



THE business landscape has changed tremendously over the years. Businesses now transcend national borders and are finding new and innovative ways to do business in response to global megatrends like the shift in global economic power, technological advancements, climate change and scarce resources.

Today's businesses are not only concerned with the bottom line. Meeting and managing the diverse needs and expectations of multiple stakeholders (ranging from employees to shareholders and the board of directors, customers to business partners and regulatory authorities) are just as critical. In recent years, the Companies Commission of Malaysia through its Corporate Responsibility (CR) Agenda, has intensified efforts to promote CR among corporate players. The CR Agenda also encourages Corporate Malaysia to integrate responsible business conduct into their business operations and practices. Reporting on CR activities/practices is mandatory for listed companies.



**Guest
writer**

**BY PHAN WAI
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These developments call for new regulations and policing methods, and stricter compliance requirements as heightened corporate governance takes centre stage, with increased disclosure and transparency requirements under the revised reporting framework. This has inevitably added to the cost of doing business. Technically, these are legitimate business expenses similar to salaries and rental expenses. Should a similar tax treatment apply then, in this case a tax break of 25 sen for every ringgit spent by companies on statutory/regulatory and corporate governance-related compliance costs?

What the law says

Section 33(1) of the Malaysian Income Tax Act 1967 (the ITA) provides that tax deduction will be given for "expenses wholly and exclusively incurred ... in the production of gross income". The words "wholly and exclusively" refer to the requirement for a sole intention behind the incurrence of the expenditure to be established, while the phrase "in the production of gross income" requires a direct nexus (connection) between the incurrence of the expense and the earning of income.

In short, an expense must be incurred solely for the purpose of producing income and not merely for any business-related purpose in order to qualify for a tax deduction. The application of this stringent test has often led to disputes between taxpayers and the tax authorities on the deductibility of business expenses. The question seems to boil down to how liberally or narrowly one reads the law.

If one were to adopt a strict and narrow interpretation of section 33(1), expenses such as audit fees and tax filing fees would potentially be denied a tax deduction albeit revenue in nature. This is because it is argued that such



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Time to ease business costs with tax deductions

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expenses are incurred after and not during the income production process. Put simply, one does not produce income from incurring such expenses. The adoption of this position by the tax authorities has led to the need for the government to issue special deduction orders to accord a specific tax deduction for such expenses.

The list of expenses which are considered as falling outside the purview of section 33(1) (but with no special legislation enacted to grant a deduction) includes expenses to comply with laws, statutory codes and directives such as expenses relating to annual general meetings, periodic listing fees payable to Bursa Malaysia Securities, Central Depository fees, secretarial fees, trustee fees, and registrar fees.

Another important area is financ-

ing. Businesses are allowed a tax deduction for interest charged on loans obtained to fund business operations or acquire capital assets (for example, factory and machinery) used for the purpose of producing income. However, the tax deduction is not extended to other costs of raising funds such as guarantee fees, arranger fees, discounts on bonds issued and other ancillary borrowing costs. As interest charged on borrowings is accepted as deductible, the tax treatment of other borrowing costs should not be differentiated. Similar consideration should also be given to costs related to alternative forms of borrowing and financing instruments offered in the market.

Bringing the law closer to reality

Retaining the existing narrowly-scoped general deduction rule without giving due consideration for the current business landscape and business practices is a very archaic taxation approach. We need to recognise the commercial realities of today and endeavour to ease the cost of doing business in Malaysia. If regulators are of the view that their hands are tied because the letter of the law must strictly be complied with by businesses or risk being challenged by the tax authorities, isn't it time to bring the law closer to the reality of today's business?

Over the years, various countries have amended their tax legislation to widen the scope of deduction for business expenses. The Australian and New Zealand income tax legislations, which have gone through various amendments since inception, currently allow a tax deduction for expenses which are "necessarily incurred in carrying on/in the course of carrying on a business", in addition to expenses which are

incurred in gaining or producing assessable income. The United Kingdom law is also wider than Malaysian law as deduction is given for expenses incurred "for the purpose of trade".

In Singapore, while the general deduction provision is somewhat similar to section 33(1) of the ITA, its government recently amended the law to allow a specific deduction for qualifying statutory and regulatory expenses effective from the year of assessment 2014. This much-welcomed amendment provides certainty to businesses on the deductibility of such expenses which, among others, include expenses incurred to comply with any written law, code, standard, rule or requirement issued by the government, public authority or securities exchange, as well as expenses to study the impact of a proposed law, for example the Foreign Account Tax Compliance Act (FATCA).

The Malaysian government could align the deduction principle to current business reality by replacing the words "in the production of income" with "for the purpose of business or for the purpose of producing income from a source".

Recognising that businesses do not operate in a vacuum and hence the need to incur necessary business expenses, providing a tax deduction for them would thus send a clear message to businesses – that they are encouraged to comply with regulations and meet the country's call for greater governance, transparency and corporate responsibility.

It has been 47 years since the enactment of the ITA. I strongly advocate that the government undertakes a review of the current laws on expense deductibility with the view to widening the scope of deduction and achieving a closer alignment of the law to the business environment of today. This is my Budget 2015 wish list. **FOCUSM**

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