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Capital Allowance for Information and Communication Technology Equipment

In the 2018 Budget, it was announced that companies would be allowed to claim capital allowance on (i) purchase of information and communication technology (ICT) equipment, and computer software packages, and (ii) expenditure relating to the development of customized software comprising consultation fee, licensing fee and incidental fee. The first proposal which has now been legislated in a new gazette order is effectively an extension of the capital allowance on ICT equipment and computer software packages given up to the year of assessment 2016, while the gazette order for the second proposal is still pending.

The contents of the new gazette order, the *Income Tax (Accelerated Capital Allowance) (Information and Communication Technology Equipment) Rules 2018* ("2018 Rules"), are very much similar to the earlier Income Tax (Accelerated Capital Allowance) (Information and Communication Technology Equipment) Rules 2014 ("2014 Rules"). In particular, the scope of qualifying expenditure and non-application provisions remain unchanged. The notable differences between the 2018 and 2014 Rules are as follows:

	2014 Rules	2018 Rules
Effective period	YA 2014 to YA 2016	From YA 2017
Capital Allowance rates	Initial allowance at 20% Accelerated annual allowance at 80%	Initial allowance of 20% Annual allowance at **20%**
Specific deeming provision relating to hire purchase agreement (HPA)	Specific provision is made under Rule 4. This rule is equivalent to paragraph 46 of Schedule 3 of the Income Tax Act 1967 (ITA), which deems a person who incurred qualifying expenditure pursuant to a HPA as the owner of the underlying asset, and that the capital portion of instalments made in each YA is taken to be the qualifying expenditure incurred for the YA.	No specific provision is provided.
Specific clawback provision	Specific clawback provision is provided under Rule 8, whereby the capital allowance claimed will be withdrawn if the asset is disposed* within two years of its purchase. ** sold, conveyed, transferred, assigned or alienated, with or without consideration*	No specific clawback provision is provided.

Our comments

Since there are no changes to the interpretation of "information and communication technology equipment", taxpayers will still be guided by the explanation provided in the Public Ruling 12/2014 – Qualifying plant and machinery for claiming capital allowance ("PR 12/2014") in determining what items fall within "software package or software systems". This has been explained in the public ruling to mean "computer software purchased together with the computer equipment from a supplier or purchased separately from a software supplier" [paragraph 8.1(iii) of PR 12/2014].

The public ruling has also specifically stated that software development expenditure such as consulting fees, licence fee and other incidental charges are not part of expenditure for the provision of software. [paragraph 8.2(ii) of PR 12/2014].

In the absence of specific deeming provisions relating to treatment of HPA and clawback provision for asset disposals within two years of purchase:

- *The qualifying expenditure for capital allowance purposes for assets acquired under a HPA is determined in accordance with paragraph 46 of Schedule 3 of the ITA.*
- *Paragraph 71 of Schedule 3 of the ITA which provides for a clawback of capital allowance claimed for assets disposed within two years of their purchase, would apply as appropriate.*

Revised Green Technology guidelines

MIDA has issued the revised guideline for Green Technology, which takes effect from 1 July 2018. The revision followed a review undertaken by the Forum on Harmful Tax Practices (FHTP) in 2017 under the Base Erosion Profit Shifting (BEPS) Action Plan 5: "Countering harmful tax practices more effectively, taking into account transparency and substance".

This incentive is classified as a Non-IP regime by the FHTP. Under BEPS Action Plan 5 companies intending to enjoy the benefits of the incentive have to ensure that substantial activities are undertaken in Malaysia. "Substantial activities" for a non-IP regime is defined as having adequate number of full-time employees working in Malaysia with the necessary qualifications and incurring adequate amount of operating expenditure to undertake the services/projects for business purposes in Malaysia.

The following are the salient changes made to the guideline:

Eligibility criteria

- The 5 full time employees required to be employed by the company must be working in Malaysia. [para IV(4)(a)]
- Only income from green technology services will be exempted whilst income from other activities will not be eligible for the exemption. [para IV(4)(c)]
- New criteria – an adequate amount of operating expenditure is to be incurred annually in Malaysia in undertaking the green services / projects for business purposes. Green technology projects for own consumption are exempted from this requirement. The operating expenditure should include services for insurance, legal, banking, ICT and transportation, which should be sourced locally. [para IV(6)]

Treatment of tax incentive approvals [para V(4)]

- Companies granted approval before 16 October 2017 can continue to enjoy the existing incentive until 30 June 2021, without the imposition of the substantial activities requirements.
- Companies granted approval from 16 October 2017 onwards without the substantial activities requirements can only enjoy the existing incentive until the earlier of the publishing of the new guideline/legislation or 31 December 2018.

In addition to changes made to comply with BEPS Action Plan 5, MIDA has also specified in the revised guideline that where a company fails to comply with the conditions in its incentive approval letter, the incentive may be revoked. [para III(1.2)]

BEPS Action Plan 5 imposes the substantial activity requirement on both IP and non-IP regimes. Malaysia's Green Technology incentive falls under the non-IP regime. In the application of the substantial activity requirement to non-IP regimes, a link is required to be established between the income that qualifies for the incentive and the activities necessary to earn the income.

Revised Real Property Gains Tax (RPGT) guidelines

The IRB has issued a revised RPGT guidelines dated 13 June 2018 ("2018 Guidelines") which has incorporated the changes made to the RPGT Act 1976 since the last RPGT Guidelines dated 18 June 2013 ("2013 Guidelines") was issued. Salient details are outlined below.

Allowable losses

Allowable losses are no longer disregarded for disposals made from the 6th year of acquisition if the disposal date is from 1 January 2014. For disposals from 1 January 2014, disposals made from the 6th year after acquisition are technically no longer "exempted" but are instead subject to a "nil" RPGT rate under Schedule 5 of the RPGT Act. Example 3 of the revised guideline illustrates this.

Procedure for aborted sale

The disposer or acquirer is to inform the IRB by furnishing the following:

- Agreement for aborting the sale
- Stamp duty refund letter
- Other official documents to substantiate the aborted sale

Procedure for refund of RPGT to acquirer

In the event that the acquirer wishes to apply for the refund, an approval letter which is duly certified by a Commissioner for Oaths stating the agreement of the disposer to allow the refund to be made to the acquirer is required to be furnished to the IRB. A sample copy of such letter is provided at the end of the 2018 Guidelines.

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