



INLAND REVENUE BOARD MALAYSIA

**DOUBLE DEDUCTION INCENTIVE ON
RESEARCH EXPENDITURE**

**ADDENDUM TO
PUBLIC RULING NO. 5/2004**

Translation from the original Bahasa Malaysia text.

DATE OF ISSUE: 3 APRIL 2008



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A Public Ruling may be withdrawn, either wholly or in part, by notice of withdrawal or by publication of a new ruling which is inconsistent with it.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



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DOUBLE DEDUCTION INCENTIVE ON RESEARCH EXPENDITURE ADDENDUM TO PUBLIC RULING NO. 5/2004

1. This Addendum provides clarification and tax treatment in relation to the:
 - (a) special deduction for research expenditure granted to a pioneer company under subsection 34(4A) of the Income Tax Act 1967 (ITA); and
 - (b) ascertainment of the adjusted income of a pioneer company which has made an election under subsection 34A(4A) of the ITA.

The Addendum also provides further clarification in relation to Public Ruling No. 5/2004 with regards to the:

- (c) definition of holding company - paragraphs 15.5 and 16.3; and
 - (d) amount claimed in the tax computation - paragraph 20.
2. The related provisions are proviso to subsection 34A(4), subsections 34A(4A) and 34A(6) of the ITA.
3. The words used in this ruling have the following meanings:
 - 3.1 "Pioneer company" means a company certified by a pioneer certificate issued by the Ministry of International Trade and Industry (MITI) and has the meaning assigned to it under the Promotion of Investments Act 1986 (PIA).
 - 3.2 "Post-pioneer business" means the business of a pioneer company deemed under section 15 of the PIA to have been set up and commenced on the day following the end of its tax relief period.
 - 3.3 "Promoted activity" means a manufacturing, agricultural, integrated agricultural, hotel, tourist or other industrial or commercial activity as determined by the Minister of International Trade and Industry.
 - 3.4 "Qualifying research expenditure" means the expenditure specified in paragraphs 13 and 14 of Public Ruling No. 5/2004.

4. **Election by a pioneer company - subsection 34A(4A), ITA**

- 4.1 A pioneer company which has incurred qualifying research expenditure for an approved project in any basis period during its tax relief period, may elect that the amount of that expenditure be deducted in the first basis period in respect of its post-pioneer business for a year of assessment. The election has to be done on a yearly basis for each relevant year of assessment.
- 4.2 By making an election, the amount of qualifying research expenditure for each particular year of assessment will be accumulated and carried forward to be deducted in the first basis period of the post-pioneer business instead



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of being given a double deduction for each relevant year of assessment. The amount of deduction to be made in the post-pioneer period is equivalent to the amount of qualifying research expenditure incurred for each year of assessment.

- 4.3 The introduction of subsection 34A(4A) is effective from year of assessment 2003.

Example 1:

Sokudu Electronics Sdn Bhd (Sokudu Electronics) is situated in Shah Alam and started its operation on 01/01/2003. The company closes its accounts on 31 December every year. The company was granted pioneer status for its promoted activity and the production day was 01/07/2003 as stated in the pioneer certificate. The tax relief period was from 01/07/2003 to 30/06/2008. Sokudu Electronics incurred expenditure on research and elected for a deduction under subsection 34A(4A) of the ITA. Details of the expenditure are as follows:

Period	Research expenditure claimed (RM)	Non-Qualifying research expenditure after audit (RM)	Qualifying research expenditure (RM)	Net Profit as per P&L account (RM)
01/01/2003 - 30/06/2003	100,000	10,000	90,000	320,000
01/07/2003 - 31/12/2003	NIL	NIL	NIL	400,000
01/01/2004 - 31/12/2004	300,000	NIL	300,000	800,000
01/01/2005 - 31/12/2005	500,000	50,000	450,000	1,230,000
01/01/2006 - 31/12/2006	NIL	NIL	NIL	1,800,000
01/01/2007 - 31/12/2007	1,000,000	150,000	850,000	2,300,000
01/01/2008 - 30/06/2008	NIL	NIL	NIL	1,360,000
01/07/2008 - 31/12/2008	200,000	NIL	200,000	1,500,000

The research for each year of assessment was approved by the Minister of Finance. The amount of qualifying research expenditure allowable for deduction against the company's gross income under section 34A and subsection 34A(4A) are as follows:



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Period	Qualifying research expenditure (RM)	Amount allowable for deduction (RM)
01/01/2003 - 30/06/2003	90,000	180,000
01/07/2003 - 31/12/2003	NIL	NIL
01/01/2004 - 31/12/2004	300,000	300,000
01/01/2005 - 31/12/2005	450,000	450,000
01/01/2006 - 31/12/2006	NIL	NIL
01/01/2007 - 31/12/2007	850,000	850,000
01/01/2008 - 30/06/2008	NIL	NIL
01/07/2008 - 31/12/2008	200,000	400,000

01/01/2003 - 30/06/2003 (pre-pioneer period)	:	RM180,000 (RM90,000 X 2)
01/01/2004 - 31/12/2004 (pioneer period)	:	RM300,000
01/01/2005 - 31/12/2005 (pioneer period)	:	RM450,000
01/01/2007 - 31/12/2007 (pioneer period)	:	RM850,000
01/07/2008 - 31/12/2008 (post-pioneer period)	:	RM400,000 (RM200,000 X 2)

Sokudu Electronics is eligible to claim double deduction for research expenditure incurred during the pre-pioneer and post-pioneer periods under section 34A of the ITA. Whereas for research expenditure incurred during the tax relief period (01/07/2003 - 30/06/2008), the company has elected under subsection 34A(4A) of the ITA to accumulate the qualifying research expenditure totalling RM1,600,000 to be carried forward to the first basis period of its post-pioneer business and this amount shall be deducted from its gross income for the period 01/07/2008 to 31/12/2008.

5. Ascertainment of adjusted income of a pioneer company which has made an election under subsection 34A(4A) of the ITA.

The following example gives an illustration of the ascertainment of the adjusted income of a pioneer company which has made an election under subsection 34A(4A) of the ITA.

Example 2:

Using the facts in Example 1 and assuming that Sokudu Electronics charged research expenditure in its P&L account for all the years of assessment concerned



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and no disallowable expenses for taxation purpose were claimed in the P&L, the adjusted income of Sokudu Electronics after deduction of qualifying research expenditure for years of assessment 2003 and 2008 are as follows:

	YA 2003		YA 2008	
	Pre-pioneer	Pioneer	Pioneer	Post-pioneer
Net profit per P&L	320,000	400,000	1,360,000	1,500,000
Add: Research expd.	<u>100,000</u>	-	-	<u>200,000</u>
	420,000	-	-	1,700,000
Less: Qualifying research expd.	<u>180,000</u>	-	-	<u>*1,700,000</u>
Adjusted Income	<u>240,000</u>	<u>400,000</u>	<u>1,360,000</u>	NIL
Unabsorbed R&D expenditure c/f				<u>300,000</u>

* Qualifying R&D expenditure accumulated during tax relief period : RM1,600,000
 Qualifying R&D expenditure for the post-pioneer period : 400,000
 Total qualifying R&D expenditure : **2,000,000**

6. The application procedures for approval for research projects/activities as stated in the Public Ruling No. 5/2004 are also applicable to a pioneer company.
7. To further clarify on the meaning of holding company in relation to research projects and research expenditure for related companies stated in paragraphs 15.5 and 16.3 of Public Ruling No. 5/2004, the mentioned paragraphs are substituted with the following paragraphs:

15.5 Research projects for related companies

As a concession, a holding company which undertakes research projects/activities at its research centre on behalf of companies within its group may submit an application for approval of research projects/activities on behalf of its subsidiary or associate companies. However, the details for each subsidiary or associate company should be separately and clearly stated. For the purpose of this ruling, a holding company refers to a company

solely engaged in the activity of research and provides research services to its subsidiary or associate companies.



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16.3 Research expenditure for related companies

In cases where research is undertaken by a holding company referred to in paragraph 15.5 for its subsidiary or associate companies, allowable expenditure incurred in relation to a project undertaken on behalf of the subsidiary or associate companies shall be allocated to each company. The subsidiary or associate companies may claim double deduction based on the allocation of expenditure made by the holding company. Research fees paid to the holding company will not be allowed a double deduction. No double deduction can be claimed by the holding company.

8. Paragraph 20 of Public Ruling No. 5/2004 is substituted with the following paragraph to provide further clarity in the method of ascertaining the adjusted income of a company which is entitled for the deduction for research projects under section 34A of the ITA.

20. Amount claimed in the tax computation

The amount of deduction shall be twice the amount of expenditure, not being capital expenditure incurred in the basis period. To ensure only qualifying research expenditure is given double deduction, a claim for research expenditure which has been charged in the profit and loss account will be adjusted in the tax computation. This is done by adding back in the tax computation the amount of research expenditure claimed in the P&L account, followed by deducting twice the amount of qualifying research expenditure in the tax computation. If the research expenditure incurred is capitalised in the balance sheet, a deduction of twice the amount of qualifying expenditure shall be allowed in the tax computation. However, the amount of deduction for a pioneer company which has made an election under subsection 34A(4A) of the ITA is only the amount of qualifying research expenditure incurred by the company during the tax relief period.

9. This Addendum forms part of the Public Ruling No. 5/2004 and is effective from year of assessment 2008.

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