



# Taxavvy

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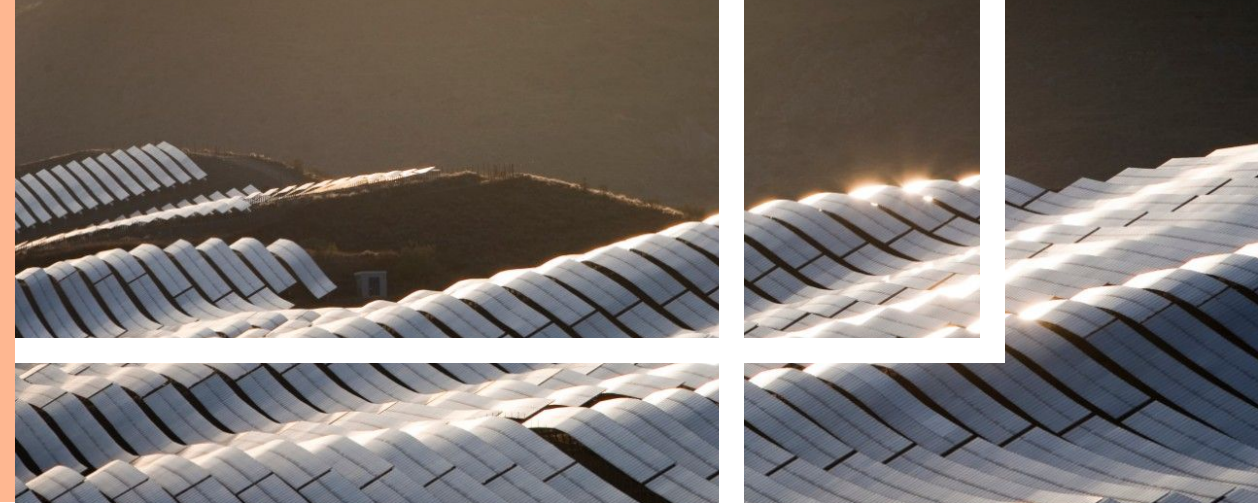


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## Special deductions for research and development

The Inland Revenue Board (IRB) has issued the following:

- Public Ruling 5/2020 - Tax treatment of research and development expenditure part 1 - qualifying research and development activity (“PR 5/2020”)
- Public Ruling 6/2020 - Tax treatment of research and development expenditure part 2 - special deductions (“PR 6/2020”)
- Guidelines on application procedure for special deduction in respect of qualifying research and development activity (“R&D guideline”)
- Various forms in respect of application and claims for the special deductions



PR 5/2020 and PR 6/2020 replace the earlier Public Ruling 5/2004 - Double deduction incentive on research expenditure, and its addendum (“PR 5/2004”). The contents of PR 5/2004 have been significantly rewritten and updated based on current legislation and practices and divided into the 2 new public rulings. The salient new points of the new public rulings are outlined as follows:

### **PR 5/2020 - Tax treatment of research and development expenditure part 1 - qualifying research and development activity**

#### **Definitions**

The legislated definition of research and development (R&D) under section 2 of the Income Tax Act 1967 (ITA 1967) has been included. In addition, PR 5/2020 has included the following definitions:

*Approved research institute* - an institute, including a company licensed under section 45 of the Companies Act 2016 [company limited by guarantee], approved

*by the Minister to mainly carry on research in an industry specified in the approval and to commercially exploit the benefit of such research.*

*R&D company* - a company which provides R&D services in Malaysia to its related company or to any other company.

*Contract R&D company* - a company which provides R&D services in Malaysia only to a company other than its related company.

*Approved research company* - a company, other than a company licensed under section 45 of the Companies Act 2016 [company limited by guarantee], approved by the Minister to mainly carry on research in an industry specified in the approval and to commercially exploit the benefit of such research thereof.

### R&D on information technology (IT) & software

The superseded PR 5/2004 had defined R&D for IT & software separately from the general definition of research. PR 5/2004 also separately explained the different types of R&D activities in the IT & software sector and sectors other than IT & software.

This distinction and dedicated explanation for R&D related to IT & software are no longer made in the new public ruling.

### R&D activity vs. R&D project

PR 5/2020 differentiates between R&D activity and R&D project where:

- An R&D project is a project undertaken to create new knowledge, or new or improved processes to develop new products or services comprising a set of R&D activities and is organised and managed for a specific purpose.
- An R&D activity is an activity undertaken to resolve scientific / technological uncertainties and challenges.

An R&D incentive is claimable at the R&D activity level (provided it is qualifying R&D activity) and not the R&D project level. For example, an R&D project may comprise multiple R&D activities, each of which individually may be a qualifying or non-qualifying R&D activity. Only the qualifying R&D activity within the R&D project would be eligible for the tax incentive.

The distinction between R&D activities and R&D projects is summarised in a table in para 6.4 of PR 5/2020 as follows:

R&D Project	R&D activities (qualifying and non-qualifying activities)	Qualifying and non-qualifying R&D activities grouped to form an R&D Project
Project MAH 1 activity	Qualifying R&D activity	Qualifying R&D activity forms an R&D project
Project YUD 2 activities	Qualifying R&D activity Qualifying R&D activity	Qualifying R&D activities grouped to form an R&D project
Project COV 3 activities	Qualifying R&D activity Non-qualifying R&D activity Non-qualifying R&D activity	Qualifying R&D activity and non-qualifying R&D activities grouped to form an R&D project. (Only the qualifying R&D activity qualifies for the incentive)
Project 19 2 activities	Non-qualifying R&D activity Non-qualifying R&D activity	Non-qualifying R&D activities grouped to form an R&D project. (Both non-qualifying R&D activities do not qualify for the incentive)

### Qualifying R&D activity

In order to be a qualifying R&D activity, the activity must fulfill all the criteria of the R&D definition in section 2 of the ITA 1967, which is broken down as follows:

- a) Has an objective - the objective of the R&D activity has to be clearly defined, i.e. the specific desired outcome to be achieved must be stated. The objective must include:
  - (i) acquiring new knowledge;
  - (ii) creating new products or processes; or
  - (iii) improving existing products or processes.
- b) Novelty or technical risk - the R&D must involve novelty (something new or original), or technical risk which arises out of technological uncertainty because of the knowledge gap between the intended outcome of the R&D and the currently available scientific knowledge.
- c) The R&D is a systematic, investigative and experimental (SIE) study in a field of science or technology.
  - (i) Systematic - planned and structured activities with evidence documented.
  - (ii) Investigative - original investigation into new scientific or technical knowledge and understanding
  - (iii) Experimental - applying a systematic series of structured and repetitive steps, undertaken to test the potential solution.

PR 5/2020 explains the above criteria in detail. In addition, it has also stated that the R&D term covers the following main works:

- Basic research - experimental work to understand the underlying foundations without any application or use in view.
- Applied research - investigation work undertaken towards a specific objective to determine methods to address a specific requirement of a product or process.
- Experimental development - systematic work drawing on existing research results and directed specifically towards the creation of new and improved products or processes.

### PR 6/2020 - Tax treatment of research and development expenditure part 2 - special deductions

#### Definitions

Similar to PR 5/2020, PR 6/2020 has included the following definitions:

- Section 2 definition of R&D
- Approved research institute
- R&D company
- Contract R&D company
- Approved research company

## The special deductions

The superseded PR 5/2004 previously dealt with the following double deductions under the ITA 1967:

- Section 34A - double deduction for revenue expenditure incurred on an approved in-house qualifying R&D activity.
- Section 34B - double deduction for revenue expenditure incurred which is cash contribution to an approved research institute, or payment for services of an approved R&D company, contract R&D company or research institute / company.

In addition to the above double deductions, PR 6/2020 also explains the single deduction under section 34(7) for revenue expenditure incurred on a qualifying R&D activity.

## Qualifying R&D expenditure

### 1) *Moulds, dies and soft tools*

PR 5/2004 previously stated in para 13.1(ii) that where a claim for double deduction is made in one basis period for moulds, dies and soft tools used in developing the prototype unit and these tools are subsequently reused in the production line in the next basis period, the claim in the first basis period must be revised accordingly to apportion the cost between its use in developing the prototype unit and in the production line. Penalty will not be imposed on any additional tax payable arising from the revision.

This paragraph has since been deleted in PR 62020. PR 6/2020 is silent on the tax treatment of moulds, dies and soft tools used to develop prototype units and which are subsequently reused in the production line.

### 2) *Technical service payment*

- Effective from 28 December 2018, a double deduction of expenditure for technical services undertaken outside Malaysia, is only allowed if the payment for such services is not more than 30% (previously 70%) of the total allowable R&D expenditure.
- However, this restriction does not apply to section 34(7). 100% of the total allowable expenditure for technical services undertaken outside Malaysia is allowed as a single deduction under section 34(7).

### 3) *Qualifying expenditure under section 34B*

It is stated in para 9 of PR 6/2020 that a claim for double deduction under section 34B is allowed provided that the revenue expenditure for the R&D activity is a qualifying expenditure. It is also noted from para 6 of PR 6/2020 that details of the qualifying expenditure are to be kept. Clarification needs to be obtained on whether this applies to section 34B as it is a deduction for payments made to an R&D company or research institute.

The public rulings are available on IRB's website [www.hasil.gov.my](http://www.hasil.gov.my) (Legislation > Public Rulings).

## Guidelines on application procedure for special deduction in respect of qualifying research and development activity

The R&D guideline sets out the application procedures, the forms to be completed and the due date for submission of these forms summarised as follows:

Provision	Special deduction	Forms to be submitted	Application / submission due date
Section 34A	Deduction of twice the amount of qualifying expenditure incurred on an in-house R&D approved by the Director General (DG) of IRB.	Form 1 <ul style="list-style-type: none"> <li>application for approved R&amp;D activity</li> <li>to be submitted with supporting documents</li> <li>also applicable for a pioneer company claiming deduction under section 34A(4A) of the ITA 1967</li> </ul>	<u>New project</u> a) R&D activity commenced in first half of financial year - Form 1 to be submitted within 6 months <i>before</i> financial year end. b) R&D activity commenced in second half of financial year - Form 1 to be submitted within 1 month <i>after</i> end of financial year end.
		Form 2 <ul style="list-style-type: none"> <li>claim for double deduction</li> <li>completed after certificate of approval issued by DG of IRB</li> </ul>	<u>Extension project</u> Form 1 to be submitted within 6 months <i>before</i> financial year end.  <u>Certificate issued <i>before</i> tax return filing due date</u> Submitted together at the same time as the tax return.  <u>Certificate issued <i>after</i> tax return filing due date</u> Submitted within 3 months from date the certificate is issued.
Section 34B	Deduction of twice the amount of: <ul style="list-style-type: none"> <li>Cash contribution to a research institution approved by the Minister,</li> <li>Payment for services of an approved research institution or approved research company,</li> <li>Payment for services of a R&amp;D company or contract R&amp;D company.</li> </ul>	Form 3 <ul style="list-style-type: none"> <li>claim for double deduction</li> <li>completed by payor / recipient of services</li> </ul>	Original copy to be kept and furnished upon audit by IRB.

Provision	Special deduction	Forms to be submitted	Application / submission due date
Section 34(7)	Single deduction of the amount of: <ul style="list-style-type: none"> <li>qualifying expenditure incurred on an in-house R&amp;D, or</li> <li>payment for services of a R&amp;D service provider.</li> </ul>	Form 4 <ul style="list-style-type: none"> <li>claim for single deduction</li> </ul>	To be submitted within 30 days after due date for submission of tax return form.

The R&D guidelines provides examples to illustrate the above procedures and are to be read together with PR 5/2020 and PR 6/2020.

The R&D guidelines and forms are available on IRB's website [www.hasil.gov.my](http://www.hasil.gov.my) (Legislation > Technical Guidelines)

## Income Tax (Special Treatment for Interest on Loan) Regulations 2020

Further to the announcement made by Bank Negara Malaysia on 25 March 2020 on the loan moratorium programme (refer to [TaXavvy 37/2020](#)), the Income Tax (Special Treatment for Interest on Loan) Regulations 2020 (“the Regulations”) has now been gazetted. The Regulations take effect from the year of assessment (YA) 2020 and prescribes the special tax treatment on income of financial institutions from interest or profit on loan / financial facilities under the moratorium programme granted to customers.

### Who qualifies for the special tax treatment?

- Licensed banks or licensed investment banks under the Financial Services Act 2013
- Licensed Islamic banks under the Islamic Financial Services Act 2013
- Development financial institutions prescribed under the Development Financial Institutions Act 2002

### What is the special tax treatment?

- Interest due and payable from 1 April 2020 until 30 September 2020 from loans / financing under the moratorium programme shall not constitute the gross income of that bank or financial institution for the basis period for that YA.
- The above interest will be brought to tax in the relevant YA if it is received during the period from 1 April 2020 until 30 September 2020, or becomes receivable on or after 1 October 2020.
- Deduction for the impairment of a loan under the moratorium programme will not be allowed to the bank or financial institution.
- A separate account is to be maintained for interest related to loans / financing under the moratorium programme.

### Type of loan / financing that qualifies for the special tax treatment.

All types of loan / financing under the moratorium programme (except for credit card facilities) granted to individuals, Small and Medium Enterprises (SMEs) and corporate borrowers / customers which are:

- Denominated in Ringgit Malaysia,
- Not in arrears exceeding 90 days as at 1 April 2020 by the individual, SME or company, and
- For a company other than an SMEs, application for the moratorium has been made.

## Definition of SME for purposes of this special tax treatment

The meaning of SME is as assigned under the Small and Medium Industries Development Corporation Act 1995 which is defined by SME Corporation Malaysia as follows:

SME size	Manufacturing sector	Services and other sectors
Medium	Sales turnover of RM15 million to ≤ RM50 million <u>OR</u> No. of employees from 75 to ≤ 200	Sales turnover of RM3 million to ≤ RM20 million <u>OR</u> No. of employees from 30 to ≤ 75
Small	Sales turnover of RM300,000 to < RM15 million <u>OR</u> No. of employees from 5 to < 75	Sales turnover of RM300,000 to < RM3 million <u>OR</u> No. of employees from 5 to < 30
Micro	Sales turnover of < RM300,000 <u>OR</u> No. of employees < 5	Sales turnover of < RM300,000 <u>OR</u> No. of employees < 5

It however, excludes:

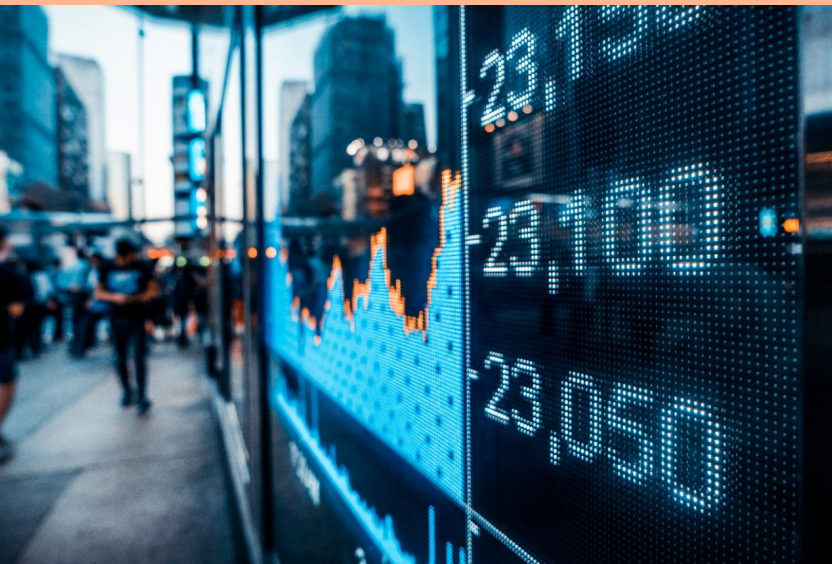
- Entities that are publicly-listed on the main board; and
- Subsidiaries of:
  - Publicly-listed companies on the main board;
  - Multinational corporations (MNCs);
  - Government-linked companies (GLCs);
  - Syarikat Menteri Kewangan Diperbadankan (MKDs); and
  - State-owned enterprises.



## Income tax rules for deduction of listing expenses

Budget 2020 proposed for a tax deduction to be given for listing expenses for technology-based companies and SMEs.

This has now been legislated via the the Income Tax (Deduction for expenses in relation to listing on Access, Certainty, Efficiency (ACE) Market or Leading Entrepreneur Accelerator Platform (LEAP) Market of Bursa Malaysia Securities Berhad) Rules 2020, which was gazetted on 3 September 2020.



### Eligible companies

A technology-based company which applies for listing in the:

- Access, Certainty, Efficiency (ACE) Market, or
- Leading Entrepreneur Accelerator Platform (LEAP) Market

of Bursa Malaysia Securities Berhad from YA 2020 to YA 2022.

### Technology-based company

A company which is involved in the design, development and manufacture, production or application in specified activities in the following fields:

- Advanced electronics and information technology
- Telecommunications
- Equipment / instrumentation, automation and flexible manufacturing systems
- Life sciences and biotechnology
- Healthcare
- Electro-optics, non-linear optics and optoelectronics
- Advanced materials
- Energy
- Aerospace
- Transportation
- Value-added services

### Tax deduction

The tax deduction granted is an amount equivalent to the following expenditure incurred for listing on the ACE Market or LEAP Market:

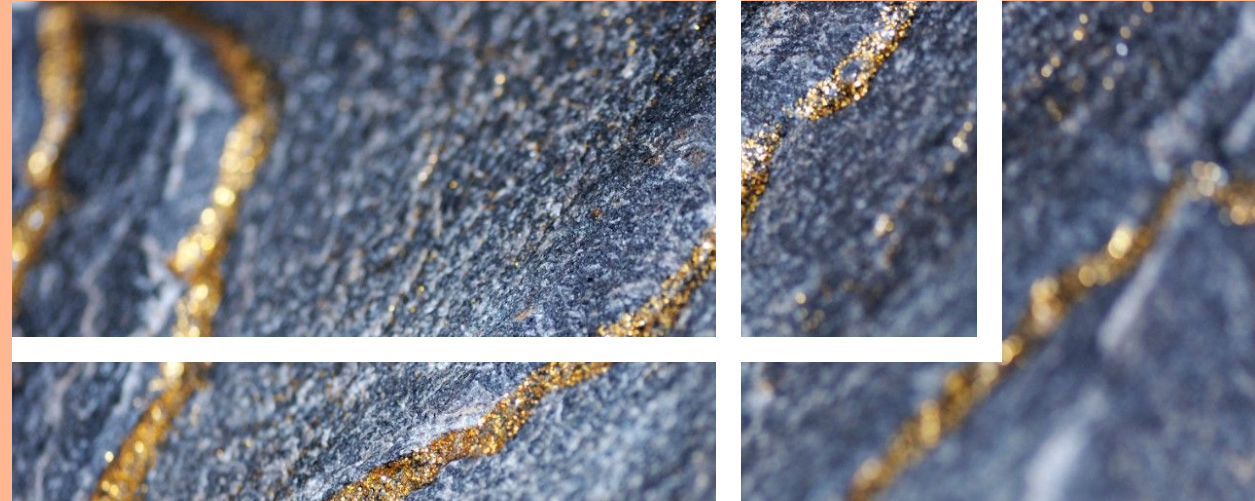
1. Fees to Bursa Malaysia Securities Berhad and Securities Commission Malaysia,
2. Professional fees:
  - Advisory fee to the sponsor/approved advisor, being the main advisor for listing on ACE Market or LEAP Market, and
  - Fees to a solicitor, company secretary, tax advisor, reporting accountant, auditor, valuer, independent market researcher, issuing house and share registrar, or
3. Fees for underwriting, placement and brokerage services.

The claim for tax deduction is only allowed in the YA in which the company is listed on the ACE Market or LEAP Market.

The deduction allowed is restricted to RM1.5 million and shall not exceed the adjusted income (prior to deduction of the above expenses). Any excess balance of expenditure which cannot be claimed cannot be carried forward to future YAs.

## Guidelines for imposition of penalties

The IRB has issued GPHDN 3/2020 - Guidelines for imposition of penalties under section 112(3) the Income Tax Act 1967 (ITA), section 51(3) of the Petroleum Income Tax Act 1967 (PITA) and section 29(3) of the Real Property Gains Tax Act 1976 (RPGTA) (“GPHDN 3/2020”). It replaces the earlier GPHDN 5/2019 of the same title.



The contents of GPHDN 3/2020 are the same as GPHDN 5/2019 except for the inclusion of paragraph 4.2 on the additional penalties under section 112(4) of the ITA, section 51(4) of the PITA and section 29(5) of the RPGTA.

These additional penalties may be imposed in the case of late submission of the tax return and where the chargeable income reported exceeds the amount in the best judgement assessment raised.

The rates of additional penalties remain the same and have been incorporated in the table setting out the relevant sections and penalty rates.

Act	Provision for best judgement assessment	Penalty for late or non-submission of tax return	Additional penalty provision*	Penalty rate
ITA	Section 90(3)	Section 112(3)	Section 112(4)	45%
PITA	Section 51(3)	Section 51(3)	Section 51(4)	45%
RPGTA	Section 29(3)	Section 29(3)	Section 29(5)	25%

\* Penalty on the difference between tax payable per tax return submitted and the best judgement assessment raised.

The guidelines are available on IRB’s website [www.hasil.gov.my](http://www.hasil.gov.my) (Legislation > Operational Guidelines)

## IRB's FAQs on International Tax Issues - Updated

The IRB has issued updated FAQs on International Tax Issues (“the FAQ”) dated 12 August 2020.



The changes in the FAQ are as follows:

Question	Key changes
<b>Residence</b>	
1. I am currently outside of Malaysia because of COVID-19 travel restrictions. How would my absence from Malaysia affect my residence status in Malaysia?	The IRB has added examples of documents / records and information to be kept as evidence that may prove the temporary absence from Malaysia is due to COVID-19 travel restrictions. The examples are travel document, local and foreign authority travel restrictions.
2. I am not a resident in Malaysia. Currently, I am in Malaysia because of COVID-19 travel restrictions. Would my temporary presence in Malaysia affect my residence in Malaysia?	

Where reference is made to the movement control order (MCO) period in the FAQ, IRB has specified that the period is from 18 March 2020 until 31 August 2020.

With the extension of the Recovery MCO period to 31 December 2020 as announced by the Prime Minister subsequent to the issuance of the amended FAQ above, it is hoped that the IRB will provide further clarification if the above reference to MCO period in the FAQ will similarly be extended to 31 December 2020.

The FAQ is available on IRB’s website [www.hasil.org.my](http://www.hasil.org.my) (Quick Links > FAQs Movement Control Order & Economic Stimulus Package).

## Stamp duty exemption for research and development for exploration/exploitation of petroleum/natural resources

The Stamp Duty (Exemption) (No 5) Order 2020 (“the Order”) was gazetted on 26 August 2020 and is effective from 28 August 2020.



The Order provides for stamp duty exemption on the agreement executed between Malaysia - Thailand Joint Authority (MTJA) and institutions of higher education in Malaysia and Thailand relating to the use of research cess to finance research and development in the fields of science and technology for the exploration / exploitation of petroleum / natural resources in the Joint Development Area (JDA).

“Research cess” is as provided in the regulation 7 of the Malaysia - Thailand Joint Authority (Payments of Royalty and Other Proceeds from Petroleum Production to the Governments) Regulations 2004 which states that:

- The research cess is received by the MTJA from the contractor under the terms of the production sharing contract and paid into the research fund.
- The research cess is to be expended for the purpose of supporting any research and development in the field of science and technology relating to exploration or exploitation of petroleum or natural resources for the JDA.
- Any project or programme for the use of research cess is to be determined by the MTJA, or may be recommended or proposed by the Director General of the Economic Planning Unit of the Prime Minister’s Department of Malaysia, or by the Director General of the Department of Mineral Fuels of the Ministry of Energy of Thailand to the Joint Authorities for its approval.

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