



INLAND REVENUE BOARD MALAYSIA

DEDUCTION FOR LOSS OF CASH AND TREATMENT OF RECOVERIES

PUBLIC RULING NO. 4/2012

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LOSS OF CASH AND
TREATMENT OF RECOVERIES**

INLAND REVENUE BOARD MALAYSIA

**Public Ruling No. 4/2012
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CONTENTS

Page



DEDUCTION FOR LOSS OF CASH AND TREATMENT OF RECOVERIES

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**Public Ruling No. 4/2012
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1.	Introduction	1
2.	Related Provisions	1
3.	Interpretation	1
4.	Loss Of Cash	1
5.	Basis For Deductibility	1
6.	Deductibility Of Loss Of Cash Caused By Theft, Defalcation Or Embezzlement	2
7.	Supporting Evidence	4
8.	Tax Treatment Of Recoveries	5

DIRECTOR GENERAL'S PUBLIC RULING

A Public Ruling as provided for under section 138A of the Income Tax Act 1967 is issued for the purpose of providing guidance for the public and officers of the Inland Revenue Board Malaysia. It sets out the interpretation of the Director General of Inland Revenue in respect of the particular tax law, and the policy and procedure that are to be applied.

A Public Ruling may be withdrawn, either wholly or in part, by notice of withdrawal or by publication of a new ruling which is inconsistent with it.

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

1. This Ruling explains:
 - (i) the deductibility of loss of cash in the course of business caused by theft, defalcation or embezzlement; and
 - (ii) the income tax treatment of recoveries in respect of the loss of cash which has been given a tax deduction in an earlier year.
2. This Ruling is to replace Public Ruling No. 5/2005 dated 14 November 2005. Among the changes made to that Public Ruling are-
 - (i) subparagraph 6.1 (now subparagraph 7.1) has been rephrased
 - (ii) paragraph 7 (now paragraph 8) has been rephrased
 - (iii) paragraph 8 has been replaced by paragraph 9
 - under subsection 22(2) of the Income Tax Act 1967 (ITA 1967) recovery is taxed on receivable or deemed received basis and not on received basis.
3. The provisions of the ITA 1967 related to this Ruling are sections 33 and 22.
4. The words used in this Ruling have the following meaning:
 - (i) "Employee" means a subordinate employee but excludes an employee in a managerial capacity.
 - (ii) "Recoveries" means monies received in connection with loss of cash caused by theft, defalcation or embezzlement.
 - (iii) "Director" includes any person who occupies the position of a director or any person in accordance with whose directions or instructions the directors or staff of a company are accustomed to act.
 - (iv) "Cash" means cash and cheques in respect of trading transactions.

5. **Loss Of Cash**

Loss of cash caused by theft, defalcation or embezzlement may happen in the course of business. This loss of cash is allowable as a deduction in computing the adjusted income of a business for the basis period for a year of assessment provided such loss is incidental to the business carried on.

6. **Basis For Deductibility**

Claims for loss of cash should be supported by sufficient evidence. All matters relating to the loss of cash should be considered first before decision is taken to claim the losses. Among the factors to be considered are as follows:

- (i) the persons involved, that is the employee in the case of embezzlement or defalcation and the employee or third party in the case of a theft or robbery;
- (ii) the action taken against the person involved namely, police report, termination of service and recovery of loss;
- (iii) the situation in which the loss occurs, that is the incident is a recognised incident of the taxpayer's business and has to occur in the ordinary course of carrying on the business; and
- (iv) the amount of loss should not be out of proportion to the reasonably expected risks of the business.

7. Deductibility Of Loss Of Cash Caused By Theft, Defalcation Or Embezzlement

7.1 Loss of cash deductible

Loss of cash caused by theft, defalcation or embezzlement in the course of business may be allowed as a deduction in computing the adjusted income under the following circumstances:

7.1.1 Theft or embezzlement by third party if-

- (i) banking of cash takings is a necessary part of the operations of the business, any loss of cash caused by theft or robbery while in transit to the bank is allowable.

Example 1

A Sdn Bhd deposits its cash collections daily. The company's van carrying cash of RM50,000 was robbed while on the way to the bank.

The loss of cash of RM50,000 is allowable as a deduction.

- (ii) an agent who is assigned to collect the cash embezzles the cash, the loss is allowable as a deduction.

Example 2

B Sdn Bhd, a furniture company, appoints an agent to collect instalment payments from clients. The agent had collected RM50,000 and misused the cash by investing in the share market. He suffered losses and absconded. The company was unable to trace the agent.

The loss of RM50,000 is allowable as a deduction.

7.1.2 Theft or embezzlement by employee

Loss of cash caused by theft, defalcation or embezzlement by an employee is allowable as it arises directly from the necessity of delegating certain duties of the business to employee.

Example 3

A clerk working in Bank C had been stealing money from customers' accounts. When detected it was found that RM10,000 had been embezzled. The bank terminated the services of the clerk.

The loss of RM10,000 is allowable as a deduction as the bank clerk embezzled the monies in the course of his duties as an employee and the loss was caused in the course of the business.

Example 4

Miss D was employed as an accounts clerk at Beautiful Wear Apparels. The store owner noticed that 9 cheques were missing during the year 2011. It was discovered that Miss D had cashed the 9 cheques for RM8,000 with forged signatures. Her services were terminated by the store.

The loss of RM8,000 is an allowable deduction as the theft arises out of the necessity of allowing the accounts clerk to handle the cheques.

7.2 Loss of cash not deductible

Loss of cash caused by theft, defalcation or embezzlement cannot be allowed as a deduction in computing the adjusted income under the following circumstances:

- 7.2.1 The employee who is involved in the theft or embezzlement is a relative of the proprietor, and there is clear evidence that the proprietor proposes to overlook the theft and even continues to employ the offender. Such a loss would not be regarded as a trade loss.

Example 5

Mr E, the owner of a sundry shop, suffered a loss of RM5,000 embezzled by his brother who is his employee. Mr E claimed the loss. However, no action was taken against the brother for the recovery of the loss and it is not deductible.

The loss of RM5,000 is not an allowable deduction since no action has been taken against the employee to recover the loss.

- 7.2.2 Loss of cash or embezzlement by a sole proprietor, a partner, a director of a company or an administrator of a deceased person's estate or any person who is in control of the business operations.

Example 6

A service director of a company Mr F had embezzled cash collections of RM10,000. A new director had discovered the loss and the sum was claimed as loss by embezzlement in the profit and loss account.

The loss of RM10,000 is not allowable as a deduction.

- 7.2.3 Loss of cash caused by theft, burglary or robbery which is not incidental to the business is not allowable as a deduction.

Example 7

Mr G, a money-changer, brought home cash amounting to RM15,000 from his office and kept the cash in the strong room in his house. Thieves broke into his house and stole the cash.

The loss of cash of RM15,000 is not allowable as the loss of cash is not an incident in carrying on Mr G's business. The loss had fallen on Mr G as the owner of the cash which was temporarily not being used for his business.

8. Supporting Evidence

Any claim for a deduction for loss of cash caused by theft, defalcation or embezzlement should be substantiated by more than one of the following documents:

- (i) police report;
- (ii) bank statement;
- (iii) responsibility of the staff involved;
- (iv) letter of termination of employment;
- (v) the minutes of board of directors meeting;
- (vi) proof of recovery action; or
- (vii) other relevant documents.

Example 8

Mr H, an employee of Syarikat Utama Sdn Bhd, is a door-to-door salesman selling electrical products. Puan Aminah had bought electrical goods amounting to RM5,000 and the payment was made by cheque. The cheque was embezzled by Mr H and this was discovered by his supervisor. Proof of payment by Puan Aminah was obtained and a police report was made.

The proof of payment and the police report should be kept as evidence of embezzlement by Mr H to substantiate a claim for tax deduction.

9. Tax Treatment Of Recoveries

9.1 Loss of cash that has been allowed in computing the adjusted income has to be taken as gross income of a business when such recoveries are obtained through-

- (i) insurance;
- (ii) agreement of payment from the employee concerned;
- (iii) legal action; or
- (iv) other recovery actions.

9.2 Recovery of cash is gross income from a business for the basis period for a year of assessment in which it is receivable or deemed to have been received. The date the cash is actually received is irrelevant.

In the case of recovery where payments made are based on an agreement between both parties, the whole amount is taken as business income at the date the amount is agreed or determined.

In short, the full amount of any recovery shall be treated as a gross income for the basis period for the year of assessment in which it is first receivable.

Example 9

Restoran J which closes its accounts on 31 December each year frequently encountered loss of cash through embezzlement by its cashiers. In the year 2010, RM50,000 was embezzled by several cashiers. The company made an insurance claim for the loss of cash on 29.12.2010. On 30.1.2012 the company recovered RM40,000 from the insurance company.

- The loss of cash of RM50,000 has been allowed as a deduction in calculating the adjusted income from the business for the year of assessment 2010.

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- The sum of RM40,000 received from the insurance company should be taxed as income of the business for the year of assessment 2012.

Example 10

Same facts as in Example 9, except that after the insurance claim was made, several consultations were held with the insurance company and the insurance company agreed on 15.12.2011 to pay RM40,000. Cheque for the payment was received on 30.1.2012.

The amount of RM40,000 is deemed to have been received on 15.12.2011 and should be taxed as business income for the year of assessment 2011 as RM40,000 was receivable in the basis period for the year of assessment 2011.

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