



INLAND REVENUE BOARD OF MALAYSIA

**OWNERSHIP AND USE OF ASSET FOR
THE PURPOSE OF CLAIMING CAPITAL
ALLOWANCES**

PUBLIC RULING NO. 5/2014

DATE OF PUBLICATION: 27 JUNE 2014



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DIRECTOR GENERAL'S PUBLIC RULING

Section 138A of the Income Tax Act 1967 [ITA] provides that Director General is empowered to make a public ruling in relation to the application of any provisions of ITA.

A Public Ruling is published as a guide for the public and officers of the Inland Revenue Board of Malaysia. It sets out the interpretation of the Director General of Inland Revenue in respect of the particular tax law and the policy as well as the procedure applicable to it.

The Director General may withdraw either wholly or in part, by notice of withdrawal or by publication of a new ruling.

**Director General of Inland Revenue,
Inland Revenue Board of Malaysia.**

1. Objective

The objective of this Public Ruling (PR) is to explain the ownership and use of asset and the effect on whether a person qualifies to claim capital allowances (CA) in respect of that asset in determining the statutory income from a business of the person.

2. Summary Of Changes

This PR is published to replace the Public Ruling No.1/2001 issued on 18.1.2001 with the following amendments:

Paragraph In Public Ruling No. 1/2001	Changes In This Ruling		
	Paragraph	Item	Reference
1	1	Objective	Paragraphs have been replaced and rearranged
2	3	Relevant Provisions of the Law	
3	5	Application of relevant law	
	6	Ownership of the asset	
	7	Jointly owned asset	
	8	Partnership asset	
4	4	Interpretation	New paragraphs inserted
None	2	Summary of changes	
	9	Limited Liability Partnership asset	
	10	Hire purchase asset	
	11	Leased asset	
	12	Business Trust asset	
	13	Use of asset	
	14	Asset classified as Held For Sale	
15	Procedure for claiming capital allowances		

3. Relevant Provisions Of the Law

- 3.1 This PR takes into account laws which are in force as at the date this PR is published.
- 3.2 The Provisions of the Income Tax Act 1967 (ITA) related to this PR are subsections 2(1), 2(8), section 42 and schedule 3.
- 3.3 Relevant subsidiary laws referred to in this PR is P.U.(A) 131/1986.

4. Interpretation

The words used in this PR have the following meanings:

- 4.1 “Asset” means plant and machinery used for business purposes and qualifying expenditure has been incurred.
- 4.2 “Special Purpose Asset” means a leased asset where no other user can use the same asset without making alterations or dismantling from a structure or land and shall be deemed to be a movable property.
- 4.3 “Business Trust” means a unit trust scheme where the operation or management of the scheme and the scheme’s property or asset is managed by a trustee-manager.
- 4.4 “Balancing Allowance” refers to the difference where the disposal value of an asset is less than the residual expenditure.
- 4.5 “Balancing Charge” ” refers to the difference where the disposal value of an asset is more than the residual expenditure.
- 4.6 “Plant” for the purpose of qualifying expenditure means any movable or immovable assets including whatever apparatus is used in a business but does not include stock-in-trade and premise where the business is conducted.
- 4.7 “Disposed” means an asset is sold, discarded or destroyed or it ceased to be used for the purposes of the business.
- 4.8 “Market Value” means the price for the goods sold in a transaction between independent persons dealing at arm’s length.
- 4.9 “Person” includes a company, a body of persons, a limited liability partnership and a corporation sole.
- 4.10 “Lease” includes a sublease, a tenancy for three years or less and any agreement for a lease or sublease.

- 4.11 “Partnership” means an association of any kind (including joint adventures, syndicates and cases where a party to the association is itself a partnership) between parties who have agreed to combine any of their rights, powers, property, labour or skill for the purpose of carrying on a business and sharing the profits therefrom, but excludes a Hindu Joint Family although such a family may be a partner in a partnership or a limited liability partnership.
- 4.12 “Qualifying Expenditure” means capital expenditure incurred on the provision, construction or purchase of plant or machinery used for the purpose of a business other than assets that have an expected life span of not more than 2 years.
- 4.13 “Limited Liability Partnership” means a limited liability partnership registered under the Limited Liability Partnerships Act 2012.
- 4.14 “Company” means a body corporate and includes any body of persons established with a separate legal identity by or under the laws of territory outside Malaysia and a business trust.
- 4.15 “Year of Assessment” means calendar year.
- 4.16 “Basis year for a year of assessment” means the calendar year coinciding with the year of assessment.
- 4.17 “Lease Term” means the period for which the lessee has contracted to lease an asset or where a lease arrangement has been terminated earlier than its expiry the actual period of the lease.

5. Application Of Relevant Law

In determining the adjusted income of a business, no deduction is allowed for expenses incurred on an asset and depreciation charged in the accounts. However, if the expenditure is qualifying expenditure (QE) [expenditure on plant and machinery] a tax deduction is given in the form of capital allowance (CA) in determining the statutory income from a business source as provided under section 42 of the ITA.

CA is only given to the person who incurred the QE on an asset used in his business as provided under Schedule 3 of the ITA and would only be allowed a deduction if claimed.

CA is given in the form of initial allowance (IA) and annual allowance (AA).

5.1 Eligibility for Initial Allowance

A person has to satisfy the following conditions in order to qualify for IA in respect of an asset for a year of assessment:

- (a) was carrying on a business during the basis period,
- (b) had incurred QE during the basis period, and
- (c) at the end of the basis period (or, if the asset was disposed of, at the time of disposal), he was the owner of the asset.

5.2 Eligibility for Annual Allowance

A person has to satisfy the following conditions in order to qualify for AA in respect of an asset for a year of assessment:

- (a) was carrying on a business during the basis period,
- (b) had incurred QE during the basis period,
- (c) that asset was used for the purpose of the business, and
- (d) at the end of the basis period, he was the owner of the asset and the asset was in use.

6. Ownership Of The Asset

Ownership of an asset in this PR refers to either legal or beneficial ownership. The person who owns an asset can be the legal or beneficial owner or both.

6.1 Legal ownership

Legal owner is the person whose name is registered or documented as proof of ownership.

Example 1

For landed asset – the person whose name is on the land grant.

For motor vehicle – the person whose name is on the vehicle card.

For machinery – the person whose name is on the warranty certificate or insurance policy.

6.2 Beneficial ownership

Beneficial owner is the person who has actually incurred the QE and payment for the asset that can be proved in the books of accounts with supporting documents such as invoices, vouchers and receipts.

For the purposes of schedule 3 of the ITA, if a beneficial owner has incurred the QE and used the asset for his business, he is entitled to claim CA

although the asset is registered in the name of another person (the legal owner).

Example 2

Akmal purchased a lorry in 2013 and registered it in the name of his brother, Ahmad. Akmal paid the installments and used the lorry for his business until the end of the basis period for the year of assessment 2013.

Akmal is the beneficial owner as he has incurred the QE and the lorry was used for the purpose of his business. Therefore Akmal is entitled to claim IA and AA on the lorry for the year of assessment 2013. Ahmad is not entitled to claim CA as he has not incurred the QE.

6.3 Legal owner who incurs qualifying expenditure

A legal owner who incurs the QE is also the beneficial owner. If the asset owned is used in his business, the owner is entitled to claim CA.

Example 3

Maniam purchased a van on HP and registered it in his name. He uses the van in his grocery business.

Maniam is entitled to claim CA as he has fulfilled the conditions stated in paragraphs 5.1 and 5.2 of this PR.

Example 4

Airina Food Sdn Bhd (AF) is a supplier and distributor of ice cream, dairy products and other frozen foods. AF purchased a few units of freezers and put them in retail outlets and supermarkets without charging any rent on the condition that the retailers and supermarket owners sell only frozen goods supplied by AF.

Although the assets are placed in the customers' premises, the assets are being used for the purpose of AF's business. Thus, AF is entitled to claim CA on the assets as AF is the legal and beneficial owner and has satisfied all the conditions stated in paragraphs 5.1 and 5.2 of this PR.

Example 5

Syarikat Insurans Ally (Ally) provided assets such as computers and furniture to its insurance agents for use in premises rented by Ally.

Although the assets are placed in the premises and used by Ally's insurance agents, the assets are being used for the purpose of Ally's business. Therefore Ally is the legal and beneficial owner of the assets and is entitled to

claim CA as Ally has satisfied all the conditions stated in paragraphs 5.1 and 5.2 of this PR.

6.4 **Legal owner who does not incur qualifying expenditure**

A legal owner who does not incur the QE even though he uses the asset for the purpose of his business, is not entitled to claim CA as he has not fulfilled all the conditions stated in paragraphs 5.1 and 5.2 of this PR.

Example 6

Ungu Sdn Bhd, a construction company, is the legal owner of a lorry which is purchased by its holding company. The lorry is used by Ungu to transport construction materials. The holding company pays the monthly installments and is responsible for the maintenance of the lorry.

Though Ungu is the legal owner of the lorry, it is not entitled to claim CA on the lorry as it did not incur the QE even though the lorry is used in its business.

6.5 **Beneficial owner incurs the qualifying expenditure but asset is not used in his business**

The QE is incurred by the beneficial owner but the asset is not used for the purposes of his business, instead the asset is being used by the legal owner or some other person. The beneficial owner is not eligible to claim CA as he has not fulfilled the conditions stated in paragraphs 5.1 and 5.2 of this PR.

Example 7

Same facts as in Example 6.

The holding company is the beneficial owner as it has incurred the QE. However, the holding company is not entitled to claim CA on the lorry as the lorry is not used in its business, but being used by the legal owner.

Example 8

MM Sdn Bhd (MMSB) carries on a business on the import of crystals. MMSB would order from its supplier based on orders received from MM Marketing Sdn Bhd. MM Marketing and the supplier are associated companies of MMSB.

MMSB incurred QE on racking system, furniture and fittings which were purchased under the supplier's name. Those assets are placed in the showrooms owned by MM Marketing and used by MM Marketing to showcase and for selling its products (crystals) to the public.

MMSB is the beneficial owner as it has incurred the QE on the assets. However MMSB is not entitled to claim CA as the assets are not used for the purpose of its business as an importer of crystals.

The supplier who is the legal owner did not incur the QE and thus is not entitled to claim CA.

MM Marketing is also not entitled to claim CA as it has not incurred the QE even though the assets are being used for the purpose of MM Marketing's business.

MMSB (beneficial owner), the supplier (legal owner) and MM Marketing (other person) are not entitled to claim CA on the assets as they have not fulfilled all the conditions stated in paragraphs 5.1 and 5.2 of this PR.

7. Jointly Owned Asset

Where –

- a) more than one person has incurred the QE on an asset,
- b) the asset is used for the purpose of a business of each of them during the basis period,
- c) the asset is still in use at the end of the basis period, and
- d) the asset is registered in the name of only one of the beneficial owners or in the name of some other person.

Each of the beneficial owners is entitled to claim CA in respect of the asset in the appropriate portion based on his share of QE incurred. In a situation where more than one person is claiming CA for the same asset, a statement which shows details of apportionment must be made in their respective tax computations [to be verified by officers of the Inland Revenue Board of Malaysia (IRBM) during tax audit].

Example 9

An audit inspection by IRBM officers discovered that Abu and Ahmad jointly purchased a van for RM80,000 on 1.9.2012. Abu paid RM48,000 (60%) and Ahmad paid RM32,000 (40%). The van is registered in the name of Abu as he has incurred a larger portion of the capital expenditure. The van is used in their respective restaurant business. Abu and Ahmad prepare their business accounts for year ending 31 December each year.

Computation of Capital Allowances

		Abu (60%)	Ahmad (40%)
Year of Assessment 2012			
QE (RM)	80,000	48,000	32,000
IA (20%)		9,600	6,400
AA (20%)		9,600 19,200	6,400 12,800
Residual Expenditure		28,800	19,200
Year of Assessment 2013			
AA (20%)		9,600	6,400
Residual Expenditure		19,200	12,800

Residual Expenditure (RE) means the cost of assets less –

- (a) initial allowance and annual allowance, or
- (b) notional allowance which is an amount equivalent to annual allowance.

8. Partnership Asset

8.1 Asset of a partnership is jointly owned by all the partners. If the asset is used in the partnership business and qualifying expenditure is incurred by all partners at the end of a basis period, all the partners are beneficial owners and are entitled to claim capital allowance.

CA is computed based on QE incurred amongst the partners based on two different situations as follows:

- (a) CA is computed based on QE incurred and then allocated amongst the partners based on their profit sharing ratios in the partnership if the asset is used in the partnership business and QE is incurred by all partners at the end of a basis period, or
- (b) CA is allocated amongst those who are partners at the end of the basis period in accordance with their profit sharing ratios if there are changes of partners in a partnership such as termination or entry of a

partner and the partnership business continues as an on-going business.

8.1.1 Continuing partnership and there is no change of partners

The CA is allocated to each partner in accordance with his profit sharing ratio in the partnership at the end of the basis period for a year of assessment. Profit sharing ratio is usually computed based on the amount of capital contribution from each partner.

8.1.2 Continuing partnership and there is a change of partners

- (a) An individual who had conducted a sole proprietorship business takes a partner into that business so that a partnership business commences.

Example 10

Alex operated a sole proprietorship business and closed the accounts on 31 December each year. On 01.10.2012, Alex invited Asyraf to join as a business partner and the business became a partnership. For the financial period 1.10.2012 to 31.12.2012, the statutory income from the partnership business is nil. Asyraf has agreed to share the profit of the partnership equally with effect from 01.01.2013.

For the purposes of CA, Alex's sole proprietorship business and the partnership business are deemed to be one continuing business. The basis period for the year of assessment 2012 is 01.01.2012 to 31.12.2012. The basis period for the year of assessment 2013 is 01.01.2013 to 31.12.2013.

For the year of assessment 2012, CA was given wholly to Alex as Asyraf did not have any statutory income from the partnership business.

For the year of assessment 2013, CA would be allocated to Alex and Asyraf based on their profit sharing ratios on 31.12.2013.

- (b) There are changes in the partners of a partnership business but at least one partner continues throughout in the partnership business.

Example 11

Ah Chong and Peter are partners of a construction business and sharing the partnership profit equally. The partnership

business closes its accounts on 31 December each year. In 2012, the partnership purchased a tractor costing RM100,000 and used it in road construction projects. On 31.08.2013, Peter retired from the partnership and a new partner Akmal entered the partnership on 01.09.2013. Ah Chong and Akmal share profits of the partnership in the ratios of 1/3 and 2/3 respectively.

There has been a change in the partners but Ah Chong remains as the continuing partner so that the partnership business is deemed to be a continuing business.

For the year of assessment 2012, Ah Chong and Peter were the beneficial owners and were entitled to claim CA. The CA would be allocated equally between Ah Chong and Peter.

For the year of assessment 2013, Peter would not be entitled to claim CA as he had ceased to be a partner in the partnership. The CA would be allocated to Ah Chong and Akmal in accordance with their profit sharing ratios of 1/3 and 2/3 respectively.

- (c) A partnership business effectively ceases but one of the former partners continues the business as a sole proprietor.

Example 12

Amira and Amylia were two partners in a pharmaceutical business that commenced on 01.01.2012. Business accounts closed on 31 December and profits were shared equally. On 21.11.2013, Amylia ceased from the partnership and the business was taken over by Amira as a sole proprietor. Closing of business accounts remains as at 31 December.

For the purposes of CA, though the partnership effectively ceased but a former partner, Amira, continued the business as a sole owner. Therefore both the partnership and the sole proprietorship business shall be deemed to be one business.

For the year of assessment 2012, CA would be allocated equally to Amira and Amylia in accordance with their profit sharing ratios as at 31.12.2012.

For the year of assessment 2013 and subsequent years, Amira would be entitled to claim the whole amount of CA as Amylia had ceased to be a partner on 21.11.2013.

- 8.3 **If an asset is used in a partnership but only one partner has incurred qualifying expenditure in respect of the asset, capital allowance is allowed to the partner who incurred the qualifying expenditure**

Example 13

Aidil, Ang and Kalish are partners of an engineering firm. Kalish has incurred QE on the purchase of a car which is used wholly and exclusively for the purposes of the partnership business.

For the purposes of schedule 3, CA in respect of the car is to be given entirely to Kalish. The other two partners are not entitled to claim the CA because they did not incur the QE although the car is used for the purposes of the partnership business.

9. **Limited Liability Partnership Asset**

Limited liability partnership (LLP) has hybrid features of a company and a partnership that provides limited liability to its partners. An LLP is a separate legal entity from its partners. For tax purposes, an LLP is an entity and is defined in section 2 of the ITA.

9.1 **Capital Allowance Claims**

An LLP is entitled to claim CA as provided under schedule 3 of the ITA and would be allowed deduction if a claim is made.

9.2 **Change of Partners in a Limited Liability Partnership**

If there is a change of partners in an LLP, in which an existing partner withdraws from the LLP due to retirement, death or other reasons or a new partner is taken into the LLP, the change does not affect the business of the LLP.

An LLP may carry on a business with less than two partners for a period not exceeding six months or such longer period as specified by the Registrar.

“Partner” in relation to an LLP, means any person who has been admitted as a partner in the LLP in accordance with the LLP agreement, and includes a salaried partner whether or not he is an employee of the LLP.

“Registrar” means the Registrar of Limited Liability Partnership as designated under the Limited Liability Partnership Act (LLPA) 2012 and includes any Assistant Registrar appointed under LLPA 2012.

For the purposes of CA, an LLP is entitled to claim CA on the assets used in the business despite changes in the partners as the assets are still owned by the LLP (a legal entity).

Example 14

Dol, Ray and Mint are three partners in an accounting firm Ayu Seri PLT (accounts ending on 31 December). It commenced business since 21.02.2012. On 02.04.2013, Mint died due to an accident and the business continues to operate with the remaining two partners.

Ayu Seri PLT is entitled to claim CA for the year of assessment 2013 despite the change in the number of partners as the assets are still owned by the LLP.

Example 15

The facts are the same as in Example 14 except that Ray withdrew from the LLP on 01.05.2013. The business then consists of one partner only. The Registrar has allowed the business of Ayu Seri PLT to continue for a period of eight months. The LLP would be dissolved after the grace period.

Despite having only one partner, the LLP may continue the business for a period of eight months commencing from 01.05.2013 to 31.12.2013 as determined by the Registrar. The LLP is entitled to claim CA for the year of assessment 2013. However, from the year of assessment 2014, the LLP is not eligible to claim any CA as the assets are no longer used in the business (in the process of winding up).

If the assets are disposed of before the LLP is dissolved, adjustments must be made to the RE. The LLP would claim the difference between the disposal values of the assets and the RE which would result in balancing allowances or balancing charges.

Example 16

The facts are the same as in example 15 except that the period allowed by the Registrar is for a period of six (6) months.

The LLP may continue its business for a period of six months from 01.05.2013 to 31.10.2013. Since the assets are still being used in the business for the period from 1.1.2013 to 31.10.2013 the LLP is entitled to claim CA for that period. The LLP would be dissolved after the period.

10. Hire Purchase Asset

Hire purchase (HP) is a system of acquiring asset on credit whereby the seller of the asset is regarded as the dealer, the purchaser is regarded as the hirer and the

financier as the owner. The ownership of the asset bought on HP does not pass to the hirer at the time of the HP agreement or upon delivery of the asset. The ownership of the asset remains with the financier until the hirer has fully settled the price agreed upon in the HP agreement.

10.1 Conventional Hire Purchase

Under the conventional financing, a person (hirer) purchases the asset on behalf of the owner. The HP agreement would commence once the owner has paid the supplier of the asset and the hirer has taken possession of the asset.

For the purposes of CA, the hirer is deemed to be the owner of the asset. The hirer is the beneficial owner as he has incurred the QE and is entitled to claim CA if the asset is used for business purposes. He would be the legal owner as well when the last installment has been made.

Amount of QE incurred by the hirer would be based on the terms and conditions of the HP agreement. The installment payments are made up of capital portion (deposit and capital repayments) and revenue portion (HP interest).

10.1.1 Computation of capital allowance

HP interest is deductible against gross income in determining the adjusted business income of the hirer. Deposit and capital repayments are QE eligible for CA given in the form of IA and AA as follows:

- (a) computation of IA is based on QE incurred each year throughout the HP period, and
- (b) computation of AA is based on cumulative QE incurred throughout the HP period.

Example 17

Villa Sdn Bhd purchased a van costing RM105,000 for use in its business. The HP agreement with a financial institution took effect from January 2012. The annual HP interest is RM1,200. In 2012, the company paid deposit RM20,000 and capital installments payments of RM9,000. In 2013, the company paid RM9,000 on installments based on the HP schedule.

Computation of Capital Allowances

Year of Assessment 2012		
QE (Deposit RM20,000 + installments RM9,000)		29,000
IA (20% x 29,000)	5,800	
AA (20% x 29,000)	5,800	11,600
Residual Expenditure		17,400
Year of Assessment 2013		
QE (Installments RM9,000)		9,000
		26,400
IA (20% x 9,000)	1,800	
AA (20% x 38,000)	7,600	9,400
Residual Expenditure		17,000

10.1.2 Qualifying Expenditure

QE for a HP asset refers to the capital expenditure actually incurred by the hirer. Therefore CA is computed based on capital installment payments that have been made for the year of assessment and not based on the amount listed in the schedule of the HP agreement.

As such, if a person makes early settlement of the HP loan, QE is the total capital repayments that have been made. On the other hand, if the payment of installments in the schedule of a HP agreement is not made, the amount would not be taken as the QE.

Example 18

Salak Sdn Bhd (Salak) purchased a used lorry for RM85,000 under HP with a finance company in January 2011. Salak paid a deposit of RM5,000, capital installments of RM7,500 and HP interest of RM 800 in the year 2011. Capital installment payments is RM7,500 each year over the period of HP.

As the engine was faulty within the warranty period, the lorry was recalled by the manufacturer for replacement of parts. To compensate for the inconvenience for loss of use of the lorry, Salak was allowed to defer several installments due in 2012 to the year 2013. Total capital repayments made in 2012 was RM4,375 and the balance was paid in 2013.

Computation of Capital Allowances

Year of Assessment 2011		
QE (Deposit RM5,000 + installments RM7,500)		12,500
IA (20% x 12,500)	2,500	
AA (20% x 12,500)	2,500	5,000
Residual Expenditure		7,500
Year of Assessment 2012		
QE (Installments RM4,375)		4,375
		11,875
IA (20% x 4,375)	875	
AA (20% x 16,875)	3,375	4,250
Residual Expenditure		7,625
Year of Assessment 2013		
QE (Installments RM7,500 + RM3,125)		10,625
		18,250
IA (20% x 10,625)	2,125	
AA (20% x 27,500)	5,500	7,625
Residual Expenditure		10,625

10.2 Asset under Islamic financing

In the context of Islamic finance, a lease contract is referred to as *Ijarah* that involves an exchange of *usufruct* or benefits of an asset for rent for an agreed period.

The *ijarah* concept is usually applicable in financing contracts such as in real property financing, vehicle financing, project financing and personal financing.

Most of the vehicle financing in Islamic financial institutions in Malaysia are implemented through the concept of *Al-ijarah thumma al-bai'* (AITAB) which means leasing (Al-ijarah) ending with sale (Al-bai') , that is AITAB is a contract of lease with an option to purchase the asset. The financing based on AITAB involves two types of contracts, namely:

(i) Leasing agreement (Al-ijarah 'ain)

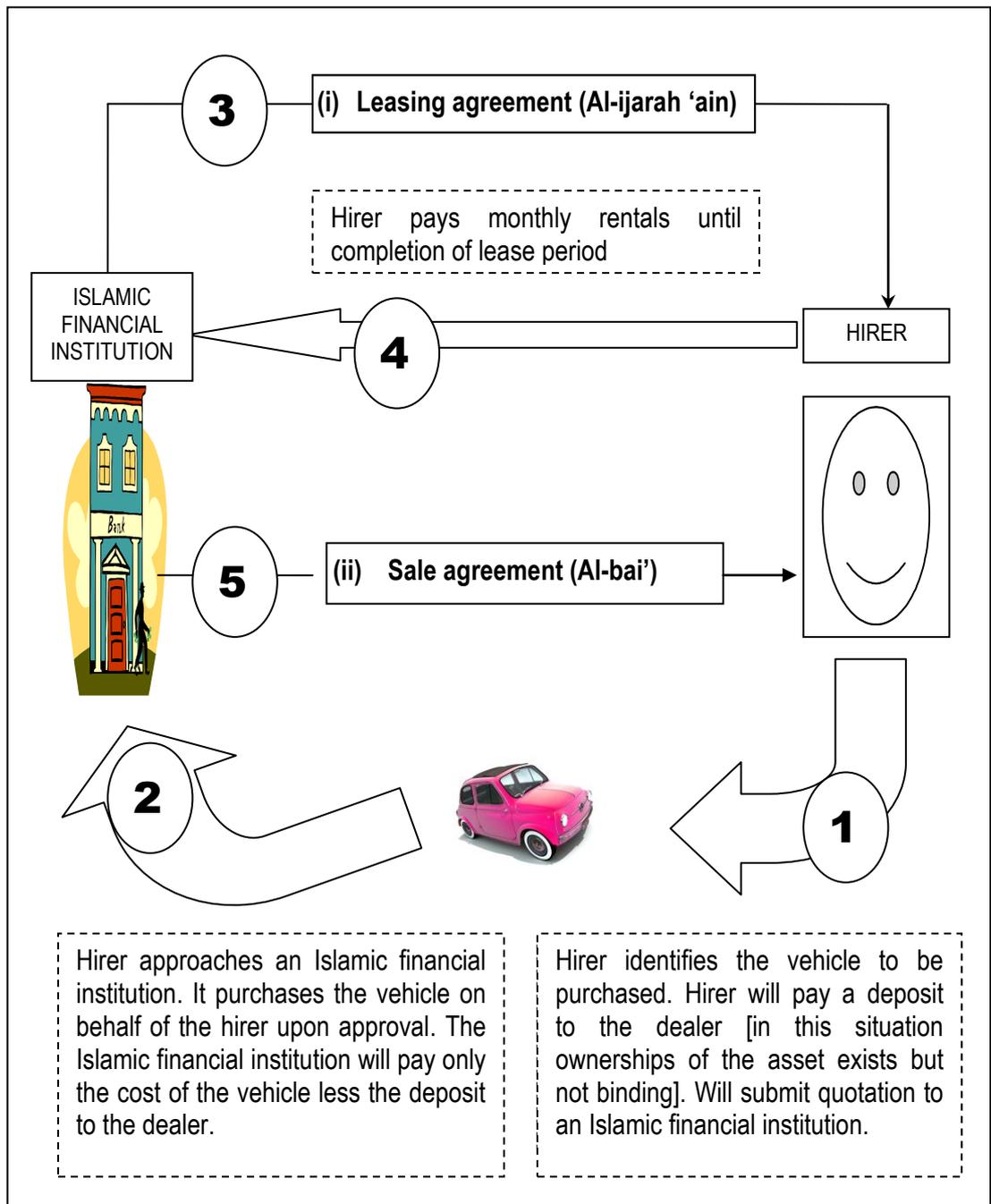
The owner which is an Islamic financial institution will conclude an *ijarah* agreement with the hirer. Under this agreement, the owner will appoint the hirer as an agent to purchase the vehicle identified by the hirer. Subsequently, the owner will lease the vehicle to the hirer for a specified period.

The costs and benefits will be calculated and the hirer pays a monthly installments for a specified period.

(ii) Sale agreement (Al-bai')

Upon expiry of the lease period, the hirer has the option to purchase the vehicle from the owner. If the hirer opts to purchase the vehicle, the owner and the hirer will conclude a sale contract and the ownership of the vehicle will be transferred from the owner to the hirer.

An illustration of AITAB agreement is as follows:



For the purposes of CA, the hirer is the beneficial owner as he has incurred the QE and if the asset is used for the purpose of his business from the date of the rental agreement (Ijarah), the hirer is entitled to claim CA in respect of the asset. The hirer would be the legal owner when the Islamic financial institution surrenders possession of the asset to the hirer or the hirer may agree to accept the offer to buy the asset subject to the terms of the sale agreement.

There is no element of interest in Islamic financing. Instead, profit would be imputed to the rental by the Islamic financial institution. Thus, the expense (in lieu of interest) incurred by the hirer is given the same tax treatment as the tax treatment of interest on conventional HP. The expense is deductible against gross income in determining the adjusted income of the hirer. Deposit and capital repayments are QE eligible for CA. Thus, CA is calculated based on the monthly rental amount (excluding the profit portion) that has been made according to the terms and conditions of the leasing agreement.

Example 19

In January 2013, Alamcyber Sdn Bhd (Alamcyber) with financial year ending on 31 December purchased a machine costing RM400,000. It paid a deposit of RM40,000 to the dealer, the balance RM360,000 was to be funded by an Islamic financial institution. The machine is being used in its business since January 2013.

In February 2013, the company made two separate agreements with the Islamic financial institution:

(i) Leasing agreement (Al-ijarah 'ain)

The Islamic financial institution bought the machine and leased the asset to Alamcyber for 6 years at RM6,000 a month (total lease rental RM432,000).

(ii) Sale agreement (Al-bai')

Alamcyber would be given the option to purchase the asset upon expiry of the agreement.

The Sale Agreement (Al-bai') would come into effect upon expiration of the Leasing Agreement (Al-ijarah)

Alamcyber is the beneficial owner and is entitled to claim CA as the asset is used in its business. The CA is given based on the amount of deposit and capital portion of rental payments incurred for each year of assessment throughout the lease period which commenced from the year of assessment 2013.

Computation of Capital Allowances For The Year of Assessment 2013

	RM	RM
Total lease rental		432,000
Amount to be funded by the Islamic financial institution		360,000
Amount of expense (profit to the bank) deemed to accrue evenly every month for 72 months (6 years)		72,000
Amount of expense per month	72,000/72	1,000
Year of Assessment 2013		
Deposit	40,000	
Capital repayment (RM5,000 x 11 months)	55,000	
QE		95,000
IA (20% x 95,000)	19,000	
AA (14% x 95,000)	13,300	32,300
Residual Expenditure		62,700

- 10.3 **The financing in accordance with the principles of Syariah involves the lease or disposal of an asset. However, these transactions are deemed not taking place as provided under subsection 2(8) of the ITA.**

Example 20

Arisha intended to obtain Islamic financing from a bank in compliance with Syariah principle. Arisha sold an asset to the bank and then the bank leased back the asset to Arisha.

Under the provision of subsection 2(8) of the ITA, the disposal by Arisha and leasing of the asset to Arisha are to be disregarded, that is the disposal and leasing of the asset are deemed not taking place. Arisha is still the beneficial and the legal owner. Therefore she is entitled to claim CA if the asset is used in her business.

10.4 Refinancing

If CA has been claimed on an asset and then it is refinanced through a HP arrangement, the hirer is allowed to continue his claim on the CA based on RE of the asset. This is because refinancing is treated as borrowing with the asset as a security, provided the hirer still uses the asset in the business.

Example 21

Lagenda Sdn Bhd purchased a car in cash for RM58,000 in the year of assessment 2008. CA in respect of the car has been fully claimed and RE is nil at the end of the basis period for year of assessment 2012. In the year of assessment 2013, the company refinanced the car for RM50,000 through a HP arrangement with a bank, commencing on March 2013.

In this case, CA has been fully claimed. Though the vehicle is refinanced through a HP arrangement, the company would not be eligible to claim CA on RM50,000 in respect of the vehicle.

Example 22

In 2011, Cleo Sdn Bhd (accounts ending on 31 December) bought a machine for use in the production of small components for watches. The company took a full loan of RM350,000 through a HP agreement with Gangsa Bank Bhd. In 2013, the company refinanced the machine for RM380,000 through another HP agreement with Jade Bank Bhd because the bank offered a lower interest rate. RE in respect of the machine for the year ended 31 December 2012 was RM140,000.

The company can continue to claim CA even though the machine was funded by another bank in the year of assessment 2013. However the total amount of CA claimed in respect of the machine is restricted to RM350,000 (cost of the machine only).

11 Leased Asset

11.1 A lease is a contract where a party being the owner (lessor) of an asset (leased asset) provides the asset for use by the lessee at a consideration (rental), either fixed or variable, for a certain period (leased period) either fixed or flexible, with an understanding that at the end of such period, the asset, subject to the embedded options of the lease will either be returned to the lessor or disposed of as per the lessor's instructions.

11.2 For a lease transaction whether a finance lease or an operating lease, both types of leases would be accorded the same tax treatment.

- 11.3 A lease transaction involves the acquisition of an asset by the lessor to be leased to the lessee via a leasing agreement. The lessee uses the leased asset by paying rent only based on amount of payments stated in the lease agreement. The lessor has acquired the asset to be used in his leasing business. As such, the lessor as the legal and beneficial owner is entitled to claim CA as he has incurred the QE and used the asset in his business.
- 11.4 The manner in which a leased asset is shown in the accounts in compliance with accounting standards does not change the tax treatment accorded to a leased asset.
- 11.5 However, if a lease transaction is deemed to be a sale transaction as stated under Regulation 4 of the Income Tax Leasing Regulations 1986 (LR) [P.U. (A) 131], it will constitute an outright sale. The lessee can claim CA on the leased asset. CA would be given based on the cost price of the asset and not based on the amount of installment payments made unless the lease agreement has salient characteristics of a HP transaction.
- 11.6 Regulation 4 of the LR is an anti-avoidance regulation. The IRBM would apply the Regulation if it is obvious that the lease agreement contains terms and conditions that are meant for tax avoidance. Under this Regulation, only the lessee is entitled to claim CA in respect of the asset. Necessary adjustments would be made to avoid both the lessor and the lessee claiming CA in respect of the same asset. If an adjustment is made by the IRBM after an audit, CA claimed by the lessor would be withdrawn.

Example 23

Alexandria Sdn Bhd (Alexandria) leased a fotocopy machine from Iskandar Leasing Bhd for a period of four (4) years. The lease provided option for Alexandria to purchase the machine at the end of the lease period but amount of down payment (which is equivalent to security deposit in a lease) and lease interest payment were not stated in the agreement.

As Alexandria (lessee) is given the option to purchase the asset, the lease agreement is deemed to be an outright sale agreement as provided under Regulation 4 of the LR1986. The lease transaction is not considered as a HP transaction as there were no elements of down payment (or security deposit) and interest payment that are characteristics of a HP transaction.

Example 24

Hospital Sinar Sdn Bhd leased a computerized x-ray machine with lease rental of RM80,000 per month. The lease term was for three (3) years from January 2011 to December 2013. Accounts closed on 31 December of each year.

When the lease term expired, Hospital Sinar Sdn Bhd purchased the machine for RM300,000 and claimed the price as the market value. The machine was purchased by the lessor for RM2.5 million and the RE of the machine on 31.12.2013 was RM500,000.

As Hospital Sinar Sdn Bhd purchased the asset at a price less than the RE of the asset, the sale was considered to be selling below the market value. The lease agreement was deemed a sale agreement on the date of execution of the original lease pursuant to Regulation 4 of the LR 1986.

Hospital Sinar Sdn Bhd was the legal and beneficial owner and would be entitled to claim CA on the machine. The amount of lease rental payment that have been given deduction in prior years would be withdrawn. Meanwhile, CA claimed by the lessor would also be withdrawn.

12 Business Trust Asset

A business trust (BT) is a unit trust scheme that has hybrid features of a company and a unit trust. The management of a BT is carried out by a trustee-manager (TM) who hold assets on trust for the unit holders of the BT. TM is the legal owner of the assets whereas the BT is the beneficial owner of the assets.

TM means the person who –

- (i) holds property or asset on trust for unit holders of the business trust, and
- (ii) manage and operates such property and asset.

For the purposes of tax treatment, BT is defined as a company in the ITA. Thus, in determining the statutory income under section 42 of ITA, the BT is entitled to claim CA as provided under Schedule 3 of the ITA.

Example 25

A BT has been registered in Malaysia and has appointed a TM to manage and operate the BT's hotel business in Malaysia. All meetings relating to the management and control of the BT are conducted in Malaysia. The BT pays management fee and trust fees to the TM for services rendered.

BT assets are registered in the name of the TM. The assets are purchased by the BT and use in the hotel business.

BT is the beneficial owner as it has incurred the QE. Therefore the BT is entitled to claim CA on the assets. TM is not entitled to claim CA although the TM is the legal owner as the TM just hold the assets on trust and manages the business of the BT.

13 Use Of Asset

A beneficial owner or legal owner is entitled to claim the full portion of CA if he has incurred expenditure on the asset and use it wholly and exclusively for business purposes.

If an asset is also used for purposes other than business purpose, the owner is only entitled to a portion of the CA. The portion is computed based on qualifying expenditure incurred and the proportion used for the business.

13.1 Asset wholly used in the business

The owner is entitled to claim full amount of the CA if he incurred the QE and used the asset wholly and exclusively in the following circumstances:

- (a) For the purpose of carrying on his business,
- (b) For asset that is temporarily disused in the business for a period, provided:
 - (i) the asset was in use for the purposes of the business immediately before becoming disused, and
 - (ii) during the period when asset is disused, the asset is constantly maintained in readiness to be brought back into use.

However, if the asset ceases to be ready for use or its disuse is no longer considered as temporary, the asset is deemed to have been disposed of at the beginning of the period of disuse. CA would be withdrawn and computation of balancing charge or balancing allowance would be made.

Example 26

Scenario 1

Hias Sdn Bhd (Hias) sent his factory machine for repair and maintenance. The machine was repaired in the following year because of inadequate supply of spare parts. Thus the machine was not used for a period of two years.

Scenario 2

Jaya Sdn Bhd (Jaya) is unable to use its milling machine because of disruption to its operations due to:

- (i) a strike by factory worker; or
- (ii) inspection on factory site by the local authority.

In both the scenarios, the machines are deemed to be temporarily disuse. Therefore, Hias and Jaya are still entitled to claim CA for the years of assessment which contain the period of temporary disuse.

13.2 Asset used partly for business

A person who incurs the QE and uses the asset in both business and non – business activities is entitled to claim a portion of the CA. CA is computed based on the full amount of QE incurred and a reasonable apportionment of its usage for business and non-business purposes must be determined. Apportionment is usually done on time basis and CA is restricted to business use.

Example 27

Hassan purchased a car for RM140,000 and used it for business and private purpose. The car is not licensed as a commercial vehicle, therefore the QE incurred is restricted to RM100,000 only. The proportion of business and private use is estimated to be 2/3 and 1/3 respectively. Hassan is entitled to claim 2/3 of the CA for deduction against his adjusted income from business.

13.3 Asset used in more than one business

A person who incurs the QE and uses the asset in more than one business is entitled to claim a portion of the CA for each of his business. The CA is computed based on the QE incurred. A reasonable apportionment of use of the asset amongst his businesses must be ascertained and it is usually computed based on time basis.

Example 28 (accounts closed on the same date)

Kirana Sdn Bhd purchased a machine for RM50,000 on 01.04.2011. The machine is used equally among its three businesses (P1, P2 and P3) which have the same accounting date ending on 30 June.

Computation of Capital Allowances

Year of Assessment 2011		
QE		50,000
IA (20% x 50,000)	10,000	
AA (14% x 50,000)	7,000	17,000
Residual Expenditure		33,000

Year of Assessment 2012			
AA (14% x 50,000)			7,000
Residual Expenditure			26,000
Year of Assessment 2013			
AA (14% x 50,000)			7,000
Residual Expenditure			19,000
The proportion of CA for the three businesses are as follows:			
Year Ending	P1(30/6)	P2(30/6)	P3 (30/6)
Year of Assessment 2011 : IA	3,333	3,333	3,334
: AA	2,333	2,333	2,334
Year of Assessment 2012 : AA	2,333	2,333	2,334
Year of Assessment 2013 : AA	2,333	2,333	2,334

Example 29 (accounts closed on different dates)

The facts are the same as in Example 28, except that the businesses (P1, P2 and P3) have different accounting periods, ending on 31 Mac, 30 June and 31 December respectively.

Computation of Capital Allowances

The proportion of CA for the three businesses are as follows			
Year Ending	P1(31/3)	P2(30/6)	P3 (31/12)
Year of Assessment 2011 : IA	-	5,000	5,000
: AA	-	3,500	3,500
Year of Assessment 2012 : AA	2,333	2,333	2,334
Year of Assessment 2013 : AA	2,333	2,333	2,334

P1 was not eligible for CA for the year of assessment 2011 as the asset was purchased on 01.4.2011 which was before the accounting period (01.04.10 to 31.03.2011) for the year of assessment 2011.

13.4 Asset not used in a business

A person who incurs the QE would not be allowed to claim CA on an asset if the asset is -

- (a) used for employment purposes,
- (b) used for personal purposes,
- (c) used for the purpose of the business of others. or
- (d) purchased for the purpose of a gift or donation.

13.5 Asset used by a person to manufacture products for the business of the beneficial owner

How an asset is used in a business and the way the business is conducted are important factors in determining whether the asset is used for the purpose of a business of a person. A person who incurs QE on an asset that is not used for the purpose of his business would not qualify for CA.

A beneficial owner is entitled to claim CA although the asset is registered in the name of another person (the legal owner) to produce the products for the beneficial owner, subject to the following conditions:

- (a) The beneficial owner incurs and bears the maintenance expenditure of the asset,
- (b) The beneficial owner determines how the products are manufactured,
- (c) The beneficial owner pays a sum of contract fees to the contract manufacturer solely for the manufacture of the products,
- (d) The contract manufacturer uses the asset wholly and exclusively to manufacture the products of the beneficial owner, and
- (e) The products are not the stocks-in-trade of the contract manufacturer.

The existence of a written agreement between the beneficial owner and the contract manufacturer would further justify the claim on CA.

Example 30

Memey Sdn Bhd (M) is a manufacturing company that produces canned seafood products. Due to shortage of space and skilled workers, M engaged

a contract manufacturer, Nano Sdn Bhd (N), to carry out the production. In relation to that, M provided and placed a few machines in the factory building of N. The business accounts indicated that -

- (a) M purchased the machines and registered it in the name of N,
- (b) M incurred the cost of maintenance and insurance premiums,
- (c) M determined the raw materials and oversees all the manufacturing processes,
- (d) N used the machines to manufacture the products of M only,
- (e) N received fees only for the contract,
- (f) N did not sell the products but transferred them to M, and
- (g) M showed the products as its stocks.

M is the beneficial owner as it has incurred the QE and fulfilled all the conditions set out in paragraph 13.5 of this PR. Therefore, M is entitled to claim CA on the machines although the machines is registered in the name of another person, N as the legal owner.

Example 31

Same facts as in Example 30 except that N, the contract manufacturer –

- (a) purchased the raw materials and billed to M,
- (b) determined the quantity and quality of the product,
- (c) used the machines to manufacture products of other clients, and
- (d) the products are its stocks-in-trade.

Though N is the legal owner of the machines and has used the machines in its business, N is not entitled to claim CA as it does not incur the QE.

M, who has incurred the QE is not entitled to claim CA as it is not using the machines for the purpose of its business. The conditions set out in paragraph 13.5 of this Ruling are not met.

Neither M nor N can claim CA in respect of the machines.

14 Asset Classified As Held For Sale

Asset classified as held for sale (HFS) means asset available for sale within one year or any period that may be extended and the asset is not used in the business. Assets that are worn-out and damaged are not included within the meaning of HFS.

14.1 A person who has incurred capital expenditure on an asset and classified it as HFS in a basis period would not be entitled to claim CA for the period as the asset is intended to be sold and is not used for purposes of the business.

14.2 If an asset that has been classified as HFS is reclassified as plant, property and equipment and then re-use them in the business, the QE for the purpose of claiming CA is the market value of the asset on the date the asset is reclassified. The market value of the asset is its fair value.

“Fair Value” means a rational and unbiased estimate of the potential market price of an asset when the actual market price cannot be determined. Fair value is the amount that shall be agreed between willing parties.

14.3 For further explanation on tax treatment of HFS asset, please refer to the Technical Guidelines titled ‘Guidelines For Income Tax Treatment Of Malaysian Financial Reporting Standards (MFRS) 5 : Non Current Assets Held For Sale and Discontinued Operations’ dated 04.06.2013 under Laws and Regulations of the IRBM website.

15 Procedure For Claiming Capital Allowances

CA claims shall be made by a person in the Income Tax Return Form (ITRF) for the relevant year of assessment. Schedules of CA computation and records must be kept by the person for the purpose of audit by IRBM officers.

**Director General of Inland Revenue,
Inland Revenue Board of Malaysia.**