business purposes. Suppose your record shows that the car was used 10,000 miles on a business purpose and 20,000 for private purposes. Then you can deduct $\frac{10,000}{30,000}$ of the car expenses from your business profit.

Having employed part of the vehicle for a business purpose you should also be able to claim capital allowances for the vehicle. This consists of an initial allowance of 20% in the first year followed by 20% on the reducing balance every year but the annual rates depend on the type of asset. Of course in the above example you will only be able to claim that part of these allowances devoted to the business.

In the case of other equipment too, repairs etc. can also be proportionately claimed. Also if these are small articles not claimed under capital allowances when they are completely worn out and you have to 'renew' them by buying new ones, the business proportion of the whole cost of the renewal can be deducted.

- (c) If you personally entertained your business clients at home or outside and assuming that these expenses have not been charged as expenses in the business accounts already, you can deduct these expenses. This can happen when you invite people home and do not charge the business. Again we must stress that YOU must be able to prove that these expenses were incurred and that they were for a business purpose. In most cases an itemised statement, guest list, bills etc. will suffice. Where you invite or entertain some business clients for a business purpose and also others you can claim the portion of the expenses for the former e.g. if 40 guests are invited to your house and 25 are invited say to encourage them to patronise your shops by showing them samples etc. and your bills for the expenses are \$800/- you can claim $\frac{25}{40} \times \$800 = \500 .

It may be argued that you and your wife and family also partook of the food etc. and you are not among the 40 above i.e. that the figure of 40 should be increased. In our opinion these expenses are also allowable as your family would not have incurred them unless you were pursuing a business motive.

(d) If an ascertainable portion of your residence is devoted to a business purpose—e.g. guest rooms used for business visitors, a store for business goods, a room used as a part of a manufacturing process, a part of the compound used to store business vehicles etc., then the expenses attributable to this part can be deducted. These include assessment, rent, repairs, electricity, water, gas, and all other expenses of maintaining the premises. In the case of guest rooms a proportion of the salary of the servants, cooks maid, etc. may also be claimed.

The principle remains the same. Where any expense can be ascertained with a reasonable degree of certainty to have been incurred wholly and exclusively in the earning of income from the business—it can be deducted. The onus of proof is on you, but all you are usually required to do is give reasonable proof of the facts.

Having done all the above you should prepare a statement in the following way to attach to Form B.

Income from (a) Sole-Proprietorship and/or (b)

	(a)	(b)
	\$	\$
Partnership	X	X ¹
Less: Expenses as below: ..	Y	Y ¹
(a) See attached No. 1 .. — —		
(b) See attached No. 2 .. — —		
(c) See attached No. 3 .. — —		
(d) See attached No. 4 .. — —		
	<hr/>	<hr/>
Total deduction claimed ..	Y	Y ¹
	<hr/>	<hr/>
Income from business profession or vocation	X—Y	X ¹ —Y ¹
	<hr/>	<hr/>

(Form B Reference—A1 and A2)

Note (a) to (d) refer of course to your additional documented expenses as explained in this section

6. SOURCE THREE—EMPLOYMENT

Most of the taxpayers fall into this category, and the income from this source is well documented. Your employer is required to give you a proper return in a specified form.

Begin by checking if the figures here are correct. Mistakes can and do occur so test the details with what you can remember about your salary etc. e.g. if your salary is about \$1,000 per month the figure for this should be about \$12,000 if you have worked a full year. Again your E.P.F. contribution should be 10% (or such other rate as applicable) of your emolument so test-check if this is correct.

(i) What can be Deducted?

We have discussed this in great detail in Chapter VIII but shall repeat here briefly.

General

Any expense wholly and exclusively incurred in the earning of the income from employment can be deducted (section 33). This does not include the food you eat, the ordinary clothes you wear, the expenses of travel to your place of work and other expenses that *put you into a position to earn income*.

The items below however are allowable if you can prove them by means of reasonable evidence. (Receipts, bills, tickets etc. are evidence but in some instances where the circumstances are such that it would be unreasonable to expect such documents to be available, your own statement as to certain expenses can be accepted if it is reasonable).

(ii) Deduction from Accommodation provided and Benefits in Kind

Besides the general authority of section 33; section 38 gives the authority for the deductions allowed to find the adjusted income from employment. The form supplied by your employer sets out the particulars, but you should check this firstly for accuracy and secondly you should ensure that certain deductions allowed are deducted before entering the *net* amount here as follows:

- (a) If the value of furniture has been added to your gross income: any rent paid by you for it.
- (b) Where the value, at unfurnished rates, of accommodation, has been added to your gross income:
 - (i) any rent paid by you;
 - (ii) any expenditure by you on public rates, insurance and repairs which you are legally required to meet as a condition of the occupation of that accommodation.

These should be listed in detail on a separate sheet of paper with supporting documents. [These deductions cannot exceed the gross income for tax-purposes, and they must be apportioned if they cover a different time period from that of the gross income or if they cover the whole premises where the gross income is only for a part.]

(iii) Travelling Expenses

If your work requires that you travel while you are doing your work the expenses, to the extent that you have not been paid back by your employer are deductible. If you

travel by taxi, train or plane then the cost of the ticket, and also the reasonable other expenses, food, hotel, etc. can be claimed. If you use your own car for doing your work as well as your private use you must keep a record of the miles covered on each of the above purposes. Usually you must include the miles from your house to your first place of work and from your last place of work to your house under the private-use column, but where you only use your house as a resting place for your car between business activities you can ask for this to be included in the other column i.e. if you are an inspector of petrol stations and begin visiting petrol stations on your way to your place of work. If you have two sources of income the travel between sources is also for the purpose of acquiring income e.g. a lawyer travelling to court from his office, an employee travelling to his business from his place of employment.

(iv) Renewals and Repairs

Generally even for assets on which capital allowances are not claimable (e.g. because they are used in the production of income from a non-business source) repairs of all such assets used in the production of income are specifically allowable under section 33 (1) (c). (Repairs are of course also allowed on assets for which capital allowances are claimable).

The capital cost of these assets (with the exceptions given below) is allowed on a "renewals basis" i.e. the first purchase is not allowed but when such "implement, utensil or article" is renewed, the cost of renewal is allowed (see example in next subparagraph.)

The following item is specifically *excluded* from a renewal allowance:

"any means of conveyance"

This is specifically excluded in section 33 (1) (c), and means that any car, motorcycle etc. used in the production of income e.g. by a salesman is not allowed on a "renewals basis" as above.

Repairs or renewals which amount to the "cost of reconstructing or rebuilding:

- (i) any premises, building, structures or works of a permanent nature;
- (ii) any plant or machine; or
- (iii) any fixtures;" (extract section 33 (1) (c))

are also not allowed.

(v) Machinery and Fixtures

These (except means of conveyance) wholly and exclusively devoted to the earning of your employment income, where not supplied or paid for separately by the employer, can have, any repairs incurred by you, deducted. In the case of smaller things like "implements, utensils or articles" the expenses of renewal repair or alteration can be deducted. This means that if you buy your own set of tools to do your job you cannot claim this but when the first or subsequent tools are repaired altered or renewed that expense can be deducted.

In our opinion "implements utensils or articles" would cover the following types of things.

Lecturer and Teacher	—Tape-recorder, stop watch, camera, projector, charts and diagrams, typewriter.
Carpenters etc.	—Tools, protective clothing and other equipment.
Insurance Salesman	—Filing cabinet, typewriter, telephone, display material etc.
Social Escort	—Special dresses, cosmetics, jewellery and accessories, car.

The assumption is that these people are "employees" and not exercising a "profession" for tax purposes.

We repeat that the following conditions must be met with:

- Where part only is used such part must be ascertainable.
- It must not have been paid for or supplied by the employer.
- It must not be for putting you in a position to work but must be used in the course of working.

7. SOURCE FOUR AND FIVE—DIVIDENDS, INTEREST OR DISCOUNTS

(i) Local Dividends

Dividends both received or only credited during the preceding year must be included here. The net dividend has to be grossed-up before entering as follows:

$$\text{Net Dividend} \times \frac{10}{9} = \text{Grossed-up dividend}$$

E.g. If you receive or are credited with \$600 then $600 \times \frac{10}{9} = \text{Grossed-up dividend}$.

The reason for this is that the company paying the dividend has already deducted tax at 40%. By multiplying the net dividend by $\frac{10}{9}$ we make it back to what it was before the deduction of tax. You must attach the tax-deduction certificate so that this tax can be credited to you. On the other hand the grossed-up dividend is added to your income. If your marginal rate of tax is less than 40% this represents a "saving" in tax.

No deductions are available from this source on the grounds that dividends are pure income requiring no further exertion or expenditure after the purchase of the shares. Of course interest on money borrowed to purchase that share can be deducted under the authority of section 33 (1) (a) (ii). Dividends from pioneer companies which are exempt should not be included at all.

(ii) Overseas Dividends

Persons ordinarily resident in Malaysia have to include overseas dividends here, but in the case of persons not ordinarily resident only dividends derived from Malaysia

have to be included (see section 14 if you are not sure about the meaning of "derived in Malaysia"). Assuming you are an ordinarily resident person, the overseas dividends fall into two sub-classes:—

- (a) Those from countries with which we have a Double Taxation Agreement.
- (b) Those from other countries.

In the case of the former type the dividends have to be grossed-up and included here. Further treatment depends on section 132 and schedule 7 of the Act and the specific Double Taxation Agreement.

In the case of the latter type of dividend these should be grossed-up and added in here. Normally where foreign tax has been suffered a unilateral credit of half the tax will be granted under section 133 and Schedule 7.

Note

1. Deductions for Bank Charges etc. on Overseas Dividends, Interest or Discounts

These are discussed in Chapter VIII, page 80.

8. SOURCE SIX—RENT ROYALTIES OR PREMIUMS

This kind of income is usually only put in this place in Form B by people who are not doing it as a business i.e. the individual who just rents out his houses.

The expenses which are deductible are:

- Interest
- Repairs
- Maintainance
- Assessment
- Quit Rent
- Fire Insurance Premium

Also the salaries of gardeners, rent-collectors and other related expenses are deductible.

If you furnish some of the properties you can claim second purchases of such items as renewals under section 33 (1) (c). Items under this may be fans, refrigerators, air-conditioners, furniture, lawn mowers and other articles used in getting the income from rent. If your rent collector uses a scooter etc. the expenses of this vehicle can be claimed if they are incurred or reimbursed by you.

If you include here rent derived from renting out an industrial building (it may be better to include this in Source One) you are eligible for the relevant Capital Allowances.

9. SOURCE SEVEN—PENSIONS, ANNUITIES OR OTHER ANNUAL PAYMENTS

There is not much scope for claiming deductions.

10. SOURCE EIGHT—OCCUPATION OF PREMISES

The points to remember are:—

1. One owner-occupied residence is exempt.
2. Un-furnished premises do not have to be included. Section 31 (1) proviso (e).
3. If only a part of the premises is occupied by you, or if you occupy it for only part of the year, only a proportion is to be included.
4. The value to be placed is the rateable value or in its absence the economic rent.
5. If the premises are occupied partly for a business purpose then the amount is to be proportionately reduced. Section 31 (4).

Deductions

1. One owner occupied premises is completely exempt. Even where the husband's and wife's income is aggregated only one is exempted.
2. The general deduction of section 33 does *not* apply to this source but section 37 provides for deduction of:
 - (a) any interest paid to borrow money to purchase the premises;
 - (b) rent, public rates, insurance premiums;
 - (c) repair or maintenance of premises e.g. painting, white-ant service charge, repairs to roof etc. but these repairs etc. should not improve the original condition.

Thus the replacement of a broken cement surface with terrazo is not a repair. Also these expenses must be for the same area and time period as the gross income i.e. if the insurance paid is for 12 months and the gross income is for 6 months then the expense must be reduced to half before deductions.

11. SOURCE NINE—"CATCH-ALL"

This is a catch-all source put in as a legal safe-guard. The thing to remember is that it must be *Income*. Thus if you win some money at poker this is not income. Toto and lotteries and prizes won in the newspaper word puzzles are not income. If you make

some money occasionally by selling some investment you have made, at a profit, this is not income, but if you do any of these too often and do them in a systematic way they may become Income, but in this case you will be able of course to deduct any expenses and losses on sales you would have incurred in earning this income.

12. GENUINE AND LAWFUL CLAIMS

Well reader you have now filled in the Sources of Income where applicable. You have now probably become aware of all your rights regarding what deductions you may make from each of these sources. We hope also you have noted that you need to produce proper documentation or some form of record to back-up every claim. In general as long as the claims are reasonable and set out carefully they are accepted. Unusual claims may require further clarification and explanation by you but if you have kept good records you do not have to worry. May we also remind you of our basic assumption which is that all these claims are genuine and lawful.

13. HOW MUCH TAX MUST I PAY

(i) Losses

It may happen that some of your sources have a minus result i.e. the result is a loss. In such a case you should enter NIL against this source. Do not enter a minus figure. If you have made a loss on source one however consisting of a sole-proprietorship of a profession, business or vocation you should enter this in Form B under B10 attaching the signed accounts. Any partnership losses should be similarly entered in Form B under B11.

(ii) Abortive Mining Expenditure

Money spent by you in trying to discover minerals can be entered here at B12.

(iii) Approved Donations

These will be allowed as deductions if you have any income left after deduction of current year losses from Aggregate Income.

(iv) Initial/Annual/Plantation/Forest Allowances

These can be claimed at Part C of Form B.

(v) What's my Tax?

We shall summarize here the method applied to compute your tax. We shall do it using in the first instance words only, but the illustrations which follow after we discuss personal deductions and tax planning will be in figures.

Tax is charged (except for non-residents) at scale rates which are given on page 297. These rates are applied to what is known as "chargeable income." (This is illustrated in the diagram on page 98.

The gross income from each source is ascertained for the basis period and from this the allowable deductions are deducted giving adjusted income for each source. To the business source only you have to take the additional step of adding balancing charges and deducting allowances (Chapter XVIII) giving Statutory Income. If the adjusted income from a business source is a minus figure (i.e. a loss) then a zero is placed here, hence Statutory Income is always zero or more and never a minus. It is this Statutory Income which you are required to put down in Form B. The summing-up of the Statutory Income from each source results in Aggregate Income but before Aggregate Income is derived, the Statutory Income from business sources is further altered by deducting any unrecouped losses of previous basis years, up to the total of the above Statutory Income from business sources. From this Aggregate Income the current year's business losses are deducted and if any income remains approved donations may be deducted giving Total Income. Chargeable Income is now derived by deducting the personal reliefs allowed to an individual by the Act. Your Income Tax will be based on this Chargeable Income. In addition Supplementary Income Tax is charged on Taxable Tin Profits, Taxable Timber Profit and Development Income. This is added to give Total Tax Charged. If any penalty or tax repaid exists this is added in and the following are deducted if applicable to your case to give Tax Payable.

- (a) Section 130 relief—non resident relief.
- (b) Section 132 relief—double taxation relief.
- (c) Section 133 relief—unilateral relief.
- (d) Section 110 relief—set-off for tax deducted at source on dividends.

[Rates for East Malaysia are 20% lower at each level of income tax.]

14. PERSONAL RELIEFS

These can be deducted from your "total income" according to your personal circumstances:—

(i) Personal Allowances and Earned Income Allowance

These are available for persons who are resident in Malaysia in the basis year, but section 130 should be referred to by those subject to double taxation in Singapore & Malaysia.

Personal Allowance for you is: \$2,000

Earned Income Allowance

Amount available is $\frac{1}{10}$ of earned income or \$1,000 whichever is less where the individual is a bachelor or his wife has no earned income. Where the wife has earned income and it has been aggregated with that of the husband, an additional relief of $\frac{9}{10}$ of her income or \$500, whichever is less, is allowed.

"Earned Income" is defined in Section 18 of the Act. Briefly in the case of an individual it consists of employment, pension and business income. The business income must have been derived by personal exertion and deductions for current year's loss and previous year's unrecovered losses made.

These are added together to calculate this relief. The purpose is to charge slightly less tax on income derived from personal exertion than to income earned otherwise. All other sources e.g. Dividends, Rents etc. are considered to be not income from personal exertion and are not added in when calculating earned income allowance.

Example

A person has income as follows:—

No.	Source	Section 4 in Act Paragraph:	Amount
1.	Trade business profession or vocation (But a loss b/f from previous year is \$8,000)	(a)	\$ 2,000
2.	Employment	(b)	4,000
3.	(a) Dividends (Grossed-up)	(c)	1,000
	(b) Interest etc.	(c)	500
4.	(a) Pensions	(e)	6,000
	(b) Voluntary pension (section 16)	(e)	2,000
5.	Rent etc.	(d)	5,000
6.	Miscellaneous	(f)	500
			\$21,000

The Earned Income Allowance is calculated as follows:

No. 1	.. .. .	\$2,000
Less: Deduction for section 43 (2)	.. .. .	2,000
No. 2	.. .. .	\$ 4,000
No. 4 (a)	.. .. .	6,000
No. 4 (b)	.. .. .	2,000
		\$12,000

$\frac{1}{10} \times \$12,000$ is \$1,200 so the relief is \$1,000.

- Note 1.** If you wish to claim this relief you must be a resident and the business income included in earned income must be from a business where you are personally involved. *E.g.* if you were a sleeping (i.e. inactive) partner it would not qualify as earned income (section 19 (6)). This qualification does not extend of course to a pension or voluntary periodic payment which is considered earned income in every case.
2. If in the above example \$1,000 of the pension was the wife's income aggregated with that of her husband, an additional earned income relief of \$500 would be available to the husband.
- $(\frac{9}{10} \times \$1,000 = \900 so the lesser amount of \$500 is allowed to the husband. Also his earned income would be \$11,000 so he still gets \$1,000).

(i) Wife, Alimony, Separation (Maximum \$1,000)—Section 47

An individual resident in Malaysia during the basis year who had his wife living together with him the whole year is allowed \$1,000. If he is divorced or separated from her say for half the year then he is only allowed a portion—in this case \$500. However if he is paying his legally separated or divorced wife alimony or maintenance he can claim this but the aggregate claim for any individual cannot exceed \$1,000. ("Wife" includes wives and secondary wives).

(iii) Child Relief — Section 48

The following children of an individual resident in the basis year who maintains or partly maintains them at any time in that year are eligible for this relief:

- (a) Unmarried and under sixteen in the year preceding the year of assessment.
- (b) Unmarried of any age receiving at any time in the preceding year full-time instruction at any University, College, School etc.
- (c) Unmarried of any age serving under articles etc. to qualify in a trade or profession, or studying part-time for that trade or profession.

The relief among the eligible children is:

First eligible child	.. .. .	\$750
Second and Third eligible child	.. .. .	500 each
Fourth and Fifth eligible child	.. .. .	300 each

Additionally if any child over 16 is receiving full-time education at a college, university or other similar institution of higher education (this would appear to exclude a school), or serving articles outside Singapore and Malaysia you can ask the D.G. to give you relief for actual amounts spent by you directly on his maintenance and education. The maximum for this is double the above rates e.g. if it is a first eligible

child studying overseas the maximum is $\$750 \times 2 = \$1,500$ and if it is a fourth child $\$300 \times 2 = \600 . A similar double relief is available to a resident of East Malaysia whose child is receiving full-time education or serving articles in Singapore or West Malaysia.

But no deduction is given for any child who is receiving any income of his own which exceeds the deduction allowed under section 48 or is working at any job not connected with his articles. [A recent Singapore case (Appeal No. 4 of (1968) decided that the phrase "appropriate deduction" there meant the scale where the first child gets \$750 etc. and not the one where it can be multiplied by two. So in Singapore if the first (i.e. oldest) child has an income of \$751 on his working at a job the parent is not allowed to claim the \$750 allowed above.] Such a child is not considered in the order of children. This has an interesting effect, for if the eldest is not considered in the order anymore your second child becomes the first child, and so on. To understand this point we must realize that this scale above is *not* arranged in the order of *age* only. Thus the oldest child may get married, or although single and under sixteen get a job or be over sixteen and not studying or have his own income of \$750 or more. In each case he is not considered in the order and the next one can then be the "first" child. This works for any child e.g. if the third oldest child marries or has income over \$500 the fourth oldest moves up to take his third place.

To sum up if any child does not need your support because of reasons of age, marriage, having own income, or having a job then the next child takes the place in the scale given.

Sometimes in divorce or separation, if both parents are qualified and want to claim this relief, the relief is appropriated according to the amount spent on the child by each person. The maximum relief is still the same.

A child for the purpose of child-relief includes a legitimate child, step-child or a child proved to the satisfaction of the D.G. to be a legally adopted child.

(iv) Relief for Insurance, Deferred Annuity, and Approved Fund Payments—Section 49

These are allowed up to a maximum of three thousand dollars but there are certain conditions attached to each which must also be complied with before a claim can be allowed.

(a) Approved Funds

An approved scheme "is one approved by the D.G. under section 150 of the Act". Also included are payments made under any other law to widow's and orphan's pensions or approved scheme. The following conditions must additionally be fulfilled.

The contributions must be "obligatory by reason of any contract of employment" or by the rules of the fund or society i.e. you must be making these payments by compulsion and not by choice.

In certain funds you **MUST** contribute say 10% but you **MAY** contribute another 5%. Only the 10% is allowed.

The amount of contributions by you as an employee can be found from your copy of the form supplied by your employer to the D.G.

(b) Insurance or Deferred Annuity

It can be with any company—foreign or local but the following conditions must exist:

- (i) It must be on your life or on your wife's or husband's life, or on the joint life of spouses. A policy on your child's life or some other policy will not qualify.
- (ii) The premium is allowed only up to 7% of the fixed capital sum payable on death in the basis year exclusive of bonus etc. e.g. if you have a policy for \$10,000 and are paying \$2,000 premium per year (perhaps because it is only for seven years or because you are a bad risk) only 7% of \$10,000 is allowed i.e. \$700.
- (iii) If two individuals are entitled and want to claim relief on one policy then each claimant is entitled to:

$$\frac{\text{premium paid by claimant}}{\text{total premium paid}} \times 7\% \text{ of capital sum}$$

If in the above example a separated wife had paid \$500 of the \$2,000 premium, she can claim $\frac{500}{2,000} \times \$700 = 175$; and the husband can claim $\frac{1,500}{2,000} \times \$700 = \$525$

15. TAX PLANNING FOR PERSONAL RELIEFS

We have heard remarks like: "Take out insurance and you can deduct it from tax", and we have read books which talk of "tax-deductible items" so frequently, that we feel it would be useful to clarify this. The person taking out an insurance or marrying or taking any other action which entitles him to a deduction, allowance or relief under the Act benefits, but this benefit is NEVER a hundred percent. No one can take out insurance and deduct it from tax because in Malaysia the maximum rate of income tax is only 50% or with the Supplementary Income Tax perhaps up to 70%, but theoretically it can never reach 100%. If a person paying tax at the maximum rate of tax takes out an insurance policy and pays a premium of \$4,000 it MIGHT mean that he saves 50% of this i.e. \$2,000 but this is the maximum he can save. Also relief is only available if he satisfies the other conditions with regard to personal reliefs available to him.

This illustrates the point that the amount of tax saved by any action depends in each case, firstly on whether this action in fact entitles the person to any deduction and if the answer is "yes", secondly on the *marginal rate of taxation* of the person. Assuming that the first condition has been fulfilled we will illustrate the effects of the marginal rate of taxation.

Illustrative Example

(We shall ignore Supplementary Income Tax)

Question

Assuming that an expense of \$4,000 is allowable in all other respects what income tax is saved by a person having a chargeable income of:

- (a) \$10,000
- (b) \$15,000
- (c) \$17,000
- (d) \$37,000
- (e) \$150,000
- (f) \$20,000,000

Tax saved can be calculated from the table of rates of taxes (see page 128).

(a) The chargeable income before the action is ..	\$10,000			
And the tax on this is				\$1,050
The chargeable income after the action is ..	6,000			
(\$10,000 — \$4,000) and the tax on this is ..				495
				<hr/>
<i>Answer:</i> Tax saved is				555
				<hr/>
(b) Tax on \$15,000 is				2,050
Tax on \$11,000 is				1,250
				<hr/>
<i>Answer:</i> Tax saved is				800
				<hr/>
(c) Tax on \$17,000 is				2,510
Tax on \$13,000 is				1,650
				<hr/>
<i>Answer:</i> Tax saved is				860
				<hr/>
(d) Tax on \$37,000 is				8,250
Tax on \$33,000 is				6,850
				<hr/>
<i>Answer:</i> Tax saved is				1,400
				<hr/>

(e) Tax on \$150,000 is	..	..	..	63,450
Tax on \$146,000 is	..	..	..	61,450
<i>Answer:</i> Tax saved is	..	..	..	<u>\$2,000</u>

(f) Answer is same as (e) because here we have reached the maximum rate of 50%.

Thus we see that the tax saved depends on the chargeable income of the person. Where this is larger the person is paying tax at a higher rate and his saving is more.

To sum up, nobody can incur an expense and *deduct* it from tax. However when trying to make a decision as to whether to do something or not, the tax effect depends on the circumstances e.g. in (a) above the person may spend \$4,000 at a discount of \$555 i.e. over the whole year he pays out of his pocket only \$3,445 while "spending" \$4,000. This is perhaps the best way to think of it: as an expense at a discount. The "discount" of course is the tax saved. This depends on the marginal rate of tax. A last word: you are still out-of-pocket by the amount *not* saved.

This principle also applies if you are trying to decide whether to earn more money e.g. a person paying tax at 20% is asked to do an extra job which will pay him \$500. Of this amount he will get only \$400 for himself or even slightly less if this moves him to a higher rate. Yet no matter how high a rate of tax you are paying, you do get some money in.

16. WEST MALAYSIAN CREDIT (SABAH CREDIT, SARAWAK CREDIT)

The previous paragraph may have been too much like bad news to some readers so perhaps it is time to give the reader some good news. There is a possibility of getting some money back from the D.G. or at least getting a tax-credit to offset what you owe him.

This arises from changes in the law into which we do not intend to delve here. The effect is that a person is able to claim the whole or a part of the tax paid by him in the year of assessment 1967 on the happening of any of the following events:

- (a) He reaches the age of 55.
- (b) He is a non-Malaysian Citizen leaving Malaysia who
 - (i) has no papers enabling him to return;
 - (ii) has no likelihood of being resident in next 5 years;
 - (iii) has no income after departure except dividends, interest, pension or leave pay from employment, which will cease on end of leave.
- (c) He satisfies the D.G. that for at least 12 months he was prevented by serious disability from following a gainful employment and had no source of income;

- (d) He satisfies the D.G. that his only source is, and will continue to be, a pension derived in Malaysia.
- (e) He satisfies the D.G. that he was not entitled to this credit before 1.1.1988.
- (f) His death. In this case this credit will be given on his behalf to his executor.

A similar credit is available for those who paid income-tax in the year of assessment 1967 in Sabah or Sarawak.

17. HUSBAND AND WIFE (SECTION 45)

(i) Residence and Citizenship

Where an individual and his wife or wives were living together in the basis year the total income of the individual is deemed to include the total income of his wife or wives.

The question of when this aggregation is applied is answered in Section 45 (2) so that a wife's total income is aggregated to her husband's for a year of assessment if:

- “(a) both were residents for that basis year;
- (b) both were not resident for that basis year and both were citizens at some time in that basis year;
- (c) both were not resident for that basis year and neither was a citizen at any time in that basis year;
- (d) he was resident and she was not resident for that basis year and she was a citizen at some time in that basis year; or
- (e) she was resident and he was not resident for that basis year and he was a citizen at some time in that basis year.” (Section 45 (2))

From the above it is clear that a wife's or husband's income will not be aggregated in the following instances:

- (a) Mr. Johnson is a resident of Malaysia but not a citizen in the year ended 31.12.1971. He is getting a salary of M\$36,000 p.a. in Malaysia. His wife Joan is working in Australia and getting there a salary of M\$24,000 p.a. She is not a citizen of Malaysia nor a resident. Joan's income of \$24,000 will not be aggregated with Johnson's income of \$36,000 for the Y/A 1972.
- (b) Noor-e-hayati wife of A. White is a resident of Malaysia in 1970 but not a citizen. Her husband A. White is working in U.K. at a salary of M\$36,000 p.a. He is not a citizen of Malaysia. Noor-e-hayati's income (if any) in Malaysia from employment and other sources will not include A. White's salary in U.K.

The positions will be reversed in (a) and (b) above if Johnson and Noor-e-hayati are citizens of Malaysia or Joan and A. White are citizens of Malaysia.

"Living together" is defined in section 19 (2) "... an individual and a wife of his shall be treated as living together unless—

- (a) they are separated under an order of a court or under a deed of separation or a written agreement for separation; or
- (b) they are in fact separated in such circumstances that the separation is likely to be permanent." (Extract from Section 19 (2)).

(ii) Income to be Aggregated

Where at any time in the basis year for a year of assessment the husband and wife are "living together" and do not cease to live together the income of the wife is aggregated to that of the husband for the year of assessment, e.g.

- (a) Mr. Tan marries Miss Leow on 1.7.1969. The entire earnings of the wife in 1969 is aggregated to the husband in y/a 1970 (1969 is basis year for the year of assessment 1970).
- (b) They separate by court order on 29.2.1972. The entire earnings of the wife in the basis year 1972 will *not* be aggregated with the husband in the year of assessment 1973, for they ceased to live together in the basis year. The death of a spouse has the same result.

18. RELIEF FOR ERROR OR MISTAKE—SECTION 131

The reader who becomes aware that he has not availed himself of his full rights as set out in this book e.g. he may not have claimed some deduction he was entitled to, can now apply for relief under Section 131. This must as nearly as possible be in the same form as an appeal, and similar provisions apply as to an ordinary appeal to the Special Commissioners (Chapter III). However in this matter as in many others the reader should be guided by a careful consideration of pros and cons, not hesitating to seek further advice where the amount is considerable or the issue complex. We set out in summary form the provisions of the Act on this matter.

1. The error or mistake must be in a return, e.g. failure to claim a relief; or a supporting schedule e.g. statement of accounts.
2. The application must be made within 6 years of the end of the year of assessment when the error or mistake occurred.
3. The assessment for the period covered by the return having the error or mistake, should not have become "final and conclusive" (see page 14 for meaning of this term) at the time the return was made.

- One kind of error and mistake, is specifically excluded—i.e. if you did not claim the relief for one residential premises as allowed under section 128 you are prohibited from claiming an "error or mistake relief" by section 128 (5).
- Also if subsequent changes in the practice of the D.G. make the earlier practice less favourable to you, such earlier returns cannot be reviewed, on these grounds.
- Finally the D.G. is required to examine all relevant circumstances of the case, and particularly whether such relief will exclude any income of the applicant from tax, and such enquiry may cover other years of assessment.

REVISION QUESTIONS

The Worked Solutions are given below

1. Mr. Romi Mistry age 58 years and single has the following income during the year ended 31st December, 1972. He retired from employment on 1st July, 1972.

Pension (\$500 p.m.) (1.7.1972 to 31.12.1972)	..	..	..	..	\$3,000
Employment Income	..	..	..	..	6,000
Retirement Gratuity	..	..	..	..	72,000

Interest:

P.O. Saving Bank	..	..	..	..	1,000
Fixed Deposit	..	..	..	..	2,000
Annuity (from father's estate)	..	..	..	..	1,000

Assuming he has a life insurance policy of \$10,000 on which he paid a premium of \$1,000 and contributions to approved funds of \$600, compute the amount of income tax payable by him for the year of assessment 1973, assuming his retirement gratuity was from an employer he has worked with for 20 years.

2. Mr. Soul age 56, and a widower has the following income during the year ended 31.12.1971. He has no children to maintain and has no E.P.F. or insurance policy.

Royalties (in respect of books he wrote)	..	..	..	..	\$5,000
Rents from properties	..	..	..	..	7,000
Coffee money on letting out a house belonging to him	..	..	..	..	5,000

Dividends:—

	Gross	Tax	Net
Moor Ltd.	\$1,000	400	\$ 600
Sona Ltd.	Tax free		600
Royal Ltd.	Exempt from tax		1,200
			<u>2,400</u>
			<u>\$2,400</u>

Compute the aggregate of income tax & development tax payable by Mr. Soul, for the year of assessment 1972.

3. Mr. Gan Ah Nee married Miss Joan Wee in Malaysia on 1st July, 1972. Their income is as follows:—

Y/e 31.12.71 Y/e 31.12.72

Mr. Gan

Salaries	..	\$ 8,000	\$10,000
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Interest:

P.O. Saving Bank (Credited on 31.2.1971)	..	500	600	(Credited on 31.12.1972)
Fixed Deposit (Credited on 30.6.1971)	500	500	(Credited on 31.12.1972)

Miss Wee

Salaries	10,000	10,000	
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Dividends:

Exempt Pioneer Companies (net)	600	600	
Other Malaysian companies (gross). (Dividend received on 30.6.1971)	1,000	2,000	(Dividends received 31.12.1972)

Both Mr. Gan and Miss Joan Wee are residents of Malaysia and have to contribute to E.P.F. at the rate of 5% p.a. They have no insurance policies.

Compute income tax payable for the relevant years by Mr. and Mrs. Gan.

4. Mr. Chiam a bachelor has been the Sales Manager of Asia Trading Company Ltd. since 1954. Details of remuneration payable to him for the year ended 31st December 1972 are given below:—

A basic salary of \$1,500 p.m.

Commission of \$2,500 for the year.

Bonus—12½% of basic salary.

Travelling allowance at \$200 per month.

Entertainment allowance \$1,500 per year.

It was proved to the satisfaction of the D.G. that \$385 of the travelling allowance had been expended for business purposes, \$240 for travelling between hotel and office and the balance for private and domestic purposes.

In respect of travelling allowance the following was agreed between Mr. Chiam and the D.G.

(a) Lunches and dinners for customers on official business \$250.

(b) Private dinner parties for personal friend and family \$340.

(c) Balance not expended.

Lodging in a first class hotel at \$500 p.m., which is given to him as a Cash allowance.

Meeting allowance—\$100 for the year plus another \$25 for every meeting attended. Mr. Chiam attended 9 meetings during the year.

- (a) You are required to ascertain the statutory income for Mr. Chiam for Year of Assessment 1973.
- (b) What would be the difference in liability if lodging had been provided in kind?
Mr. Chiam was married in January 1st 1973 and his wife had an income of \$12,000 from rent in b/y 1972.
5. Mr. Teo commenced employment as an Assistant in Master's International Ltd. on 1st Jan. 1972, and was paid as follows:—
Salary — 1972 (\$14,400); 1973 (\$15,600).
Commission—10% on gross receipts from customers introduced by Mr. Teo.
Bonus—\$1,200 plus 1% of the net profit for each year after providing for depreciation of assets.

In addition a residence (defined value \$4,800) was provided by the company together with Furniture—Total value of benefit from furniture agreed with the D.G. \$600 p.a. (shared 50% with another Assistant).

Refrigerator—Total value agreed with the D.G. \$40 p.m. (shared with another Assistant).

Air-conditioning—Total value agreed with the D.G. \$20 p.m. (not shared).

Cooker—Total value agreed with the D.G. \$6 p.m. (shared with another Assistant).

The residence provided by the Company was occupied by Mr. Teo and another assistant each of whom paid \$20 p.m. to the Company as rent for such residence provided.

For the year ended 31st December, 1972, the gross receipts from customers introduced by Mr. Teo amounted to \$22,800 and the net profit was \$100,600 before providing for depreciation which amounted to \$3,200. For the year ended 31st December, 1973, all these were increased to \$24,000, \$120,000, and \$4,000 respectively.

(a) Ascertain Mr. Teo's statutory income (if any) for the Years of Assessment 1972, 1973 and 1974.

6. Mr. Lee commenced his appointment as Sales Representative in Mombo Limited on 1st April 1972 at a salary of \$15,600 p.a. with an annual increment of \$4,800 p.a. after each complete year of service.

He was entitled to bonus of \$9,000 for the nine months ended 31st December 1972 but received payment on 31st March 1973. A commission of \$3,000 in respect of the year 1972 was also received in 1973. It is to be assumed that he was entitled to the commission at 31st December, 1972.

The commission for 1973 also remained at \$3,000 and the bonus for 1973 was \$3,600 but was received on 31st March 1974.

The company provided Mr. Lee with a bungalow the defined value of which was \$3,600 and for which he paid to the Company a nominal rent of \$80 per month.

The following benefits were enjoyed by Mr. Lee at the expense of the Company. It was agreed that the Company's car was also used for private purposes to the extent of one-third of the total mileage covered.

Television	..	..	..	..	\$ 9 per month
Furniture	..	..	..	..	5 per month
Refrigerator	..	..	..	..	15 per month
1 Air-conditioner	..	..	..	..	10 per month
3 Fans each at	..	..	..	..	2 per month
Driver's salary	..	..	..	..	90 per month
Car maintenance expenses	..	..	..	..	4,500 per month

Mr. Lee also received dividends from the following Companies:—

Name of Company	Date Declared Payable	Date Received	Amount
P.Q. Ltd. Malaysia	31.12.1972	21.1.1973	\$1,800 after tax
TOBA Ltd. Malaysia	1.11.1973	1.12.1973	\$1,200 after tax
COCA Ltd. Malaysia	1.11.1973	4.11.1973	\$3,000 after tax

- (a) What would be the amount of Mr. Lee's statutory income for each of the years of assessment 1972, 1973, and 1974?
- (b) What would be the amount of his statutory income if he permanently ceases to carry on employment on 31.12.1973?

**WORKED SOLUTIONS TO REVISION QUESTIONS
ON PERSONAL INCOME TAX**

Question 1**Mr. Romi Mistry****Computation of Income Tax Payable for Y/A 1973**

Pension - - - - -		\$ 3,000
Employment income - - -		6,000
Interest:		
P.O. Savings Bank - - -		1,000
Fixed deposit - - - - -		2,000
Annuity - - - - -		1,000
Aggregate Total Income - -		\$13,000
Deductions for Personal Allowances:		
Self - - - - -		\$2,000
E.I.A. - - - - -		900
Life Assurance - - - - -	\$700	
Approved Fund - - - - -	600	4,200
Chargeable Income - - - - -		\$8,800
Income Tax on first 7,500 - - -		675
Income Tax on next 1,300 @ 15% -		195
Income Tax payable - - - - -		\$870

- Note:** 1. Gratuity of \$72,000 is exempt from tax (Schedule 6, paragraph 25 (1) (b)).
2. Insurance premium is allowed up to $7\% \times 10,000 = \$700$.

Question 2

Mr. Soul

Computation of Income Tax Payable for the Y/A 1972

Royalties - - - - -		\$ 5,000
Development income:		
Rents from properties - - - - -	\$7,000	
Coffee money from properties - - - - -	5,000	12,000
	<hr/>	
Dividends (gross):		
Moor Ltd. - - - - -	\$1,000	
Sona Ltd.* - - - - -	1,000	2,000
	<hr/>	
Aggregate Total Incomes		\$19,000
Deductions for Personal Allowances:		
Self - - - - -		2,000
		<hr/>
Chargeable Income - - - - -		\$17,000
	<hr/>	
Income Tax on first \$15,000 - - - - -	\$2,050	
Income Tax on next 2,000 @ 23% - - - - -	460	
	<hr/>	
		\$2,510
Development tax @ 5% on \$12,000 - - - - -		600
		<hr/>
		\$ 3,110
Less: Tax deducted at source from dividends - - - - -		800
		<hr/>
Tax Payable - - - - -		\$ 2,310
		<hr/>

* 'Tax Free' dividend has to be grossed up.

Question 3

Years of Assessment	Mr. Gan		Miss Wee	
	1972	1973	1972	1973
Salaries: Self - - - - -	\$8,000	\$10,000		
Miss Wee - - - - -		10,000	\$10,000	—
Interest:				
P.O. Savings Bank - - - - -	500	600		
Fixed Deposit - - - - -	500	500		
Dividends (gross):				
Miss Wee - - - - -	—	2,000	1,000	—
	<hr/>	<hr/>	<hr/>	
Aggregate Income - - - - -	\$9,000	\$23,100	\$11,000	—

Deduct personal Allowances

Self - - - - -	\$2,000	\$2,000	\$2,000	
E.I.A. - - - - -	800	1,000	1,000	
Wife's E.I.A. - - - - -	—	500	—	
Wife - - - - -	—	1,000	—	
E.P.F. - - - - -	400	3,200	1,000	5,500
				500
				<u>3,500</u>
Chargeable Income - - -		<u>\$5,800</u>	<u>\$17,600</u>	<u>\$7,500</u>
Income Tax Thereon:				
On the first 5,000 - - -			\$15,000	\$7,500
		= 375	= 2,050	= 675
On the next - - - 800 @ 12%		96	2,100	
			@ 23% = 483	
				<u>—</u>
Income Tax Chargeable - - -		<u>471</u>	<u>2,533</u>	<u>675</u>
Less Tax deducted at source from dividends - - - - -		—	800	400
				<u>400</u>
Income Tax Payable - - -		<u>\$ 471</u>	<u>\$1,733</u>	<u>\$275</u>

Question 4 (a)

Mr. Chiam

Computation of Statutory Income for the Y/A 1973

Salary - - - - -			\$18,000
Commission - - - - -			2,500
Bonus 12½% of 18,000 - - - - -			2,250
Travelling allowance - - - - -			2,400
Entertainment allowance - - - - -			1,500
Lodging 500 × 12 - - - - -			6,000
Meeting Allowance - - - - -			325
			<u>\$32,975</u>
Less: Deductions allowed for Travelling on business - - -		385	
Entertainment of customers - - - - -		250	635
			<u>635</u>
Statutory Income from employment - - - - -			<u>\$32,340</u>

Question 4 (b)

If lodging was provided in kind (i.e.) money paid direct to the hotel by the Company.

Statutory income as above - - - - -		\$32,340
Less: Cash allowance for lodging - - - - -		6,000
		<u>\$26,340</u>

Add: Lodging in a hotel

The amount will be lesser of \$6,000 or 3% \$26,340 i.e.

\$790 - - - - - 790

Statutory Income - - - - - \$27,130

Note: Marriage does not affect the income for the Y/A 1973.

Question 5

Mr. Teo

Computation of Statutory Income for the

Y/A	1972	1973	1974
Basis period - - - - -		1.1.1972 to 31.12.1972	1.1.1973 to 31.12.1973
Salary - - - - -		\$14,400	\$15,600
Commission 10% of \$22,800 -	—	2,280 10% of \$24,000	2,400
Bonus			
Net Profit - - - - -	\$100,600		\$120,000
Less: Depreciation - - - - -	3,200		4,000
	<u>\$97,400</u>		<u>\$116,000</u>
1% thereof - - - - -	\$974		\$1,160
Add: - - - - -	1,200	2,174	1,200
	<u>\$18,854</u>	<u>\$18,854</u>	<u>\$20,360</u>

Benefits in kind

Furniture $\frac{1}{4}$ of \$600 - - - - -	\$300		
Refrigerator $\frac{1}{4}$ of 40 × 12 - - - - -	240		
Air. Con. \$20 × 12 - - - - -	240		
Cooker ($\frac{1}{4}$ of 6) × 12 - - - - -	36	816	816

Residence:

$\frac{1}{4}$ of D.V. \$4,800 or		$\frac{1}{4}$ of D.V. \$4,800 or	
20% of 18,854		20% of 20,360	
$\frac{1}{4}$ D.V. - - - - -		2,400 $\frac{1}{4}$ D.V.	2,400
		<u>\$22,070</u>	<u>\$23,576</u>
Less: Rent Paid - - - - -		240	240
		<u>\$21,830</u>	<u>\$23,336</u>

There will be no income for the Y/A 1972.

Question 6 (a)

Mr. Lee

Computation of Statutory Income

Basis Period	Y/A 1972 y/e 31.12.1971	Y/A 1973 y/e 31.12.1972	Y/A 1974 y/e 31.12.1973
Employment			
Salary - - - - -	—	\$11,700	\$19,200
Bonus - - - - -	—	9,000	3,600
Commission - - - - -	—	3,000	3,000
		<u>\$23,700</u>	<u>\$25,800</u>
Residence:			
D.V. - - - - -		\$3,600	
For 9 months - - - - -		2,700	
or 20% of 23,700 i.e. whichever is less - - - - -		4,740	
			2,700
D.V. - - - - -		3,600	
or 20% of 25,800 i.e. whichever is less - - - - -		5,160	
			3,600
Benefits in kind for a year			
T.V. - - - - -		\$ 108	
Furniture - - - - -		60	
Refrigerator - - - - -		180	
Air-conditioner - - - - -		120	
Fans (3) - - - - -		72	
Driver's salary - - - - -		360	
Car $\frac{1}{3}$ of \$4,500 - - - - -		1,500	
		<u>\$2,400</u>	
Benefits for 9 months - - - - -		\$ 1,800	
Benefits for 12 months - - - - -			2,400
		<u>\$28,200</u>	<u>\$31,800</u>
Less: Rent paid - - - - -		720	960
S.I. from Employment - - - - -		<u>\$27,480</u>	<u>\$30,840</u>
Dividends (gross):			
P.Q. Ltd. - - - - -		\$ 3,000	—
Toba Ltd. - - - - -			\$ 2,000
Coca Ltd. - - - - -			5,000
S.I. from Dividends - - - - -		<u>—</u>	<u>\$ 7,000</u>
Aggregate income - - - - -		<u>—</u>	<u>\$37,840</u>

Question 6 (b)

There will be no difference except that he can claim a West Malaysian Tax Credit if he is over 55 years of age and paid the relevant income tax for the Y/A 1967.

CHAPTER XI

GENERAL RULES FOR ASCERTAINMENT OF ADJUSTED INCOME — SOLE TRADER

Preliminary Note

In Chapter X we discussed how an individual is charged on his income tax from all sources and how he should fill in his Form B but there we assumed that the amount of his income from a business source had been supplied to him. In this and subsequent chapters we shall try to illustrate how this figure is arrived at by different sorts of enterprises. In this first section on a sole trader however we shall include a set of general rules which can be used for all sorts of enterprises.

Before we do this it should be stressed that accountancy principles are not wholly recognized by the Act, but for accountancy students the analogy of the Bank Reconciliation Statement may be useful to understand the process. The computation to be based on the commercial accounts to derive the income for tax purposes (i.e. adjusted income) is similar in principle to a Bank Reconciliation Statement which begins say with the cash book balance and arrives at the bank balance. The student should recall that the rules for adding and subtracting, reverse signs depending on whether the opening balance is a debit or credit balance; a similar convention is necessary for the tax computation. Essentially we take a commercial account and re-do it according to taxation principles. After reading the rather comprehensive rules the reader may feel that it is probably simpler to do them over again but in most cases this would be undesirable because only some of these rules are applicable in a particular case and also the commercial accounts are usually a truer reflection of the state of the business, even if not statutorily required to be kept in that way in every case.

Our plan in this chapter is to first give the Rates of Income Tax applicable in each case followed by a discussion of the General Rules. We end this chapter with comprehensive illustrations of a Sole Proprietor's accounts and the calculation of his Adjusted Income and Chargeable Income by the Application of the rules.

1. RATES OF INCOME TAX

Income tax is charged on the chargeable income of persons as defined in section 2. Schedule 1 paragraph 1 and 2; & Section 6(1)(b) prescribe the rates of income tax as follows:

Schedule 1 paragraph 2

1. Companies	40%
2. A person (other than a company) not resident for the basis year for that year of assessment	40%
3. A trust body	40%
4. An executor of a deceased person's estate (where the deceased person was domiciled outside Malaysia and the income was derived from Malaysia)	40%
5. A receiver appointed by the Court for income on which tax is chargeable (also see section 68 (4))	40%

Schedule 1 paragraph 1 and Section 6(1) (b)

1. Resident individuals	at scale rates
2. Clubs, associations, societies and a trustee for an incapacitated person	at scale rates
3. Executor of an individual who died domiciled in Malaysia	at scale rates
4. Non-residents on Interest on "approved loans" 15% of gross interest.	

"approved loan" means any loan or other indebtedness made or incurred on or after 1st January, 1972, for the purpose of financing development projects or for the purchase of capital equipment for development projects, and approved by the Minister;

Scale Rates of Income Tax on Chargeable Income

			Rate	Tax
For every dollar of the first	\$ 2,500	@	6%	\$ 150
For every dollar of the next	2,500	@	9%	225
On the first	5,000			375
For every dollar of the next	2,500	@	12%	300
On the first	7,500			675
For every dollar of the next	2,500	@	15%	375
On the first	10,000			1,050
For every dollar of the next	5,000	@	20%	1,000
On the first	15,000			2,050
For every dollar of the next	5,000	@	23%	1,150
On the first	20,000			3,200
For every dollar of the next	5,000	@	25%	1,250
On the first	25,000			4,450
For every dollar of the next	10,000	@	30%	3,000
On the first	35,000			7,450
For every dollar of the next	15,000	@	40%	6,000
On the first	50,000			13,450
For every dollar exceeding \$50,000 @ 50%				

In the case of an individual resident in East Malaysia an abatement of 10% in respect of each level of tax specified in this paragraph is given except the rate in respect of every dollar exceeding \$50,000.

2. GENERAL RULES FOR CALCULATING ADJUSTED PROFIT

- I. Add to the profit as shown by the commercial profit and loss account, expenses which have been charged to the profit and loss account but which are not allowable as deductions under the Act.
- II. Add to the profit any trading income which has not been credited to the profit and loss account.
- III. Deduct from the profit any item which has been credited to profit and loss account, but which need not be included for income tax purpose.
- IV. Deduct from the profit any expenses which are allowable but which have not been charged to profit and loss account.

If at any stage a loss results in place of a profit the rules have to be modified accordingly i.e. deduct where it is mentioned "add", and add where it is mentioned "deduct".

The above adjustments can be further sub-classified as follows:—

(i) Expenses Not Allowed

- (a) Expenses not wholly and exclusively incurred for the purpose of business e.g. any domestic expenses of the proprietor; and excessive emoluments to members of the family.
- (b) Losses not connected with the business and not arising out of the business e.g. loss on the sale of shares in the case of a textile merchant.
- (c) Capital expenditure such as improvements to a building, extensions to plant and machinery, depreciation of fixed assets.
- (d) Appropriation of profits such as income tax payments, general or capital reserves, salaries of proprietors, interest on capital, dividends to shareholders.
- (e) Expenses in respect of exempt income.
- (f) Contributions to any pension, provident or other similar fund or society which is not approved for income tax purpose.
- (g) Expenses incurred on qualifying expenditure for which special allowances are given e.g.
 1. Qualifying mining expenditure (Schedule 2).
 2. Qualifying plantation expenditure (Schedule 3).
 3. Qualifying forest expenditure (Schedule 3).
 4. Qualifying prospecting expenditure (Schedule 4).

- (h) Interest paid to any non-resident person if income tax on it has not been deducted and paid over to the D.G.
 - (i) Any sum payable for the use of a licence or permit to extract timber from a forest in Malaysia unless it is paid to a State Government.
- (ii) **Receipts to be Excluded**
- (a) Income which is exempt under section 127 of the Income Tax Act or Investment Incentives Act 1968.
 - (b) Writing back of provisions; general or capital reserves previously not allowed as deduction, these having been taxed in that period.
 - (c) Capital profits or receipts e.g. profit on the sale of fixed assets or investments.
 - (d) Income which is not assessed under section (4) (a) but under section 4 (b) to 4 (f) e.g. rents, interest, royalties, dividends etc. to be assessed separately.
- (iii) **Income to be Included**
- (a) Bad debts recovered credited to a reserve account and not to profit and loss account.
 - (b) Recovery of insurance claims or indemnities regarding current assets lost, credited to any other account and not to profit and loss account.
- (iv) **Expenses that may be Allowable but not Charged to the Profit and Loss Account**
- These may have been charged to:—
- (a) A reserve account.
 - (b) A fixed asset account i.e. capitalised.
 - (c) Personal account of the proprietor.
- (v) **Other Items in the Profit and Loss Account Requiring Adjustments**
- (a) **Salaries, wages, overtime, bonus and E.P.F.:** These expenses in respect of a partner or a sole-proprietor must be added back.
 - (b) **Rent:** Where a proprietor of the business or a partner lives on the business premises, a portion of the rent which is applicable to private use is to be added back.
 - (c) **Water, light and power:** Amount of expenses applicable to private use is added back.
 - (d) **Subscription:** Subscriptions to trade associations like Chinese Chamber of Commerce, International Chamber of Commerce, Manufacturers Association are allowable. But subscriptions to clan associations or clubs are not allowed and must be added back.

- (e) **Donations:** These are not chargeable deductions and are only allowed if there is any aggregate income, and the donations are to the Government or State Government or consist of *Zakat* or *Fitrah* or to an approved institution (section 44 (6) & (7)). Hence donations must be added back first and claimed later on if there is still an aggregate income.
- (f) **Repairs and Renewals:** Expenses on repairs are allowable if these are incurred in maintaining, and keeping the assets in a running condition. Any improvement, addition or extension is not allowable. Where an asset is completely replaced, the replacement will be allowed as a deduction provided that:—
- (aa) no wear and tear allowances have been claimed, on the asset;
- (bb) it was not a reconstruction or rebuilding of any premises, structures or works of permanent nature, any plant or machinery or fixture or any means of conveyance.

To repeat, cost of a pure replacement distinguishing it from an improvement is allowed.

Initial repairs, incurred in putting a newly purchased fixed asset in a working condition, were up to now not allowed because of the "Law Shipping Case", but in view of the decision in *Odeon Associated Theatres Ltd., v. Jones* where sound accountancy principles would rule them as allowable revenue expenditure, a good case can be made out for allowing them. Where alterations include repairs, usually a portion of the expenses should be allowed as notional repairs. Where instead of repairing an existing asset a new asset is built or bought, the expenditure is of course not allowed.

- (g) **Bad and Doubtful Debts:** Bad debts actually written off and doubtful debts which are specified, to the extent they are estimated to be bad are allowed as deductions if:—
- (aa) they have been shown as a trading receipt, and
- (bb) they were not incurred before the commencement of the business, and
- (cc) they were not incurred before 1.1.1947.

A general provision for doubtful debts is not allowed. Any recovery of a bad debt written off and allowed previously is to be added back to the profit.

- (h) **Legal Expenses:** Legal expenses of a capital nature are not allowed but legal expenses of a revenue nature are allowed. The examples of the legal and other expenses not allowed are expenses of acquiring fixed assets and leases, architect's fees for the construction of a building, and penalties and fines for breach of the law. These latter are actually not connected with the business, for they are losses not arising out of the trade. However, fines for infringement of the law by the employees in the course of the trade may be allowable. Legal expenses incurred in the collection of debts and also on renewing a trade mark are allowed but not in respect of a new trade mark.

- (f) **Travelling and Transport Expenses:** Expenses incurred in the course of business i.e. visiting customers or going from office to branches are allowed. But expenses incurred in travelling from home to the place of business or place of business to the home are generally not allowable.
 - (j) **Exceptional Payments:** Where the wages and other expenses are incurred in the construction of a fixed asset they have to be capitalised i.e. are disallowed.
 - (k) **Losses due to Robbery or Embezzlement:** If they are incurred in the normal course of business they are allowable otherwise not. However, embezzlements by directors are generally not allowed (See also Chapter XIV).
 - (l) **Interest:** Interest on partner's capital is not allowed, and neither is the interest paid to a non-resident allowed unless tax is deducted and paid to the D.G. on it. Hire purchase interest included in the hire purchase instalment is allowed.
 - (m) **Depreciation:** Depreciation charged in the accounts is not allowed as a deduction in computing adjusted profit. However, special capital allowance are given which may be deducted from the adjusted income (See Chapter XVIII).
 - (n) **Preliminary Expenses:** Expenses incurred in the formation of a firm are not allowed.
 - (o) **Income Tax:** Income tax paid on the profits of the business is not allowed. However, income tax paid for an employee whose emoluments are 'free-of-tax' is allowed. It is considered as an extra remuneration or benefit.
 - (p) **Professional Fees:** Retainer fees, audit fees and book-keeping charges are allowed. Income tax consultant's fee is not allowed, being expenses incurred after the production of income. (But in the case of a limited company, income tax consultant's fee is allowed as a concession.)
 - (q) **Removal Expenses:** These are allowable only if the size and scope of the new premises is very much similar to the old premises. If the new premises represent an extension and improvement of the business these are not allowable and must be added back.
 - (r) **Reserves and Provisions:** Transfer to general reserve or capital reserve is not allowed as deduction e.g. transfer to capital redemption fund or debenture redemption reserve. But provisions for accrued but unpaid expenses are allowed. The unallowed provision must be added back.
- (vi) **Credit Items**
- (a) **Rents, Interest, Dividends etc.:** Where these items are not part of a trade and are assessable under another paragraph of section 4 i.e. under section 4 (b) to (f), to ascertain the profit of the trade, these must be excluded. These will be computed separately and total income will be arrived at. All expenses incurred in relation to these should also have been excluded in the calculation of adjusted income by adding them back.

- (b) **Capital Profits:** Profits on the sale of fixed assets must be excluded.
- (c) **Exempt Income:** Income exempted from tax under section 127 or Investment Incentives Act 1968, has to be excluded.
- (d) **Sales of "Know How":** If it is not the business of the firm to sell "know-how" i.e. it is not a firm of management-consultants etc.; any payment received from an isolated sale of such "know-how" is not assessable to income and should be excluded. If the amount is to be large, legal advice on this point should have been obtained. The judgements of the House of Lords in *Moriarty v. Evans Medical Supplies* (1957) (37 T.C. 540) and *Rolls Royce v. Jeffery* (1962) (41 A.T.C. 17) should be closely studied.

(vii) **Basis of Stock Valuation**

See Chapter IX paragraph 1 sub-paragraph (xi).

(viii) **Profits or Losses on Exchange**

These arising from revenue transactions can be ignored but the effect of profits and losses on capital items must be nullified in the tax computation.

(ix) **Long-Term Contracts**

It is usual to bring in a part of the profits on such contracts in every accounting period according to certain formulas applied according to accounting principles. Where the treatment is reasonable and consistent the procedure used may usually be acceptable to the D.G.

(x) **Stock of Work-in-Progress and Direct Costing**

Work in progress normally includes the raw material, direct labour and manufacturing expense. Where the variable costs are included under a direct costing method, this appears to accord with the definition of "total cost" given in section 35 (3) (a) (ii), but according to this provision the person must elect to use this basis so the opinion of the D.G. should be sought as to whether this basis is acceptable to him.

(xi) **Hire Purchase Sales**

Any practice consistently applied according to sound accountancy principles is usually acceptable. In the calculation of the provision for losses on defaulted instalments a flat rate percentage is unlikely to be acceptable. Some attempt must be made to relate the provision to specific debts perhaps by means of an "age of debts" schedule in the case where the very large number of accounts makes it impracticable to consider each individual account separately. But the D.G. has the power under section 36 to direct that special treatment be applied.

**COMPUTATION OF ADJUSTED PROFIT (SOLE-PROPRIETOR)
AND CHARGEABLE INCOME**

ILLUSTRATION I — QUESTION & ANSWER

Chop Lee Gee Song

Profit and Loss Account for the year ended 31st December 1971

Administrative Expenses				
1. Shop rent	\$12,000			
2. Water and light	1,800			
3. Salaries	84,000			
4. Payroll tax and C.P.F.	4,400			
5. General expenses	5,200			
6. Printing and stationery	1,500			
7. Repairs	2,500			
8. Bank charges	500			
9. Depreciation	3,500			
10. Legal expenses	1,750			
11. Audit fees	3,000			
12. Donations	250			
13. Subscriptions	350	\$120,750		
Selling and Distribution Expenses				
14. Advertising	8,000			
15. Travelling and transport	6,250			
16. Commissions	10,000	\$24,250		
Financial Expenses				
17. Bad debts and provision for bad debts	10,500			
18. Loan interest	5,000	15,500		
19. Loss on the sale of a motor car		1,500		
Net profit		10,000		
			172,000	
				\$172,000

Notes on the Profit and Loss Account and Tax Adjustment	Adjustment
1. Proprietor lives on the first floor $\frac{1}{2}$ is considered as 'personal use'	Add \$ 6,000
2. $\frac{1}{2}$ is for personal use	Add 900
3. Includes \$18,000 for the proprietor—appropriation of profit	Add 18,000
4. No payroll tax for the proprietor but includes E.P.F. for the proprietor of \$1,440	Add 1,440
5. Includes a custom's fine of \$2,000	Add 2,000
6. \$500 for personal use	Add 500
7. Includes capital expenditure of \$1,500	Add 1,500
8. All business	—
9. Expressly disallowed	Add 3,500
10. Include expenses of \$1,000 for arranging a loan	Add 1,000
11. Include a fee of \$350/- for preparing income tax returns	Add 350
12. Donations all allowable—but have to be added back here to find out the profit	Add 250
13. Subscriptions not allowable \$100	Add 100
14. All allowable	—
15. Includes private travelling of \$2,400	Add 2,400
16. All allowable	—
17. Includes general provision of \$5,000	Add 5,000
18. Allowable	—
19. Capital loss (but balancing charge or allowance has to be calculated separately)	Add 1,500
20, 21 & 22. Assessed separately	Deduct 16,050
23. Exempt income	Deduct 250
24. Capital profit (but balancing charge or allowance has to be calculated separately)	Deduct 1,050

Note 2—Other Information

(i) Following has been agreed with the D.G. for the Y/A 1972.

A Balancing charge on the sale of a machinery—\$1,000.

A Balancing allowance on the sale of another machinery—\$590.

Capital Allowances—\$1,000.

(ii) Statutory income from other business, profession or vocation agreed with the D.G. —\$3,500.

	<i>Brought Forward</i>	\$54,440
<i>Deduct:</i>		
16. Dividends	\$ 600	
17. Rents	15,000	
18. Fixed deposit interest	450	
19. P.O.S. Bank interest	250	
20. Profit on the sale of machinery	1,050	17,350
Adjusted profit		\$37,090
Computation of Chargeable Income for the Y/A 1972		
Adjusted Profit from Business (as above)		\$37,090
<i>Add:</i> Balancing Charge		1,000
		38,090
<i>Deduct:</i> Balancing allowance	\$ 590	
Capital allowances	1,000	1,590
Statutory income from this business		36,500
Statutory income from other business		3,500
		40,000
<i>Add:</i> Abortive mining expenditure recouped during the year		—
		40,000
<i>Deduct:</i> Previous years business loss not yet recouped (up to a maximum of \$40,000 can be recouped in this case)		20,000
		20,000
<i>Add:</i> Statutory income from all other non-business sources		
Dividends (gross)		1,000
Rents from properties (net) (after deduction of all allowable expenses)		15,000
Interest (Fixed deposit and P.O.S. Bank)		700
Aggregate income		36,700
	<i>Carried Forward</i>	\$36,700

	<i>Brought Forward</i>	\$36,700
<i>Less:</i> Donation to an approved institution		500
		<hr/>
Total income		36,200
Deducted Personal Allowances:		
Self	2,000	
E.I.R.	1,000	
Wife	1,000	
Children (\$1,500 + \$500)	2,000	
Life Assurance \$4,000 but restricted to (maximum)	3,000	9,000
		<hr/>
Chargeable Income		\$27,200
		<hr/>

ILLUSTRATION II — QUESTION

1. Mr. David Yong has been carrying on a business known as "National Emporium" for some years. From the following profit and loss account and the information given below prepare a computation of profit for income tax purposes.

National Emporium

Profit and Loss Account for the year ended

31st August, 1970

Administrative Expenses:

Office Rent	\$ 4,800	Gross profit b/f	\$180,000
Water and Electricity	500	Bad debts recovered	10,000
Food	400	Rents from sub-tenant	10,000
Printing and Stationery	2,400		
Telephone and Postage	700		
Repairs	15,500		
Assessment	6,000		
Entertainment	3,500		
Donations	10,000		
Miscellaneous	7,000		
Salaries, Bonus & Overtime	45,700		
	<hr/>		
	\$104,500		

Selling and Distribution**Expenses:**

Advertising	12,000	
Travelling and Transport Ex- pense	5,000	
Depreciation	3,000	\$ 20,000
		<hr/>

Financial Expenses:

Bad Debts	2,500	
Provision for B/Debts	10,000	12,500
		<hr/>
		137,000
Net Profit for the year		63,000
		<hr/>
		\$200,000
		<hr/>

\$200,000

Salaries, Bonus and Overtime—\$45,700

This includes \$1,000 per month for Mr. David Yong.

Food—\$8,400

This is in respect of 6 employees and Mr. David Yong.

Printing and Stationery—\$2,400

This includes \$100/- for printing invitation cards for a birthday party of Mr. David Yong.

Telephone and Postages—\$700

\$50 were spent on replies to congratulatory messages received from personal friends on Mr. David Yong's birthday.

Repairs—\$15,500

Repairs to furniture and show-cases	..	..	..	..	\$ 500
Painting and whitewashing	..	..	..	..	2,000
Extension to existing store and construction of one additional store	..	..	..	..	12,500
Minor repairs (all revenue items)	..	..	..	..	500
					<hr/>
					\$15,500
					<hr/>

Entertainment—\$3,500

David Yong's birthday party	..	..	..	..	\$ 1,000
Green Spot for staff	..	..	..	..	500
Tea, coffee and drinks for customers	..	..	..	..	2,000
					<hr/>
					\$3,500
					<hr/>

Assessment—\$6,000

It was in respect of store

Donations—\$10,000

Approved by Minister	..	..	..	..	..	\$ 7,500
Others	..	..	..	..	..	2,500
						<u>\$10,000</u>

Miscellaneous—\$7,000

Annual Stock-Taking expenses	..	..	..	..	..	\$ 250
Income Tax for Mr. David Yong	..	..	..	..	..	4,000
Chess for staff	..	..	..	..	..	50
Traffic offence committed by staff	..	..	..	..	..	250
Office removal expenses (Extra-ordinary expansion scheme)	..	..	..	..	..	2,450
						<u>\$ 7,000</u>

Advertising—\$12,000

In Newspapers and Journals	..	..	..	..	..	\$ 5,000
Handbills and samples	..	..	..	..	..	1,500
In T.V.	..	..	..	..	..	5,500
						<u>\$12,000</u>

Travelling and Transport—\$5,000

All in respect of business.

Bad Debts—\$2,500

D.C. Tong & Co. (Customer)	..	..	..	..	..	\$ 2,000
K. P. Lalla (Customer)	..	..	..	..	..	500
						<u>\$ 2,500</u>

No Capital allowances are claimed by Mr. David Yong.

Bad Debts Recovered—\$10,000

These are all trade debts written off in the previous years.

Rents from Sub-Tenants—\$10,000

These are in respect of two shop places let out in the main building of the store.
It has been agreed with the D.G. that this income be taken to be business income.

Illustration II—Solution

National Emporium

Computation of Adjusted Profit for the year of assessment 1971

Net profit as per accounts to 31.8.1970	\$63,000
Add: Salaries—Proprietor	12,000
Food $\frac{1}{7}$ of \$8,400	1,200
Printing & stationery—Yong's invitation Cards	100
Postage—personal	50
Repairs—Store extension and addition	12,500
Entertainment—birthday party	1,000
Donation	10,000
Miscellaneous—David Yong's income tax	4,000
—Traffic fine	250
—Office removal expenses	2,450
Depreciation	3,000
Provision for bad debts	10,000
	<hr/>
Adjusted profit	\$119,550
	<hr/>

Donations of \$7,500 approved by the Minister will be deducted from the aggregate income which in this case is \$119,550 to arrive at the total income.

ILLUSTRATION III — QUESTION

3. From the following information compute the total aggregate income, for the relevant years of assessment of Mr. Teo Guan Huat who is the proprietor of People's Confectionery. He commenced business on 1st April, 1970.

People's Confectionery

Profit and Loss Account for the year ended

31st March, 1971.

Rent	\$ 8,400	Gross profit b/f	\$89,025
Water and Light	1,200	Interest	700
Repairs	2,000	Dividends (Net)	2,500
Insurance	400	Surplus on Sale of Invest- ments	200
Salaries, Bonus and O/T	72,000	Profit on Sale of Bicycle	25
E.P.F.	4,800	Net loss	5,000
Payroll Tax	1,200		
Printing and Stationery	500		
Subscriptions	450		
Donations	1,650		
Sundry Expenses	1,500		
Depreciation	2,500		
Bad Debts w/off	850		
	<u>\$97,450</u>		<u>\$97,450</u>

Rent—\$8,400

This is in respect of a shop-house. The shop is on the ground floor and the house is on the top of it. Mr. Teo resides in the house. The floor areas of the shop and the house are approximately equal.

Water and Light—\$1,200

This is in respect of the shop and the house.

Repairs—\$2,000

Alteration of shop windows	\$1,000
Whitewashing and painting the shop-house	500
Cost of one iron gate for the shop	500
	<u>\$2,000</u>

Insurance—\$400

This is for shop-house.

Salaries, Bonus and Overtime—\$72,000

This includes \$1,000 per month for Mr. Teo.

E.P.F. and Payroll Tax

These are for the staff.

Printing and Stationery—\$500

This includes \$200 in respect of school textbooks for Mr. Teo's children.

Subscriptions—\$450

Chinese Chamber of Commerce	\$ 200
S.C.R.C. (for Mr. Teo)	125
Malaysian Confectioners' Association	125
	<u>\$ 450</u>

Donations—\$1,650

1.9.1970	Approved donations	..	..	..	..	\$ 500
30.9.1970	Temples in aid of various shows	..	..	..	..	100
1.3.1971	Beggars	..	..	..	..	25
1.3.1971	Various Churches	..	..	..	..	25
1.3.1971	Approved donations	..	..	..	..	1,000
						<hr/>
						\$1,650

Sundry Expenses—\$1,500

Wrappers and paper bags for the shop	..	..	..	..	..	\$1,000
Dresses for children and family (self)	..	..	..	..	..	200
Household (utensils for own house)	..	..	..	..	..	100
Miscellaneous items for bakery	..	..	..	..	..	50
Wages to a relief worker	..	..	..	..	..	150
						<hr/>
						\$1,500

Bad Debts—\$850

Sundry trade debtors	..	..	..	..	..	\$ 500
Wee Ah Seng—an employee	..	..	..	..	..	200
Personal loan to Mr. Soh Hai Guan	..	..	..	..	..	150
						<hr/>
						\$ 850

No Capital allowances have been claimed and there are no unrecovered losses from previous years. There is no other business source.

Interest—\$700

P.O. Savings bank account (credited on 31.3.1971)	..	..	..	..	\$ 500
Chartered Bank Savings account (credited on 30.12.1970)	..	..	..	..	200
					<hr/>
					\$ 700

Dividends—\$2,500

Date Declared Payable	Received	Gross	Tax	Net
From Tosca Ltd. (Malaysia)				
30.6.1970	10.7.1970	\$2,000	\$800	\$1,200
31.12.1970	6.1.1971	1,000	400	600
From T.S. Co. Ltd. (Malaysia)				
31.12.1970	10.1.1971		Free of Tax	600
From Shell (M) Ltd.				
1.1.1971	31.3.1971	(Pioneer Co.—exempt)		100

Illustration III—Solution

People's Confectionery

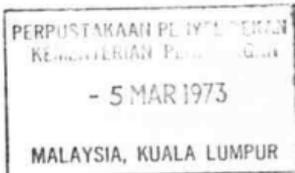
Computation of Adjusted profit for the year ended 31st March, 1971

Loss as per accounts		\$ 5,000	
Add: Interest		700	
Dividends		2,500	
Surplus on sale of investments		200	
Profit on sale of bicycle		25	
			8,425
Less: Rent $\frac{1}{2}$ of \$8,400—personal use	\$ 4,200		
Water & Light $\frac{1}{2}$ of \$1,200 — personal use	600		
Repairs: Alteration of windows	1,000		
White washing $\frac{1}{2}$ of \$500 — p.u.	250		
1 iron gate	500		
Insurance $\frac{1}{2}$ of \$400—personal use	200		
Salaries—Mr. Teo	12,000		
Printing and Stationery—personal use	200		
Subscriptions—S.C.R.C.	125		
Donations	1,650		
Sundry Expenses:			
Dresses for Children—personal use	200		
Household utensils — personal use	100		
Bad debts (200 \times 150)	350		
Depreciation	2,500		
Sweets and Cakes:			
For use in the house—20 \times 12	240		
Presents—personal—50 \times 12	600		
			24,715
Adjusted profits			\$16,290

Mr. Teo Guan Huat

Computations of Total Aggregate income for

	y/A 1971	y/A 1972
Business		
Basis period		1.4.1970 to 31.3.1971
People's Confectionery—adj. profit		\$16,290
Interest		
Basis period—b/y	1.1.1970 to 31.12.1970	1.1.1971 to 31.12.1971
Chartered Bank S a/c	200	—
Dividends		
Basis period—b/y (as above)		
Tosca Ltd. (Malaysia) (gross)	3,000	—
T.S. Co. Ltd. (Malaysia) (gross)	1,000	—
Aggregate income	<u>4,200</u>	<u>16,290</u>
Less: Approved Donations	500	1,000
Total aggregate income	<u>\$ 3,700</u>	<u>\$15,290</u>
Set off to be claimed for tax deducted at source from dividends		\$ 1,600



ADJUSTED PROFITS OF PARTNERSHIPS AND COMPANIES

1. WHAT IS PARTNERSHIP

(i) General

In Malaysia a partnership's profit are not assessed on the partnership itself as a separate entity but the tax is charged on the individual partner on his share of the divisible profit and other income from the partnership along with his income from other sources. In this chapter we shall illustrate (a) how adjusted and divisible profits are computed and divided between the partners; (b) how wear and tear allowances and donations if any are adjusted between them and (c) how division is made where there is a change in the partnership. But before we go into these details it may be useful to consider what we mean by a partnership, for income tax purpose. It is a relationship which must subsist between the persons carrying on a business in common, with a view to profit. It is a matter of fact. An agreement is not operative if it is not acted on. A verbal agreement of partnership is as good as a written one. Some questions relevant in deciding whether a partnership exists could be as follows.

1. In whose name is the partnership registered?
2. In whose name is the bank account and who signs the cheques?
3. Whose name is printed on the letterheads and other stationery?
4. Who is liable in respect of the debts of the partnership?
5. Who can close down the business?
6. How would the assets of the partnership be divided on dissolution?

(ii) Special Provisions for ascertaining the Income from a Partnership Business Source— Section 55

As the partnership structure of economic interests provides considerable opportunity for tax avoidance by means of special arrangements between partners, by trying to charge expenses on the borderline of private and business expenses to the business, and by other means too numerous to list, the Act in sections 55 to 59 makes specific provisions on the postulates which are deemed to apply in bringing about an individual partner's adjusted income from a business partnership.

These postulates become necessary because the partnership as such is neither assessable nor chargeable to income tax, hence it is postulated by section 56 that each partner is deemed to have had transferred to him the business and assets together with the rights and liabilities of the partners and this postulated transfer constitutes a business carried on by each partner as a sole-proprietorship and the accounts of the partnership are deemed to be the accounts of this sole proprietorship. On the basis of this legal construct to which Part III of the Act (Ascertainment of Chargeable Income) and specifically sections 55 to 59* are applied to calculate the adjusted income of the sole-proprietor (i.e. the partner) from that business for the basis period for a year of assessment. This is to be done in the following way:—

Step 1 Take the "Provisional adjusted income" of the sole-proprietorship, i.e. the figure in the accounts of the partnership, after adjustments for tax-purposes say: †\$100,000

Step 2 Deduct the total amount of:— \$ 44,000

(a) any remuneration payable to a partner by virtue of any partnership arrangement say:

AS 5,000

B 10,000

C 20,000

\$35,000

(b) any interest on capital or advances payable to any partner say:

AS —

B —

C 5,000

\$ 5,000

(c) Any expense charged in partnership accounts which would be a private and domestic expense if incurred by a partner or a reimbursement of the above say:

AS —

B 1,000

C 3,000

\$ 4,000

Divisible Income

\$ 56,000

**Legal Note:* Section 52 the first section in Chapter VIII of Part III provides that the previous seven chapters also apply but in cases of inconsistency chapter VIII (which contains sections 55 to 59) is to prevail, the provisions in the previous seven chapters being held void to the extent of the inconsistency.

† The equivalent figure in the Illustration in paragraph 3 below is \$126,300.

Note on Divisible Income

1. It is presumed to accrue evenly over the basis period (i.e. an individual who is partner for half the period is presumed to get his share of half of the above divisible income).
2. The sharing is on the basis of agreement/agreements subsisting during the time (i.e. different parts of the period may have different profit sharing ratios with different persons).

Step 3 Divide as indicated in notes say: A $\frac{1}{3}$: B $\frac{2}{3}$: C $\frac{1}{3}$:

i.e.	A\$ 8,000
	B 16,000
	C 32,000

Step 4 Find adjusted income of the sole-proprietor (i.e. the partner) as follows:
To his Divisible Income (Step 3 above):
add his share of the items deducted in Step 2 above.

The result is shown for all 3 partners. (In law each of them is treated as a "sole-proprietor").

	Total	A	B	C
Divisible Income	\$ 56,000	\$ 8,000	\$16,000	\$32,000
+ Share of Remuneration and Interest etc.	44,000	5,000	11,000	28,000
Adjusted Income	\$100,000	\$13,000	\$27,000	\$60,000

(iii) Special provisions where an individual has a continuous interest in successive partnerships—section 56

Where a partnership (the old partnership) prepares its normal accounts for a 12 month period, and this old partnership ceases business on the last day of this period and a new partnership to take over the business of the old partnerships is immediately formed with some old partners also being partners in the new partnership, and furthermore this new partnership also prepares its accounts for a 12 month period, the provisions outlined below do *not* apply.

If the change in the above partnership occurs on a date other than on the first day of a new accounting period any individual who was a partner in both the old and the new partnership is treated as a "continuing partner" and his adjusted income from the partnership as set out in sub-paragraph (ii) above is modified by section 56.

This provision may be easier to understand if it is realized that, in its absence, a change in a partnership could be manipulated to reduce the adjusted income from this source in that year of assessment while increasing that of the next year of assessment. This

1973

(For $X, Y + Z$)	1.10.1971 to				
	30.9.1972	51,000	17,000	17,000	17,000

The basis period applicable to the new partners and to Z in future years of assessment is governed by section 21.

(iv) **Other Partnership Income**—section 58

Any income receivable by a partnership other than from the ordinary business source is to be also included in this computation whether or not it has been distributed to the partner. Where dividends, rents, etc. form business income (i.e. for investment or property dealers) this is treated in the same manner as other partnership income, even where such a business is not connected with the main partnership. Where these items are not business income (i.e. dividends from incidental shareholdings) they are deemed to be the dividends, rents, etc. of the individual partners, in their profit sharing ratios.

(v) **Partnership a partner in another partnership**—section 57

In this case only person who is a partner in the first partnership is postulated to be a partner in the second partnership. The computation of his adjusted income is done by applying the procedures outlined in the chapter, on the assumption that his share in the first partnership is also his share in the second partnership e.g. "Abraco" has 3 partners $A B C$ sharing profits $\frac{1}{2}; \frac{1}{3}; \frac{1}{6}$; and it owns outright "Braxo". A is postulated to be a partner in "Braxo" with $\frac{1}{2}$ a share.

2. COMPUTATION OF DIVISIBLE AND ADJUSTED PROFIT OF A PARTNERSHIP

The rules for computing the adjusted income from the commercial profit and loss account are the same as those in the case of a sole-proprietor. The only difference is that here we have to further apply the relevant statutory provision to find the "Adjusted Income" of each partner (see paragraph 1 sub paragraph (ii) above). We shall now work out a fuller example to illustrate the principles and procedures.

Note 1 The brief illustration in paragraph 1 sub paragraph (ii) is arranged to reflect the statutory provision. The order in *this* illustration gives effect to the law, but reflects the usual practice. To help comparison the comparative figures from the previous illustration are given in brackets.

Note 2 In the case of a partnership *loss* the same rules apply except that the rules for "add" & subtract reverse signs. (also see section 59).

3. ILLUSTRATION

X, Y and Z are in partnership, sharing profits and losses equally. Interest at the rate of 6% per year is allowed, on the capital at the commencement of the year. During the year ended 31st December 1970 they received the following salaries.

X \$24,000; Y \$18,000; Z \$12,000

The following is the firm's profit and loss account for the year ended 31st December, 1970.

Profit and Loss Account

Business expenses (see Note below)	\$ 85,000	Gross profit b/f	\$196,000
Interest on Capital:			
X	1,200		
Y	900		
Z	1,500		
Partners Salaries:			
X	24,000		
Y	18,000		
Z	12,000		
Balance of profit	54,000		
	\$196,000		\$196,000

Wear and tear allowances for the Y/A 1971 have been agreed with the D.G. as \$2,400.

Note: Business expenses includes—depreciation \$5,000; legal expenses in respect of formation of a proposed limited company \$900; provision for bad debts \$7,000; approved donations \$1,800.

X, Y, Z

Computation of Adjusted Income

Profit as per accounts to 31.12.1970	..	..	..	..		\$54,000
<i>Add:</i> Depreciation	..	..	..	..		5,000
Legal expenses	..	..	..	..		900
Provision for bad debts	..	..	..	..		7,000
Donations	..	..	..	..		1,800
						68,700
Divisible income	..	..	..	..	*(56,000)	68,700
<i>Add:</i> Interest on capital						
X	..	..	..	..	\$ 1,200	
Y	..	..	..	..	900	
Z	..	..	..	..	1,500	3,600
						72,300
					<i>Carried Forward</i>	72,300

*The bracketed figures are for comparison with the illustration on pages 147 and 148.

	<i>Brought Forward</i>	72,300
Add: Partners Salaries:		
X	24,000	
Y	18,000	
Z	12,000	54,000
Adjusted income	(100,000)	\$126,300
Wear and tear allowance		2,400
Allowable donations		1,800

Allocated to the partners as follows: [Assumption: No other income or loss]

Name	Share of Profit	Divisible Income	Interest	Salaries	Adjusted Income	W & T	Donations	Total Income in the hands of Partners
		\$	\$	\$	\$	\$	\$	\$
X	$\frac{1}{3}$	22,900	1,200	24,000	48,100	800	600	46,700
Y	$\frac{1}{3}$	22,900	900	18,000	41,800	800	600	40,400
Z	$\frac{1}{3}$	22,900	1,500	12,000	36,400	800	600	35,000
		68,700	3,600	54,000	126,300	2,400	1,800	122,100

4. LIMITED COMPANY—ADJUSTED PROFIT

The general rules given in Chapter XXIV also apply in the case of limited companies. But the following items are specially concerned with companies. We will explain here how they should be treated for income tax purpose.

(i) Formation and Preliminary Expenses

As these expenses are incurred before the commencement of the business, they are not allowed, being expenses incurred to put the company in a position to earn income and therefore not in the production of income.

(ii) Expenses on Increasing the Share Capital or Issuing Debentures

Being capital expenses these are not allowed.

(iii) Goodwill Written-off

It is not allowed being an appropriation of profit.

(iv) Research and Development Expenses

Where the expenses are of revenue nature i.e. incurred during the course of one year for that year's benefit these are allowed as the expenses incurred in the production of income (section 34(7)). Where these are of capital nature i.e. the benefit of the expenditure is to be derived for a number of years, it is not allowed. In addition any sum paid during the basis period to a scientific association which conducts research connected with the business, if such association is approved at the time by the Minister and similar sums paid to any university, college, research institution etc., which are approved by the Minister, are also allowed.

(v) Misappropriations by a Director

Embezzlements by a managing director are not allowed. However, embezzlement by an employee is allowed if it was in the course of his employment.

(vi) Dividends, Income Tax, Transfer to Reserves etc.

These are considered as appropriation of profits and are not allowed as deductions, but payroll-tax and turnover tax are allowed specifically under section 34(6).

5. ILLUSTRATIONS**Illustration I — Question**

From the following balance sheet and profit and loss account of the Unico Limited and the information given below compute the tax payable by the company for the year of assessment 1971. The company was incorporated in 1965. In the previous years, no claim has been made in respect of industrial building and wear and tear allowances. The company has claimed all the allowances this year.

UNICO LIMITED**Profit and Loss Account for the year ended****31st December, 1970**

Salaries and E.P.F.	\$ 715,425	Gross profit b/f	\$1,006,950
Bonus	80,000	Discounts received	1,550
Director's fee	16,000	Dividends	10,000
Office expenses	6,230	Rents	4,000
Repairs	5,350	Insurance claim—re-stock	
Water and light	5,500	destroyed by fire	18,000
Subscriptions	1,500	Profit on sale of invest-	
Entertainment	2,500	ments	350
Legal fees	1,900		
Advertising	6,505		
	<hr/>		<hr/>
<i>Carried Forward</i>	840,910	<i>Carried Forward</i>	1,040,850

	<i>Brought Forward</i>	840,910		<i>Brought Forward</i>	1,040,850
Vehicles—upkeep		10,500			
Travelling and transport		3,500			
Bad debts		30,000			
Bank interest and cheques		540			
Discounts allowed		3,400			
Debentures interest		12,000			
Depreciation:					
Land and building		20,000			
Plant and machinery		10,000			
Vehicles		5,000			
Net profit c/d		105,000			
		<hr/>			<hr/>
		\$1,040,850			\$1,040,850
		<hr/>			<hr/>
Income tax	\$	50,000	Balance b/f		\$ 120,000
First and final dividend — 10% less tax		36,000	Balance b/d		105,000
Balance c/f		139,000			
		<hr/>			<hr/>
	\$	225,000			\$ 225,000
		<hr/>			<hr/>

1. Salaries and E.P.F.—\$715,425

It includes:

Accrued payroll tax	\$	500
Accrued salaries		6,000

2. Provision for Bonus Account

Bonus paid	\$	40,000	Balance b/f	\$	30,000
Balance c/f		70,000	Profit and loss account		80,000
		<hr/>			<hr/>
		\$110,000			\$110,000
		<hr/>			<hr/>
			Balance b/f		\$ 70,000

UNICO LIMITED

Balance Sheet as at 31st December, 1970

31.12.1969	Share Capital	Authorised	Issued and Fully Paid	31.12.1969	Fixed Assets		
\$ 500,000	Ordinary shares of \$1 each	\$5,500,000	\$ 500,000	\$ 320,000	Land and building at cost less depreciation	\$300,000	
100,000	General reserve		120,000	180,000	Plant and machine at cost less depreciation	\$170,000	
120,000	Profit and loss account		139,000	97,000	Vehicles at cost less depreciation	92,000	562,000
720,000			759,000	597,000			
150,000	8% Debentures (secured against land and building)		150,000		Investments (at cost)		
				60,000	Tobas Ltd., (Malaysia)	55,000	
				75,000	Guru Ltd., (Malaysia)	75,000	
				10,000	X Ltd. (Malaysia)	10,000	140,000
	Current Liabilities				Current Assets		
125,398	Sundry creditors and accrued expenses	184,561		140,000	Stock	200,000	
35,000	Provision for income tax	50,000		120,000	Sundry debtors less provision	190,000	
30,000	Provision for bonus	70,000		50,000	Loan to Holiday (M) Ltd.	90,000	
2,000	Bank overdraft	3,000		18,398	Cash in hand and at bank	40,561	520,561
8,000	Managing Director's current account	6,000	313,561				
<u>\$1,070,398</u>			<u>\$1,222,561</u>	<u>\$1,070,398</u>			<u>\$1,222,561</u>

3. Office Expenses—\$6,230

Insurance of stock	\$3,500
Part-time worker's wages	150
Office cleaning	1,580
Replacing electric lamps	100
Newspapers	250
Redecoration of office	650
	<hr/>
	\$6,230
	<hr/>

4. Repairs—\$5,350

Repairs to factory building	\$3,500
Architect's fee in respect of repairs	500
Cost of changing plant and machinery from petrol to diesel	850
Repairs to plant and machinery	500
	<hr/>
	\$5,350
	<hr/>

5. Subscriptions—\$1,500

The Malaysia Manufacturers' Association	\$ 500
The Chinese Chamber of Commerce	300
Contributions to a political party in Malaysia	700
	<hr/>
	\$1,500
	<hr/>

6. Entertainment—\$2,500

Office refreshment for staff	\$ 300
Managing director's allowance	600
Lunch for discussion on technical education for office staff and factory workers	1,100
Lunches and dinners for customers	500
	<hr/>
	\$2,500
	<hr/>

7. Legal Fees—\$1,900

Staff service agreement	\$ 100
Proposed purchase of a new factory building	800
Debts collection from customers	50
Recovery of a loan from an ex-employee	150
Regarding letting out a part of factory 1st time	800
	<u>\$1,900</u>

8. Advertising—\$6,505

Cinema slides	\$ 890
Advertising in the cinemas	2,500
T.V.	1,000
1 Neon sign (new)	2,115
	<u>\$6,505</u>

9. Bad Debts Provision Account

Bad debts w/off	\$ 8,500	Balance b/f	\$ 4,200
Balance c/f:		Specific provision	\$ 4,200
Specific provision	\$ 8,000	General provision	10,000
General provision	<u>29,700</u>	Bad debts recovered	2,000
	37,700	Profit and loss account	30,000
	<u>\$ 46,200</u>		<u>\$46,200</u>
		Balance b/f	
		Specific provision	\$ 8,000
		General provision	<u>29,700</u>
			37,700

Bad debt written off above include the following:

Trading debts incurred in 1962	\$ 4,000
Loan to an employee who has left the employment	3,000

10. Dividends—\$10,000

	Gross	Tax	Net
Tobas Ltd., Malaysia	\$10,000	\$4,000	\$ 6,000
Guru Ltd., Malaysia	5,000	2,000	3,000
X Ltd., Malaysia (a pioneer company) exempt from tax	—	—	1,000
			<u>\$10,000</u>

11. Rents—\$4,000

A part of factory was rented out first time on 1st November, 1970, at a monthly rent of \$2,000.

12. Managing Director's Current Account—\$6,000

Cash	23,285	Balance b/f	\$ 8,000
Property tax	1,200	Director's fee	1,000
Income tax	2,515	Salaries	24,000
Balance c/d	6,000		
	<hr/>		<hr/>
	\$33,000		\$ 33,000
	<hr/>		<hr/>
		Balance b/f	\$ 6,000

13. General Reserve Account

Balance c/d	\$120,000	Balance b/f	\$100,000
		Cash:	
		Profit on the sale of raw materials bought for production but sold at a profit	20,000
	<hr/>		<hr/>
	\$120,000		\$120,000
	<hr/>		<hr/>
		Balance b/f	\$120,000

14. The original cost of fixed assets was as follows:—

Land	\$150,000
Factory building	250,000
	<hr/>
	\$400,000
	<hr/>

Plant and machinery	\$230,000	(Plant and machinery = \$200,000)
Vehicles	\$150,000	(Air-conditioners—15 units = \$30,000)

Rates of wear and tear allowances:

	Industrial Building	P & M	Vehicles	Air Cond.	Neon Signs
I.A.	10%	20%	20%	20%	20%
A.A.	2%	7½%	20%	10%	10%

15. Provision for Income Tax

Cash	\$35,000	Balance b/f	\$35,000
Balance c/f	50,000	Profit and loss account	50,000
	<u>\$85,000</u>		<u>\$85,000</u>

ILLUSTRATION I — SOLUTION

UNICO LIMITED

Computation of Adjusted Profit for the Y/A 1971

Profit as per accounts to 31.12.1970			\$105,000
<i>Add:</i> Provision for bonus		\$80,000	
<i>Less:</i> Paid		<u>40,000</u>	40,000
Repairs—changing plant and machinery from petrol to diesel			850
Subscription—contributions to a political party			700
Legal Fees:			
Purchase of new factory			800
Recovery of loan from an ex-employee			150
Letting out a part of factory—first time			800
Advertising—1 Neon sign			2,115
Bad debts provision		30,000	
<i>Add:</i> Bad debts recovered		<u>2,000</u>	
		\$32,000	
<i>Less:</i> Bad debts w/off	\$8,500		
<i>Less:</i> Bad debts not allowed to be w/off	<u>7,000</u>		
	1,500		
<i>Add:</i> Increase in the specific provision (\$8,000 — \$4,200)	<u>3,800</u>	<u>5,300</u>	26,700
Depreciation			35,000
General Reserve—profit on the sale of raw materials			<u>20,000</u>
			232,115
<i>Less:</i> Dividends		10,000	
Rents		4,000	
Profit on sale of investment		<u>350</u>	14,350
Adjusted profit			<u>\$217,765</u>

Computation of Tax Payable for the Y/A 1971

Adjusted profit as above		\$217,765
<i>Add:</i> Dividends (gross)		
Tobas	\$10,000	
Guru	5,000	15,000
	<hr/>	
Rents		4,000
		<hr/>
		236,765
<i>Less:</i> Industrial building allowance	5,000	
I.A.	593	
A.A.	48,276	53,869
	<hr/>	
Assessable income		\$182,896
		<hr/>
Tax @ 40% thereof		\$73,158.40
<i>Less:</i> Tax deducted at source from dividends		6,000.00
		<hr/>
Tax payable		\$67,158.40
		<hr/>

Industrial Building Allowance

Cost	\$250,000
	<hr/>
A.A. 1971 @ 2%	\$ 5,000

Initial allowance cannot be claimed as the expenditure on the building was not incurred in the basis period for Y/A 1971 i.e. during 1.1.1970 to 31.12.1970.

CAPITAL ALLOWANCES SCHEDULE

	P & M 7½%	Vehicles 20%	Air-con. 10%	Neon Sign 10%	
Residue of Expenditure on 1.1.70	200,000	150,000	30,000		
Additions during 1970	850	—	—	2,115	
	<hr/>				
	200,850				
Y/A 1971					
I.A.	170	—	—	423	\$ 593
A.A.	15,064	30,000	3,000	212	\$48,276
	<hr/>	<hr/>	<hr/>	<hr/>	
	15,234	30,000	3,000	635	
Residue of Expenditure	<hr/>	<hr/>	<hr/>	<hr/>	
	85,616	120,000	27,000	1,480	\$48,869

ILLUSTRATION II — QUESTION

White, Black and Brown commenced business on 1st January, 1970. The partnership agreement provided as follows:—

1. Accounts to be made annually to 31st December.
2. Profits and losses should be divided equally after charging the following:—
 - (a) A salary of \$500 p.m. to White, \$200 p.m. to Black and \$100 p.m. to Brown.
 - (b) A travelling allowance of \$50 p.m. to each partner.
 - (c) An entertainment allowance of \$150 to each partner.
 - (d) Partners to be allowed an interest of 5% on their capitals at the beginning of the year.

After giving effect to the above provisions the profit and loss account for the year ended 31st December, 1970, was as follows:—

Profit and Loss Account for the year ended 31st December, 1970.			
Salaries (including partners) ..	\$12,258	Gross profit b/f	\$38,350
Office expenses	622		
Insurance	302		
Delivery and transport (including partners allowances) ..	4,003		
Advertising	3,463		
Bad debts	202		
Entertainment expenses (including partners)	6,000		
Depreciation	1,500		
Interest on capital	1,000		
Profit:			
White $\frac{1}{3}$	3,000		
Black $\frac{1}{3}$	3,000		
Brown $\frac{1}{3}$	3,000		
	\$38,350		\$38,350

Partners capital on 1st January, 1970 was:

White	\$10,000
Black	5,000
Brown	5,000

Capital Allowances as agreed with the D.G. were \$5,100 for the Y/A 1971.

Prepare computation of adjusted income of the partnership and the amount attributable to each partner.

ILLUSTRATION II — SOLUTION

Messrs. White, Black and Brown
Computation of Adjusted Profit

Net profit as per accounts to 31.12.1970		\$9,000
Add: Depreciation		1,500
		<hr/>
Divisible profit		10,500
Add: Partners' salaries	\$9,600	
Partners' travelling allowance	1,800	
Partners' Entertainment allowance	5,400	
Partners' interest on Capital	1,000	17,800
		<hr/>
Adjusted profit		\$28,300
		<hr/>
Wear and tear allowances		\$ 5,100

	Share of profit	Amount of profit	Salary	T.A.	E.A.	Int.	Total	W&T	S.I.
White	1/3	3,500	6,000	600	1,800	500	12,400	1,700	10,700
Black	1/3	3,500	2,400	600	1,800	250	8,550	1,700	6,850
Brown	1/3	3,500	1,200	600	1,800	250	7,350	1,700	5,650
		<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
		\$10,500	9,600	1,800	5,400	1,000	28,300	5,100	23,200
		<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>

ILLUSTRATION III — QUESTION

A, B, C, and *D* are partners sharing profits and losses equally. The partnership started on 1st April, 1969, and the accounts are made annually to 31st March. *D* retired from the partnership on 30th June, 1970. *A, B* and *C* carried on the business sharing profits and losses equally.

On 31st December, 1970, *C* also retired and *A* and *B* carried on the business on the previous terms. On 1st March, 1971, *E* was taken into partnership and it was agreed that he would share the profits and losses equally with *A* and *B*.

From the following information, compute the partnership incomes of *A, B, C, D,* and *E* each for the relevant years of assessment.

Adjusted Profits

1.4.1969 - 31.3.1970	..	..	\$24,000
1.4.1970 - 30.6.1970	..	..	20,000
1.7.1970 - 31.12.1970	..	..	18,000
1.1.1971 - 28.2.1971	..	..	10,000
1.3.1971 - 31.3.1971	..	..	9,000
1.4.1971 - 31.3.1972	..	..	27,000

ILLUSTRATION III — SOLUTION

Y/A	B.P.	A.I.	PARTNER				
			A	B	C	D	E
1971	1.4.1969 to 31.3.1970	\$ 24,000	\$ 6,000	\$ 6,000	\$ 6,000	\$ 6,000	\$
1972	1.4.1970 to 31.3.1971						
For A,B,C+D	1.4.1970 to 30.6.1970	20,000	5,000	5,000	5,000	5,000	
For A,B+C	1.7.1970 to 31.12.1970	18,000	6,000	6,000	—		
For B+C	1.1.1971 to 28.2.1971	10,000	5,000	5,000	—	—	
For B,C+E	1.3.1971 to 31.3.1971	9,000	3,000	3,000	—	—	3,000
		57,000	19,000	19,000	11,000	5,000	3,000
1973 A,B+E	1.4.1971 to 31.3.1971	27,000	9,000	9,000			9,000

ILLUSTRATION IV — QUESTION

Tan, Lee and Low have been in partnership for many years sharing profits and losses in the ratio of 4:2:2, respectively. From the following profit and loss accounts of the partnership for the year ended 31st December 1971, prepare computation of adjusted income of the partnership and of each of the partners for the year of assessment 1972.

Capital Allowances for the year of assessment 1972 agreed with the Income Tax Department were \$800.

Profit and Loss Account for the year ended
31st December, 1971.

Food (Mr. Tan and 5 employees)	\$ 6,000		
Trade Expenses	1,500		Gross Profit
Penalty	500		\$100,000
Salaries:			
Staff	\$20,000		
Mr. Tan	4,800		
Mr. Lee	1,800	26,600	
<hr/>			
Allowances:			
Staff	\$10,000		
Mr. Tan	1,800		
Mr. Lee	1,200	13,000	
<hr/>			
Transport Allowances:			
Staff	10,000		
Mr. Tan	1,200	11,200	
<hr/>			
Depreciation	5,000		
Net Profit	36,200		
	<u>\$100,000</u>		<u>\$100,000</u>

ILLUSTRATION IV — SOLUTION

**Messrs. Tan, Lee and Low
Computation of Adjusted Profit**

Net Profit as per accounts to 31.12.1968	\$36,200
Add: Penalty	500
Depreciation	5,000
	<hr/>
Divisible profit	c/f 41,700

	b/f	\$41,700
Add: Partner's Food 1/6 of \$6,000	\$1,000	
Partner's Salaries	6,600	
Partner's Allowances	3,000	
Partner's transport	1,200	11,800
		<hr/>
Adjusted profit		\$53,500
		<hr/>
Wear and Tear Allowances		\$800

Statutory incomes of Partners

Name of Partner	Profit Sharing ratio	Amount of D. profit	Food	Salary	Allowances	Transport	Total for assessment	W & T allowances	S.I.
1. Tan	4	\$20,850	\$1,000	\$4,800	\$1,800	\$1,200	\$29,650	\$400	\$29,250
2. Lee	2	10,425	—	1,800	1,200	—	13,425	200	13,225
3. Low	2	10,425	—	—	—	—	10,425	200	10,225
	8	\$41,700	\$1,000	\$6,600	\$3,000	\$1,200	\$53,500	\$800	\$52,700

ILLUSTRATION V — QUESTION

5. Soh, Koh and Mok have been in partnership for many years sharing profits and losses in the ratio of 3:2:1, after charging a salary of \$100 p.m. to Soh, \$200 p.m. to Koh and \$300 p.m. to Mok and income tax on their incomes respectively. Mok retired from the partnership on 31st December, 1970. From the following profit and loss account for the year ended 31st December, 1970, and the additional information compute adjusted profit of the partnership. Compute also the amount of total income of each partner for the year of assessment 1971 (if any).

Profit and Loss Account for the year ended
31st December, 1970.

Office Salaries	\$ 22,580	Gross Profit b/d	\$149,100
Office Expenses	16,220		
Insurance	3,020		
Delivery Expenses	22,030		
Advertising	34,610		
Repairs	10,000		
Legal Expenses	9,000		
Tax	7,000		
Subscriptions	1,540		
Entertainment	5,500		
Travelling Expenses	1,500		
Printing and Stationery	1,525		
Depreciation	2,575		

Net Profit:

Soh $\frac{3}{6}$	\$6,000		
Koh $\frac{2}{6}$	4,000		
Mok $\frac{1}{6}$	2,000	12,000	
		\$149,100	\$149,100

Office Salaries—\$22,580

Soh	..	..	..	..	..	..	..	\$ 1,200
Koh	..	..	..	..	..	..	..	2,400
Mok	..	..	..	..	..	..	..	3,600
Employee (including E.P.F.)	..	..	..	..	..	..	..	15,380
								\$ 22,580

Office Expenses—\$16,220

Wreath for watchman's funeral	..	..	..	..	..	\$ 50
Office cleaning	..	..	..	..	..	1,200
Income Tax penalty for not filing the partnership return	..	..	..	..	..	250
Partitioning of office (not moveable)	..	..	..	..	..	1,050
Newspapers and magazines	..	..	..	..	..	75
Cost of removal to new office—(not extraordinary)	..	..	..	..	..	905
Rent for office	..	..	..	..	..	10,840
Water and light	..	..	..	..	..	600
A new carpet each for partner's offices	..	..	..	..	..	1,250
						<u>\$ 16,220</u>

Insurance—\$3,020

Goods in transit	..	..	..	..	..	\$ 1,500
Stock in trade	..	..	..	..	..	1,200
Office building including fixture and fittings	..	..	..	..	..	320
						<u>\$ 3,020</u>

Delivery Expenses—\$22,030

Petrol, oil etc. for vans	..	..	..	..	..	\$ 12,000
Repairs to vans	..	..	..	..	..	1,500
New tyres for vans	..	..	..	..	..	550
Hire of outside vehicles	..	..	..	..	..	5,050
Traffic fine incurred by the firm's driver in the course of his duties	..	..	..	..	..	50
Cost of delivery of new van bought in Singapore	..	..	..	..	..	350
Walkie-talkies installed in the vans	..	..	..	..	..	2,530
						<u>\$ 22,030</u>

Advertising—\$34,610

*Newspaper advertising	..	..	..	..	..	\$ 13,550
*T.V. advertising	..	..	..	..	..	10,050
New neon signs	..	..	..	..	..	5,500
Free gifts for customers	..	..	..	..	..	1,800
Calenders for customers	..	..	..	..	..	2,510
Replacing a signboard of the firm's name—(no improvement)	..	..	..	..	..	1,200
						<u>\$ 34,610</u>

*These expenses are considered normal and are agreed by the D.G. as such.

Repairs—\$10,000

Alteration of windows in the office	..	..	..	..	\$ 1,075
New window curtains	..	..	..	..	225
One table for typist	..	..	..	..	150
Repairs to locks	..	..	..	..	15
1 Burglar alarm and fitting charges	..	..	..	..	350
Whitewashing and painting	..	..	..	..	2,500
Repairs and polishing of office tables and chairs	..	..	..	..	385
1 iron gate to replace the old one	..	..	..	..	200
Replacement of tea cups	..	..	..	..	50
Installation of 5 air-conditioners	..	..	..	..	5,050
					<hr/>
					\$ 10,000

Legal Expenses—\$9,000

Retainer fees	..	..	..	..	\$ 1,000
Renewal of lease of office	..	..	..	..	400
Debts collection	..	..	..	..	3,500
Registration of new trade marks	..	..	..	..	1,500
Renewal of trade marks	..	..	..	..	1,800
Advice on dissolution of partnership	..	..	..	..	700
					<hr/>
					\$ 9,000

Tax—\$7,000

Payroll tax	..	..	..	..	\$ 307
Income tax for the employees (as per employment agreement)	..	..	..	..	2,500
Fee for income tax appeal	..	..	..	..	793
Audit and accounting charges	..	..	..	..	1,000
*Income tax for partners	..	..	..	..	2,400
					<hr/>
					\$ 7,000

* (Soh = \$1,000; Koh = \$800; and Mok = \$600)

Subscriptions—\$1,540

International Chamber of Commerce	..	..	..	..	\$ 500
Chinese Chamber of Commerce	..	..	..	..	500
Rubber goods exporters association	..	..	..	..	200
General Merchants Association	..	..	..	..	340
					<hr/>
					\$ 1,540

Entertainment—\$5,500

Hotel expenses of a representative of supplier of goods	\$ 1,850
A private cocktail party given on the arrival of Mr. Soh's son from U.K.—he has nothing to do with the business—partners have agreed to charge this in the accounts	850
Office refreshments	1,200
Manager's allowance	1,600
	<hr/>
	\$ 5,500
	<hr/>

Travelling Expenses—\$1,500

Trip to Kuala Lumpur by Mr. Koh to settle claim by a customer for late delivery of goods	\$ 350
Transport by salesmen visiting the customers	1,150
	<hr/>
	\$ 1,500
	<hr/>

Printing and Stationery—\$1,525

Printing of invoices, receipts, and books	\$ 1,525
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Depreciation—\$2,575

It is on fixed assets of the firm.

No Capital allowances have been claimed by the firm.

ILLUSTRATION V — SOLUTION

**Messrs. Soh, Kok and Mok
Computation of Adjusted Profit**

Net profit as per accounts to 31.12.1970	\$12,000
Add: Office expenses—	
Income tax penalty	250
Partitioning of office	1,050
New carpets	1,250
Delivery expenses—	
Delivery cost of new van	350
Walkie-talkies	2,530
Advertising—	
New Neon Signs	5,500

Repairs—	
Alteration of windows	1,075
New window curtains	225
One table for typist	150
1 Burglar alarm	350
Installation of 5 air-conditioners	5,050
Legal expenses—	
Registration of new trade marks	1,500
Advice on dissolution of partnership	700
Tax—	
Fee for income tax appeal	793
Entertainment—	
Cocktail party for Soh's son	850
Depreciation	2,575
Divisible profit	36,198
Add: Partner's salary	7,200
Income Tax for partners	2,400
Adjusted profit	\$45,798

Statutory Incomes of Partners

Name of partner	Profit Sharing ratio	Amount of D. profit	Salary	Income Tax	Total S.I.
Soh	3	\$18,099	\$1,200	\$1,000	\$20,299
Koh	2	12,066	2,400	800	15,266
Mok	1	6,033	3,600	600	10,233
		\$36,198	\$7,200	\$2,400	\$45,798

Year of assessment 1971—Soh \$20,299; Koh \$15,266; Mok \$10,233

ILLUSTRATION VI — QUESTION

6. From the following balance sheet and profit and loss account of the Soda Universal (Pte.) Limited and the information given below compute the tax payable by or refundable to the company for the years of assessment 1969, 1970, and 1971. The company was incorporated on 1st November 1969 but commenced business on 1st December 1969.

Soda Universal (Pte.) Ltd.

Trading and Profit and Loss Account for the year ended

30th November, 1970.

Manufacturing costs	\$175,551	Sales	\$ 255,742
Gross profit c/d	80,191		
	<u>\$255,742</u>		<u>\$255,742</u>

Administration and General Expenses

Salaries	\$ 25,320	Gross profit b/d	\$ 80,191
Leave pay and passage	2,000	Cash discount	90
Rent, water and electricity	4,382	Profit of sale of machinery	300
Fire insurance	72	Dividends (net)	600
Accident insurance	67		
Repairs	3,872		
Assessment	6,034		
Bank charges and interest	603		
Legal expenses	820		
General expenses	4,834		
Depreciation	1,513		
Bad debts provision	100		
Net profit c/d	31,564		
	<u>\$ 81,181</u>		<u>\$ 81,181</u>
Provision for income tax	10,000	Net profit b/d	\$ 31,564
Proposed dividend 5% less tax	15,000		
Profit unappropriated	6,564		
	<u>\$ 31,564</u>		<u>\$ 31,564</u>

Soda Universal (Pte.) Limited

Balance Sheet as at 30th November, 1970.

Share Capital	Authorised and Fully Paid	Fixed Assets	
500,000 shares of \$1 each	\$500,000	Land and building	\$250,000
Capital Reserves:		Plant and machinery	100,000
Share premium	5,000	Furniture and fit- tings	\$50,000
Revenue Reserves:		Less depreciation	1,513
Profit and loss Account	6,564		<u>48,487</u>
	<u>\$511,564</u>		\$398,487
		Investments	\$ 80,000

Current Liabilities

Trade creditors	\$ 50,000	
Accrued expenses	1,800	
Income tax	10,000	
Proposed dividends	15,000	76,800
		<u>588,364</u>

Current Assets

Stock	\$70,000	
Debtors	21,000	
Cash in hand and at bank	18,877	109,877
		<u>588,364</u>

1. Manufacturing Costs—\$175,551

This include carriage inward of \$162 on the weaving machines.

2. Leave Pay and Passage—\$2,000

Leave pay and passage paid	..	..	..	..	..	1,000
Provision for leave pay and passage	..	..	..	..	..	1,000
						<u>2,000</u>

3. Accident Insurance—\$67

Premium was paid in respect of a director's life, who was travelling on company's business.

4. Repairs—\$3,872

New fencing for the factory	..	..	\$1,500	} Industrial building allowances are to be claimed.
Partitioning a room in the factory	..	..	1,200	
Other repairs all allowable	..	..	1,172	
			<u>3,872</u>	

5. Assessment—\$6,034

This was in respect of the factory building.

6. Legal Expenses—\$820

In respect of a proposed lease to be taken of a new godown	..	..	\$ 150
Claim against the architects for defective construction of factory building	..	..	500
Collection of trade debts	..	..	170
			<u>820</u>

7. General Expenses—\$4,834

One new carpet for board room	..	..	..	..	\$ 350
All other expenses—allowable	..	..	..	..	4,484
					<u>4,834</u>

8. Bad Debts Provision

Specific provision	..	..	..	..	..	..	\$ 50
General provision	..	..	..	..	..	..	\$ 50
							<u>\$100</u>

9. Profit on Sale of Machinery—\$300

A colouring machine was bought originally on 1st December 1969 for \$15,000.

It was sold on 15th December, 1969 at a profit of \$300 and a new colouring machine was bought on 16th December, 1969 for \$15,000.

10. Dividends (Net) —\$600

It was declared payable on 25th December, 1969 by a Malaysian company after deduction of tax at source.

11. Details of Fixed Assets on which Capital Allowances were Claimed—Land and Building¹

1.12.1969	Land	..	..	..	..	..	\$100,000
	Factory building completed on 30th November 1969	..	..				150,000
							<u>\$250,000</u>

Date of Purchase	Plant and Machinery		Rate
1.12.1969	2 Weaving Machines	\$ 50,000	7½ %
16.12.1969	1 Colouring machine	15,000	7½ %
10.1.1970	2 Motor trucks	20,000	20 %
30.11.1970	2 Motor cars	15,000	20 %
		<u>\$100,000</u>	

Furniture and Fittings

1.12.1969	Electrical wiring for air-conditioners	350	} 10 %
12.12.1969	14 Air-conditioners	14,000	
20.2.1970	5 Cabinets	2,450	5 %
20.2.1970	12 Tables	1,200	5 %
20.2.1970	50 Chairs	1,500	5 %
20.2.1970	20 Cupboards fixed in the walls in the factory	15,000	—Nil-industrial building allowances are to be claimed.
20.2.1970	10 Type-writers plus 2 adding machines	15,500	
		<u>\$ 50,000</u>	

ILLUSTRATION VI — SOLUTION

Soda Universal (Pte) Ltd.
Computation of Adjusted Profit

Net Profit as per a/cs to 30.11.1970		\$31,564
Add: Manufacturing costs		162
Leave pay and passage provisions	2,000	
Less paid	1,000	1,000
Repairs		2,700
Legal expenses		650
General expenses		350
Depreciation		1,513
Bad Debts provision	100	
Less specific provision	50	50
		37,989
Less: Profits on the sale of Machinery	300	
Dividends net	600	900
Adjusted Profit		\$37,089
Less: Capital allowances		
I.B.A.	20,184	
W & T	42,162	62,346
Capital Allowances c/f		\$25,257

	Y/A 1969	Y/A 1970	Y/A 1971
Income	NIL	Dividend gross 1,000	NIL C.A. C/F 25,257
Income Tax payable	NIL	400	NIL
Less Tax deduction at source	—	400	—
		NIL	

Soda Universal (Pte) Ltd.
Wear and Tear Schedule

	Industrial Building 2%	Fur. & Fitting 5%	P. & M. 7½%	Elec. Eqp. 10%	Office Eqp. 10%	Motor Vehicles 20%	Total
Purchases to 30.11.1970	168,200	5,150	65,162	14,350	15,500	35,000	
Y/A 1971							Y/A 1971
I.B. I.A. @ 10%	16,820	—	—	—	—	—	I.B. I.A. 16,820
I.B. A.A. @ 2%	3,364	—	—	—	—	—	I.B. A.A. 3,364
							<u>20,184</u>
I.A. (others) @ 20%	—	1,030	13,032	2,870	3,100	7,000	I.A. 27,023
A.A. (others)	—	258	4,887	1,435	1,550	7,000	A.A. 15,130
W.D.V.		3,862	47,243	10,045	10,850	21,000	42,162

NOTE: Some of the problems here cannot be solved by using this book, but need a reference to the comprehensive "Malaysian Income Tax"

APPENDIX I

EXAMINATION PAPERS WITH WORKED SOLUTIONS

UNIVERSITY OF MALAYA
THIRD YEAR EXAMINATION FOR THE DEGREE IN ECONOMICS
SESSION 1969/70
ECONOMICS: COURSE 334

TAXATION

Friday, 16 January 1970.

9.00-12.00 noon (3 hours)

Answer **ANY TWO** questions from Section A, and

answer **ANY FOUR** questions from Section B.

All questions refer to the Malaysian Income Tax Act, 1967).

SECTION A

(Answer any **two** only)

1. An individual arrives in Malaysia for the first time on 1.12.1962 and has the following history:—

1.12.1962 to 31.12.1962	-	-	-	-	-	in Malaysia
1.1.1963 to 30.9.1963	-	-	-	-	-	in Malaysia
year ended 31.12.1964	-	-	-	-	-	not in Malaysia
year ended 31.12.1965	-	-	-	-	-	not in Malaysia
year ended 31.12.1966	-	-	-	-	-	not in Malaysia
1.12.1967 to 31.12.1967	-	-	-	-	-	in Malaysia
year ended 31.12.1968	-	-	-	-	-	in Malaysia

the individual has no intention of leaving Malaysia within the next five years.

State the basis years in which the individual was a resident and was ordinarily resident. Substantiate your answers with reasons.

(10 marks)

2. An individual had the following income for the year ended 31.12.1967:—

Salary	-	-	-	-	-	\$18,000
Commission	-	-	-	-	-	5,000

He received an entertainment allowance of \$200/- per month during the year. He was provided by the company with a servant whose salary paid by the company was \$150/- per month. He was provided with a furnished house. The house was rented by the company, which paid a rental of \$1,000/- per month. It was agreed with the Department of Inland Revenue

that the individual spent \$1,500/- per annum on entertaining the clients of the company. Calculate the Adjusted and Statutory income from his employment for the year of assessment 1968.

(10 marks)

3. State the types of remuneration included for payroll tax purposes and define the terms employee and employer in respect of payroll tax.

(10 marks)

SECTION B

(Answer any four only)

4. An individual B has a business consisting of the extraction of timber from a forest in Malaysia and also saw milling. A summary of the profit and loss account for the year ended 31.12.1968 is as follows:—

Expenses in felling timber	-	\$200,000	Sales of logs	-	-	-	\$500,000
Saw milling expenses	-	100,000	Sale of sawn timber	-	-	-	80,000
General Administrative Expenses	-	-	-	-	-	-	<hr/>
	-	50,000					\$580,000
Net Profit	-	-	-	-	-	230,000	<hr/>
							\$580,000

The timber used in the saw milling part of the business is valued at cost of \$100,000/- and market value of \$90,000/-. Capital allowances for year of assessment 1969 applicable to timber operation are \$40,000/-. Calculate the timber profit tax for the year of assessment 1969.

(20 marks)

5. An individual who is ordinarily resident for the basis year 1968 has the following income:—
- | | | | | |
|---|---|---|---|--------------------|
| Dividends from a company in Malaysia | - | - | - | \$600 (Net) |
| Shares distributed by a Malaysian Company | - | - | - | 300 (Market Value) |

Interest from:—

- | | | | | | | |
|----------------------------|---|---|---|---|---|--------|
| (i) A Bank in Canada | - | - | - | - | - | \$ 400 |
| (ii) A United Kingdom Bank | - | - | - | - | - | 1,000 |
| (iii) A Malaysian Bank | - | - | - | - | - | 2,000 |

He received rent for the year in respect of properties amounting to \$70,000/- out of which \$30,000/- was three years' rent received in advance for a property bought on 1.1.1968.

Expenses incurred during the year ended 31.12.1968 was:—

- | | |
|---|-------------|
| (i) Interest paid on money borrowed for the purchase of property on 1.1.1968 | was \$300/- |
| (ii) Repairs to properties amounting to \$12,000/- out of which \$3,000/- was spent on property bought on 1.1.1968. | |

Calculate the statutory income in respect of the various sources for the year of assessment 1969.

(20 marks)

6. An individual arrived in Malaysia for the first time in December 1967 and stayed throughout 1968. Had the following income for the year ended 31.12.1968.

Employment in Malaysia	-	-	-	-	-	-	\$30,000
Travelling Allowance in Malaysia	-	-	-	-	-	-	5,000
Accommodation (unfurnished)—defined value	-	-	-	-	-	-	10,000
Interest from a United Kingdom Bank	-	-	-	-	-	-	4,000
Dividends (Malaysia)	-	-	-	-	-	-	6,000 (Net)

His wife arrived in Malaysia in October 1968. They have four children:—

- (i) Born in 1946 and attending University of London. Expenditure per month is \$300/-.
- (ii) Born in 1952 and attending Public School in Edinburgh at a cost of \$500/- per month.
- (iii) Born in 1954 and attending school in Malaysia.
- (iv) Born in 1960 and attending school in Malaysia.

A joint wife assurance policy, securing a capital sum at death of \$50,000/- with profit was taken out by the individual in 1955 from a company in the United Kingdom. A life assurance premium of \$4,000/- per year is paid to this United Kingdom insurance company.

Calculate the income tax chargeable in respect of the individual for the year of assessment 1969.

(20 marks)

7. A husband and wife both resident in Malaysia were living together in 1967. The husband's adjusted income from each source for the year ended 31st December 1967 was as follows:—

<i>A</i> Company, Ltd.	-	-	-	-	-	\$12,000 (Profit—Not Dividend)
Interest from Fixed Deposit	-	-	-	-	-	2,000
<i>B</i> Company, Ltd.	-	-	-	-	-	9,000 (Loss)

Losses brought forward under Section 44(5) were \$6,000/-.

The wife's adjusted income for the year ended 31st December 1967 was as follows:—

<i>X</i> Company, Ltd.	-	-	-	-	-	\$10,000 (Profit—Not Dividend)
Interest from Savings Account	-	-	-	-	-	4,000
<i>Y</i> Company, Ltd.	-	-	-	-	-	3,000 (Profit—Not Dividend)

Loss brought forward under section 44(5) in respect of the wife's business was \$3,000/-.

Compute aggregate of the husband's and wife's total income for the year of assessment 1968.

(20 marks)

8. A partnership consists of *A* and *B* and makes up accounts to 30th of June each year.

A has a salary of \$8,000 per annum and *B* \$10,000 per annum. The ratio of sharing profit is 1:2 for *A* and *B* respectively. On 30.9.1968 *A* leaves the partnership and *C* and *D* join the partnership. The new arrangements are:—

- B* receives a salary of \$10,000 per annum
- C* receives a salary of \$ 6,000 per annum
- D* receives a salary of \$ 4,000 per annum

The new profit sharing ratio for *B*, *C* and *D* are 2:1:1 respectively.

The accounts for the year ended 30.6.69 show a loss of \$30,000/- after charging the partners' salaries and other allowable expenses.

Calculate the statutory income/loss of each partner.

(20 marks)

9. A company with accounting year ending 31st December purchased plant and machinery under hire purchase terms. The normal cash price of the plant was \$10,000/-.

The hire purchase terms were:—

(i) Deposit of \$4,000/- on 1st January 1967.

(ii) 24 instalments of \$350/- per month from 31st January 1967.

Calculate the capital allowances for the year of assessment 1968, 1969 and 1970.

(20 marks)

10. An individual has the following sources and amount of adjusted income:—

	Year ended 31.12.67	Year ended 31.12.68
Business - - - - -	\$ 5,000 (Loss)	\$20,000 (Profit)
Rent - - - - -	10,000	Nil (Loss of \$4,000)
Interest - - - - -	5,000	6,000
Gifts to Approved Institutions - -	1,000	1,000

Calculate the development income for the year of assessment 1968 and 1969.

(20 marks)

JANUARI 1971

MASA: 3 jam

Answer any **ONE** question from Section A,

any **TWO** questions from Section B, and

any **TWO** questions from Section C.

Answer **FIVE** questions in all.

The questions are based on the Malaysian Income Tax Act, 1967. The rates of tax given are as follow:—

Chargeable Income	Rate of Tax
For every dollar of the first	\$ 2,500 - - - - - 6%
For every dollar of the next	2,500 - - - - - 9%
For every dollar of the next	2,500 - - - - - 12%
For every dollar of the next	2,500 - - - - - 15%
For every dollar of the next	5,000 - - - - - 20%
For every dollar of the next	5,000 - - - - - 23%
For every dollar of the next	5,000 - - - - - 25%
For every dollar of the next	10,000 - - - - - 30%
For every dollar of the next	15,000 - - - - - 40%
For every dollar exceeding	50,000 - - - - - 50%

SECTION A

Answer any **ONE** question from this section

1. An individual arrived in Malaysia for the first time in 1963 and has the following history:—
- 1.7.1963 to 30.8.1963 in Malaysia
 - 1.4.1964 to 30.4.1964 in Malaysia
 - 1.10.1965 to 30.11.1965 in Malaysia
 - 1.8.1966 to 31.10.1966 in Malaysia
 - 1.1.1967 to 31.12.1967 in Malaysia
 - 1.1.1968 to 31.12.1968 in Malaysia
 - 1.1.1969 to 28.2.1969 in Malaysia

The individual leaves Malaysia with no intention of returning on 28th February, 1969.

State the basis year in which the individual was a resident and ordinarily resident.

Substantiate your answers with reasons.

(10 marks)

2. An individual not ordinarily resident for the basis year 1968 has the following sources of income for year ended 31.12.1968:—

(i) Rents from properties in Malaysia - - -	\$10,000
(ii) Interest from bank in London remitted to Malaysia - - - - -	2,000
(iii) Dividends from a London Company - -	3,000 (Gross)
(iv) Dividends from a Malaysian Company - -	5,000 (No tax deducted by the company)
(v) One house furnished, rateable value - -	1,000 (Vacant all year)
(vi) One house occupied during 3 months of the year, otherwise vacant - - - - -	12,000 (Rateable value)

Calculate the statutory income in respect of the various sources for the year of assessment 1969.

(10 marks)

SECTION B

Answer any **TWO** questions from this section.

3. X, an individual ordinarily resident in Malaysia for the basis year 1968, was divorced from his wife on 1st April, 1968. He re-married on 1st October, 1968, his present wife being resident and a citizen. X's 1969 return shows the following income for the year ended 31st December, 1968:—

Business Loss - - - - -	\$8,000
Capital Allowance - - - - -	7,000
Dividend (Net) - - - - -	6,000

Ex Wife's Income

Employment - - - - -	\$6,000
Interest (Non-Malaysian) - - - - -	400

Present Wife's Income

Business No. 1	-	-	-	-	-	-	\$4,000 (Loss Brought Forward \$3,000)
Business No. 2	-	-	-	-	-	-	8,800 (Loss)
Employment	-	-	-	-	-	-	8,000
Interest	-	-	-	-	-	-	200

X claims relief on alimony of \$200 per month made to his former wife and the following children by his previous marriage:—

- Born in 1946, attending University in Australia. Paid \$1,000/- per annum on his maintenance as the child worked during vacation earning \$1,800/.
- Born in 1949, attending University of Malaya. As she married on 1st May 1968 he only expended \$600/- for her maintenance and education.
- Born on 1st January, 1953, attending school during the year but commenced employment in December, 1968 earning a salary of \$500/.
- Born in 1954, X paid a premium of \$600/- for 1968 to enable the child to be articled to an Accountancy firm.
- Born in 1956, attending cooking class. Paid \$50/- per month for her maintenance.

The former wife has the custody of the fourth and fifth children. She spends \$100/- per month on maintenance, on each child throughout the year.

X also claims the following:—

- Endowment Policy on self:

Capital sum	-	-	-	-	-	-	\$30,000
Premium	-	-	-	-	-	-	2,500
Bonus for the year	-	-	-	-	-	-	500

- Ex-Wife's contribution to E.P.F. \$300/- per annum.
- Present wife's contribution to E.P.F. \$360/- per annum.

Calculate the income tax liability of X for the year of assessment 1969.

(25 marks)

- A firm of wholesalers, which normally made up its accounts to 30th September each year, has the following agreement in force up to 31st December, 1967:—

Salary A	-	-	-	-	-	-	\$6,000 per annum
Salary B	-	-	-	-	-	-	4,000 per annum
Interest A	-	-	-	-	-	-	\$1,000 per annum
Interest B	-	-	-	-	-	-	500 per annum

Share of Profit A— $\frac{2}{3}$

Share of Profit B— $\frac{1}{3}$

Partner *B* left on 31st December, 1967 and his son *C* succeeds him on 1st January, 1968. Under the new agreement, the accounts were to be made up to 30th September, 1968 and then to 31st December, 1968 and to 31st December for subsequent years. The new allocations are:—

Salary <i>A</i>	-	-	-	-	-	-	-	\$6,000 per annum
Salary <i>C</i>	-	-	-	-	-	-	-	2,000 per annum
Interest <i>A</i>	-	-	-	-	-	-	-	\$1,000 per annum
Interest <i>C</i>	-	-	-	-	-	-	-	600 per annum
Share of Profits <i>A</i> — $\frac{1}{3}$								
Share of Profits <i>C</i> — $\frac{1}{3}$								

The provisional adjusted incomes are as follows:—

Accounts year ended	30.9.1967	-	-	-	-	-	-	\$ 7,500
Accounts year ended	30.9.1968	-	-	-	-	-	-	\$35,075
Period from 1.10.1968 to	31.12.1968	-	-	-	-	-	-	\$ 7,000

You are required to allocate the income for the relevant periods and calculate the statutory income of each partner for the relevant years of assessment.

(25 marks)

5. An individual *A* has the following income for the year ended 31st December, 1967. The mining lease is on a profit sharing basis, *A* taking 50% of the net profits.

Business Income

Gross income from sale of tin	-	-	-	-	-	-	-	\$100,000
Gross income from sale of rubber	-	-	-	-	-	-	-	50,000
Miscellaneous business income	-	-	-	-	-	-	-	25,000
								<u>175,000</u>
Less: Expenses applicable to tin mining	-	-	-	-	-	-	-	\$20,000
Expenses applicable to rubber production	-	-	-	-	-	-	-	5,000
General Working Expenses and overheads	-	-	-	-	-	-	-	40,000
								<u>65,000</u>
Adjusted income from business	-	-	-	-	-	-	-	<u>\$110,000</u>
Gross income from mining lease (50% basis)	-	-	-	-	-	-	-	\$15,000
Less: Expenses (50% basis)	-	-	-	-	-	-	-	5,000
								<u>10,000</u>
Gross income from interest and dividends								5,000
								<u>\$125,000</u>

Business Capital Allowance \$20,000/- for year of assessment 1968.

Gift to Government \$1,000/-

Tin concentrates sold 60 piculs in the business and 30 piculs in the Mining Lease.

Calculate the taxable tin profit for the year of assessment 1968.

(25 marks)

SECTION C

Answer any **TWO** questions from this Section.

6. An individual not resident and not a citizen of Malaysia has a wife who is ordinarily resident in Malaysia for the basis year 1968. They have the following income for the year ended 31st December, 1968.

Husband:	Employment income (Malaysian)	-	-	-	-	-	-	\$ 8,000
	Pension from former employment shown above	-	-	-	-	-	-	4,000
	Dividend from Malaysian (Net)	-	-	-	-	-	-	3,600
	Bank Interest (Non-Malaysian)	-	-	-	-	-	-	10,000
Wife:	Business (Malaysian)	-	-	-	-	-	-	\$12,000
	Interest (Malaysian)	-	-	-	-	-	-	6,000

They have two children over sixteen attending university in Australia, on each of whom he expanded \$2,000/- per annum.

Calculate the income tax payable for 1969 showing all reliefs due to the taxpayer.

(20 marks)

7. Company *A* (accounting date 31st of December) constructed in 1960 at a cost of \$260,000 including site \$10,000, a building which was leased to Company *B* for 20 years from 1st September, 1960 at an annual rent of \$10,000/-. Company *B* was an old established food manufacturing company and used the whole of the building as a factory. In 1967 Company *B* expended and built an extension to the existing factory, expenditure being.

Year ended 31.12.1967

Building cost	-	-	-	-	-	\$15,000
Architect's Fees	-	-	-	-	-	8,000
Site cost	-	-	-	-	-	5,000

Year ended 31.12.1968

Building cost	-	-	-	-	-	\$52,000
---------------	---	---	---	---	---	----------

The extension was brought into use on the 1st of October, 1968. In 1970 Company *B* purchased the original building from Company *A* for \$160,000 including site cost \$10,000/-.

Calculate the allowances, if any, due to Companies *A* and *B*.

(20 marks)

8. An individual has income from:—

- a business '*A*' consisting wholly of the extraction of timber from a forest in Malaysia;
- a business '*B*' consisting of the extraction of timber from a forest in Malaysia and saw-milling;
- interests and dividends.

Summaries of the profit and loss accounts of the two businesses for the year ended 31st December, 1968 are as follows:—

Business 'A'

General operating expenses	\$200,000	Sale of logs - - -	\$500,000
Depreciation of plant and machinery - - -	50,000		
Administrative expenses -	30,000		
Net Profit - - -	220,000		
	<u>\$500,000</u>		<u>\$ 500,000</u>

Business 'B'

Expenditure on felling timber - - -	\$ 500,000	Sale of logs - - -	\$1,000,000
Expenditure on saw-milling - - -	100,000	Sales of sawn timber -	200,000
General administrative expenses - - -	200,000		
Net Profit - - -	400,000		
	<u>\$1,200,000</u>		<u>\$1,200,000</u>

Logs used in sawmilling business were valued at cost \$60,000/- and market value \$50,000/-.
Capital allowances in respect of:—

(i) Sawmilling - - - - -	\$10,000
(ii) Timber extraction - - - - -	20,000
(iii) General Office Equipment - - - - -	5,000

Gross income and adjusted income from:—

(i) Interest - - - - -	\$ 5,000
(ii) Dividends (Gross) - - - - -	10,000
Gifts to approved institutions - - - - -	2,000

Calculate the timber profits tax for the year of assessment 1969.

(20 marks)

9. (a) State the types of persons chargeable to development tax.
(b) An individual X and his wife Z are both ordinarily resident for the basis year 1967. They have the following adjusted income for the year ended 31st December, 1967:—

Husband: Business No. 1 (Malaysian) - -	\$10,000
Capital Allowances year of Assessment 1968 - - - -	2,000 (In respect of business No. 1)
Business No. 2 (Non-Malaysian)	
Loss - - - - -	4,000

Balancing Charge Year of Assessment 1968	- - - -	1,000 (In respect of business No. 2)
Capital Allowances Year of Assessment 1968	- - - -	3,000 (In respect of business No. 2)
Interest (Malaysian)	- - -	2,000
Dividends (Malaysian) Net	- -	5,000
Rental income (Malaysian)	- -	2,000
Rental income (Non-Malaysian)	-	3,000
Loss from Business No. 1 not allowed in previous year	- -	2,000
Rental loss from Non-Malaysian properties year ended 31.12.1966	-	1,000
Wife:		
Employment (Malaysian)	- -	\$12,000
Rental income (Malaysian)	- -	5,000
Rental loss (Non-Malaysian)	-	2,000

A donation of \$2,000/- was made in year ended 31st December, 1967 to a State Government. Compute the development tax payable for the year of assessment 1968.

(20 marks)

WORKED SOLUTIONS

1969/70 Paper

Solution to Question 1

It is presumed that residence is to be computed under the Income Tax Act 1967. The actual years do not matter. The answer should be:—

Basis year	Status	Reason
1962	Resident	7(1) (b) NOR
1963	Resident	7(1) (a) NOR
1964	NR	
1965	NR	
1966	NR	
1967	Resident	7(1) (b) NOR (10(6))
1968	Resident	7(1) (a) NOR (10(7))

Solution to Question 2

Computation of the Adjusted and Statutory Income for Y/A 1969

Salary	- - - - -	\$18,000
Commission	- - - - -	5,000
Entertainment Allowance	- - - - -	\$2,400
Cash allowances c/f	- - - - -	\$25,400

Solution to Question 5

Computation of Statutory Incomes for the Year of Assessment 1969

Dividends:

Malaysian Company (Gross) - - - - -	\$ 1,000	
Shares distributed by a Malaysian Co. (Gross) - -	500	\$ 1,500
	<u> </u>	

INTEREST

A Bank in Canada - - - - -	\$ 400	
A United Kingdom Bank - - - - -	1,000	
A Malaysian Bank - - - - -	2,000	3,400
	<u> </u>	

Rents

Property bought on 1.1.1968 - - - - -	\$ 30,000	
Less: Interest paid - - - - -	300	
	<u> </u>	
	\$ 29,700	
Other Properties - - - - -	\$ 40,000	
Less: Repairs - - - - -	9,000	31,000
	<u> </u>	<u> </u>
Total Statutory Income		\$ 65,600
		<u> </u>

Note: Repairs of \$3,000 to property bought on 1.1.1968 will be considered as initial repairs at the time the paper was set and will not be allowed in accordance with the principle of the "Law Shipping Case". However at the present time in view of a subsequent case *Odeon Associated Theatres v. Jones* (1970), this amount of repairs may be allowed (see Page 165),

Solution to Question 6

This individual is a short term resident so he will be chargeable to tax only on his Malaysian income.

Computation of Chargeable Income for the Year of Assessment 1969

Employment in Malaysia - - - - -	\$30,000
Travelling Allowance in Malaysia - - - - -	5,000
	<u> </u>
	\$ 35,000

Accommodation:

The amount will be lesser of \$10,000 or 20% of \$35,000 i.e. \$7,000 - - - - -	7,000
Dividends (gross) - - - - -	10,000
	<u> </u>
Aggregate total income c/f	\$ 52,000

Note 1: Profits of a limited company are distributed only in one of the following ways:—

1. As dividends.
2. As return of capital on reduction of capital.
3. As return of capital on winding up.

In the above question the companies should not be limited companies. In solving the question it is assumed the companies were sole proprietorships.

Note 2: The problem could also be worked on the assumption that this profit of company A Ltd. is *not* the income of the husband, but this would appear to contradict the preamble to the question.

Solution to Question 8

Computation of Statutory Loss of Each Partner

Total Divisible loss	\$30,000
Divisible loss for the period 1.7.1968 to 30.9.1968 (3 months, $\frac{1}{4}$ of \$30,000)	7,500
Divisible loss for the period 1.10.1968 to 30.6.1969 (9 months, $\frac{3}{4}$ of \$30,000)	22,500
	\$30,000

Less:

Salaries to Partners

A—3 months @ 8,000 p.a.	\$2,000
B—3 months @ 10,000 p.a.	2,500
B—9 months @ 10,000 p.a.	7,500
C—9 months @ 6,000 p.a.	4,500
D—9 months @ 4,000 p.a.	3,000
	19,500
Adjusted Loss	\$10,500

Statutory Loss of Each Partner

Name	Ratio of Loss	Divisible Loss	Salary	Statutory Loss
A	$\frac{1}{4}$	\$ 3,750	\$ 2,000	\$ 1,750
B	$\frac{1}{4}$	3,750	2,500	1,250
B	$\frac{3}{4}$	11,250	7,500	3,750
C	$\frac{1}{4}$	5,625	4,500	1,125
D	$\frac{1}{4}$	5,625	3,000	2,625
		\$30,000	\$19,500	\$10,500

Note: It is assumed that the loss was incurred equally each month.

Solution to Question 9

Cash Price	-	-	-	\$10,000
Deposit	-	-	-	4,000
Balance Due				<u>\$ 6,000</u>

Total payable by instalment 350×24	-	-	-	-	\$8,400
Less: Balance Due	-	-	-	-	6,000

Interest Payable for 24 Months					<u>\$2,400</u>
--------------------------------	--	--	--	--	----------------

Interest per month \$100

Sum paid during the year ended 31.12.1967

	Capital	Interest	Total
Deposit	\$4,000	—	\$4,000
12 Instalments @ \$350 p.m.	3,000	\$1,200	4,200
	<u>\$7,000</u>	<u>\$1,200</u>	<u>\$8,200</u>

Sum paid during the year ended 31.12.1968

12 Instalments @ \$350 p.m.	<u>\$3,000</u>	<u>\$1,200</u>	<u>\$4,200</u>
-----------------------------	----------------	----------------	----------------

Capital Allowances

Cost in 1967	-	-	-	-	-	\$7,000
Y/A 1968—I.A. @ 20%	-	-	-	-	\$1,400	
—A.A. @ $7\frac{1}{2}\%$	-	-	-	-	525	1,925
						<u>\$1,925—1968</u>
R.O.E. at 31.12.1967	-	-	-	-	-	\$5,075
Additions in 1968	-	-	-	-	-	3,000
						<u>\$8,075</u>
Y/A 1969—I.A. @ 20% on \$3,000	-	-	-	-	\$600	
—A.A. @ 72% on \$8,075	-	-	-	-	706	1,306
						<u>\$1,306—1969</u>
R.O.E.	-	-	-	-	-	\$6,769
Y/A 1970=A.A. @ $7\frac{1}{2}\%$ on \$6,769	-	-	-	-	-	508
						<u>\$ 508—1970</u>
R.O.E. at 31.12.1969	-	-	-	-	-	<u>6,261</u>

Solution to Question 10

Computation of Development Income for the Y/A 1968 & 1969

	1968	1969
Business Income - - - - -	—	\$20,000
Rent Income - - - - -	10,000	—
Aggregate statutory incomes - - - - -	\$10,000	\$20,000
Less: Business Loss - - - - -	5,000	—
Less: Property Loss - - - - -	—	—
Net aggregate statutory income - - - - -	\$5,000	\$16,000
Less: Proportion of Donation		
$\frac{5,000}{10,000} \times 1,000 =$	500	
$\frac{16,000}{22,000} \times 1,000 =$		727
Development Income	\$ 4,500	\$15,293

Jan. 1971 PAPER

Solution to Question 1

The individual in the question was in Malaysia as follows:—

Basis year	Days
1963	61 days
1964	30 days
1965	61 days
1966	92 days
1967	365 days
1968	365 days
1969	59 days

Basis year	Reason	Result
1966	He was in Malaysia for more than 30 days in 1966 and for each of the three basis years (i.e. 1965, 1964, and 1963) for the four immediately preceding years of assessment (i.e. ys/A 1966, 1965, 1964 and 1963 for which basis years are 1965, 1964, 1963 and 1962) Section 7(1) (c) (ii).	O.R.
1967		O.R.
1968		O.R.
1969	Resident under 7(1) (b) & (c) Not ordinarily resident under 10 (7).	N.O.R.

Solution to Question 2

As the individual is not ordinarily resident for the basis year 1968, his statutory income for the Y/A 1969 will be the income derived in Malaysia. Any income received from or accrued outside Malaysia will not be taxable in Malaysia.

Source	Statutory Income
(i) Rents from Properties in Malaysia - - - -	\$10,000
(iv) Dividends from a Malaysian company ($\frac{100}{60} \times 5,000$) -	8,333
(v) One house furnished (rateable value) - - -	1,000
(vi) One house owner occupied for 3 months (rateable value)	\$12,000
Less: Occupied by the owner $\frac{3}{12}$ of \$12,000 - - -	3,000
	9,000

(Note: It is assumed that the house was furnished if it had been unfurnished there would have been no gross income from this source).

Solution to Question 3

X

Computation of Tax Liability for the Year of Assessment 1969**Husband**

Business income - - - - -	Nil
loss c/d \$8,000	
C.A. c/f \$7,000	
Dividends - - - - -	10,000
loss b/d Section (44) (2) - - - - -	8,000
	\$ 2,000

Ex-wife (see note below)

Nil

Present wife

Business No. 1 income - - - - -	4,000
Less: Loss b/f Sec. 43 (2) - - - - -	3,000
	1,000
Employment - - - - -	8,000
Interest - - - - -	200
	9,200
Less: Business No. 2 loss - - - - -	8,800
	\$ 400

Aggregate total income:

Husband - - - - -	2,000
Present wife - - - - -	400
	2,400
A.T.I. - - - - -	\$ 2,400

Less: Deductions:

Self (husband) - - - - -				\$2,000	
E.I. (self) - - - - -				Nil	
Wife - - - - -				1,000	
Wife's E.I. - - - - -			\$12,000		
less loss - - - - -			11,800		
			<u>200</u>		$200 \times \frac{8}{10} 180$
Children: (b)					750
(c)					500
(d) $\frac{600}{1,800} \times 500$					167
(e) $\frac{600}{1,800} \times 300$					100
L. Assurance			\$2,100		
C.P.F. (present wife) - - - - -			360	2,460	\$7,157
Income Tax Liability - - - - -					Nil

Note: Ex-wife's income cannot be aggregated with husband's income as she has ceased to live together with the husband.

Refund Due from the D.G.

Income Tax payable - - - - -				Nil
Income Tax deducted at source from dividends				4,000
Refund Due - - - - -				<u>\$ 4,000</u>

There is no liability in respect of development tax as there is no development income.

Solution to Question 4

As only provisional adjusted profits are given we have to find out the divisible profits which will be as follows:—

	y/ended	y/ended	P/ended
	30.9.67	30.9.68	31.12.68
A.P. - - - - -	<u>\$ 7,500</u>	<u>\$35,075</u>	<u>\$ 7,000</u>
Less: Salaries			
A - - - - -	6,000	6,000	1,500
B - - - - -	4,000	1,000	—
C - - - - -	—	1,500	500
<i>Carried Forward</i>	<u>10,000</u>	<u>8,500</u>	<u>2,000</u>

	<i>Brought Forward</i>	10,000	8,500	2,000	
Interest					
A	- - - - -	1,000	1,000	250	
B	- - - - -	500	125	—	
C	- - - - -	—	450	150	
		<u>11,500</u>	<u>10,075</u>	<u>2,400</u>	
Divisible					
(Loss)/Profit	- - - - -	(4,000)	25,000	4,600	
Statutory incomes					
y/A 1968 (Business basis period y/e 30.9.1967)		A	B	C	
Loss ($\frac{A}{3} : \frac{B}{3}$)		(3,000)	(1,000)	—	
Salaries for y/e 31.12.1967	- -	6,000	4,000	—	
Interest	- -	1,000	500	—	
		<u>4,000</u>	<u>3,500</u>	<u>—</u>	
Y/A 1969		Total	A	B	C
Business					
Basis period 1.10.67 to 31.12.67					
($\frac{A}{3} : \frac{B}{3}$)	- - - - -	6,250	4,688	1,562	—
1.1.68 to 30.9.68					
($\frac{A}{2} : \frac{C}{2}$)	- - - - -	18,750	12,500	—	6,250
1.10.68 to 31.12.68					
($\frac{A}{2} : \frac{C}{2}$)	- - - - -	4,600	3,067	—	1,533
		<u>29,600</u>	<u>20,255</u>	<u>1,562</u>	<u>7,783</u>
Salaries:	- - - - -	8,000	6,000	—	2,000
Interest	- - - - -	1,600	1,000	—	600
		<u>9,600</u>	<u>7,000</u>	<u>—</u>	<u>2,600</u>
Total Statutory Income		<u>\$39,200</u>	<u>\$27,255</u>	<u>\$1,562</u>	<u>\$10,383</u>

Solution to Question 5

Calculation of Taxable Tin Profit for the Y/A 1968

Gross income from sale of Tin	- - - - -		\$100,000
Less: Expenses applicable to Tin profits	- - - - -	\$20,000	
General Working expenses and overheads applicable to Tin	- - - - -		
	$\frac{100,000}{175,000} \times 90,000$	22,857	42,857
		<u>—</u>	<u>\$ 57,143</u>

Less: Capital Allowances $\frac{100,000}{175,000} \times 20,000$	-	-	-	-	-	11,428
						<u>\$ 45,715</u>
Add: Income from Mining lease	-	-	-	-	-	10,000
						<u>\$ 55,715</u>
Less: Donations $\frac{1,000}{125,000} \times \$110,000$	-	-	-	-	-	880
						<u>\$ 54,835</u>
Less: Business						
$\frac{75}{100}$ of 60 Piculs \times \$100	-	-	-	-	-	\$4,500
Mining Lease						
$\frac{75}{100}$ of $\frac{50}{100}$ of 30 Piculs of \$100	-	-	-	-	-	1,125
						<u>5,625</u>
Taxable Tin Profit	-	-	-	-	-	<u>\$ 49,210</u>

Solution to Question 6

This is a case where Sec. 130 relief is due as he earns pension.

Tax payable @ 40% on income of \$18,000 derived in Malaysia \$ 7,200

Section 130 Relief

$$\frac{\text{Pension \& Employment}}{\text{Total Income}} \times 7,200$$

$$= \frac{12,000}{18,000} \times 7,200 = 4,800$$

Tax on the assumption of ordinary residence

Malaysian Income	-	-	-	-	-	18,000
Outside Income	-	-	-	-	-	10,000
						<u>28,000</u>
World Income	-	-	-	-	-	28,000
Less P.R.:						
Self	-	-	-	-	-	2,000
Wife	-	-	-	-	-	1,000
E.I.A.	-	-	-	-	-	1,000
Children	-	-	-	-	-	2,500
						<u>6,500</u>
Chargeable Income	-	-	-	-	-	<u>\$21,500</u>

Tax payable @ Scale rates \$ 3,575.00

Tax on pension & employment

$$= \frac{12,000}{28,000} \times 3,575 = \$1,532.14$$

Tax chargeable on pension & employment as non-resident

\$4,800.00

Less tax computed above 1,532.14

Section 130 relief \$ 3,267.86

Solution to Question 8

Computation of Timber Profit Tax for the Year of Assessment 1969

	Business <i>A</i>	Business <i>B</i>	Total
Sales of logs - - - - -	\$500,000	\$1,000,000	\$1,500,000
Add: Market value of logs used in sawmilling -	—	50,000	50,000
		<hr/>	<hr/>
		\$1,050,000	\$1,550,000
Less: General operating Exp. - - - -	200,000	—	
Exp. on Falling Timber - - - -	—	500,000	
Admin. Exp. - - - -	30,000	—	
Prop. of Gen. Adm. Exp. $200,000 \times \frac{1,050,000}{1,300,000}$	—	175,000	
	<hr/>	<hr/>	
	\$230,000	\$675,000	\$905,000
	<hr/>	<hr/>	<hr/>
	\$270,000	\$375,000	\$645,000
		<hr/>	<hr/>
Less: Capital Allowances Timber - - -		\$20,000	
Capital Allowances—General Office Equip. $5,000 \times \frac{1,550,000}{1,750,000}$ - - - -		4,429	24,429
		<hr/>	<hr/>
			\$620,571
Less: 10% of the gross timber income of \$1,550,000			155,000
			<hr/>
Less: Gifts to approved institutions $2000 \times \frac{1,550,000}{1,715,000}$			465,571
			<hr/>
			1,808
			<hr/>
Taxable timber profit: - - - -			463,763
			<hr/>

Timber Profit Tax

Taxable Timber Profit

\$155,000

308,763

\$463,763

Rate

10%

20%

Timber Profit Tax

\$15,500

61,752

\$77,252

Note: Timber log sales (as above)

Sawmilling sales

\$1,500,000

200,000

\$1,700,000

15,000

\$1,715,000

Interest and Dividends income

Solution to Question 9 (a)

A person having a development income is charged to development tax. Development income from (1) a business or (2) letting of property situated in Malaysia.

A person for development tax purposes may be:

1. An individual—having more than \$3,000 development income
2. A limited company—minimum development tax \$500 p.m.
3. A trade association or club—minimum tax \$100 (repealed—no minimum tax)
4. A partner having more than \$2,000 development income from a partnership

Solution to Question 9 (b)**Computation of Development Tax Payable for the Y/A 1968***

* Assumption: Donations deemed to be by husband.

Husband

Business 1	-	-	-	-	-	-	-	-	-	\$10,000	
Less C/A	-	-	-	-	-	-	-	-	-	2,000	\$ 8,000
Business 2	Balance Charge	-	-	-	-	-	-	-	-	1,000	
	Less C/A	-	-	-	-	-	-	-	-	3,000	
	C/A c/f	-	-	-	-	-	-	-	-	(2,000)	Nil
Rent (Malaysian)	-	-	-	-	-	-	-	-	-		2,000
											10,000
Less Sec. 43(2) Loss B/F	-	-	-	-	-	-	-	-	-	2,000	
B/Y Loss (Sec. 44(2))	-	-	-	-	-	-	-	-	-	4,000	6,000
Net Aggregate S.I. from all development Sources	-	-	-	-	-	-	-	-	-		4,000
Less Donations:	$\frac{2,000 \times 4,000}{4,000 + (\text{Non Dev. Income i.e. } 13,333)}$										
	$= \frac{2,000 \times 4,000}{17,333}$										462
D.I. of husband	-	-	-	-	-	-	-	-	-		3,538
D.I. of wife—rent	-	-	-	-	-	-	-	-	-		5,000
D.I.	-	-	-	-	-	-	-	-	-		8,538
Dev. Tax @ 5%	-	-	-	-	-	-	-	-	-		\$426.90

Notes: 1. Non-Development Income of Husband consists of interest 2,000, dividends (gross) 8,333; rent (non-Malaysian) 3,000—i.e. a total of 13,333.

2. Development Income includes rental on Malaysian property only. Also non-Malaysian property loss may not be deducted.

3. See text—chapter XX—for a full exposition.

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