



INLAND REVENUE BOARD OF MALAYSIA

**LOAN OR ADVANCES TO DIRECTOR BY
A COMPANY**

PUBLIC RULING NO. 8/2015

Translation from the original Bahasa Malaysia text

DATE OF PUBLICATION: 30 NOVEMBER 2015



INLAND REVENUE BOARD OF MALAYSIA

**LOAN OR ADVANCES TO DIRECTOR
BY A COMPANY**

**Public Ruling No. 8 /2015
Date of Publication: 30 November 2015**

Published by:

Inland Revenue Board of Malaysia

First edition

© 2015 by Inland Revenue Board of Malaysia

All rights reserved on this Public Ruling are owned by Inland Revenue Board of Malaysia. One print or electronic copy may be made for personal use. Professional firms and associations are permitted to use the Public Ruling for training purposes only. Systemic or multiple reproduction, distribution to multiple location via electronic or other means, duplication of any material in this Public Ruling for a fee or commercial purposes, or modification of the content of the Public Ruling are prohibited.



INLAND REVENUE BOARD OF MALAYSIA

| CONTENTS | PAGE |
|--|------|
| 1. Objective | 1 |
| 2. Relevant Provisions of the Law | 1 |
| 3. Interpretation | 1 |
| 4. Tax Treatment | 2 |
| 5. Interest Income Computation On Loan Or Advances To Directors of The Company | 8 |
| 6. Loan Or Advances By A Dormant Company To Directors of The Company | 15 |
| 7. Other Provisions Related To Loan Or Advances To Directors | 16 |

DIRECTOR GENERAL'S PUBLIC RULING

Section 138A of the Income Tax Act 1967 [ITA] provides that the Director General is empowered to make a Public Ruling in relation to the application of any provisions of the 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 this Public Ruling either wholly or in part, by notice of withdrawal or by publication of a new Public Ruling.

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

1. Objective

The objective of this Public Ruling (PR) is to explain the tax treatment of:

- (a) company that provides loans or advances to director of the company without interest or with interest rate lower than the arm's length rate; and
- (b) interest income deemed to be received by the company from the loans or advances.

2. Relevant Provisions of The Law

- 2.1. This PR takes into account laws which are in force as at the date this PR is published.
- 2.2. The provisions of the Income Tax Act 1967 (ITA) related to this PR are sections 2 and 140B, subsections 21A(8), 29(3), 75A(2) and 140(2) and paragraph 4(c).

3. Interpretation

The words used in this PR have the following meanings –

- 3.1 "Interest" is the return or compensation for the use or retention by a person of a sum of money belonging to or owed to another
- 3.2 "Employer", in relation to an employment, means –
 - (a) where the relationship of master and servant subsists, the master;
 - (b) where the relationship of master and servant does not subsist, the person who pays or is responsible for paying any remuneration to the employee who has the employment, notwithstanding that that person and the employee may be the same person acting in different capacities.
- 3.3 "Employee", in relation to an employment, means –
 - (a) where the relationship of master and servant subsists, the servant;
 - (b) where that relationship does not subsist, the holder of the appointment or office which constitutes the employment.
- 3.4 "Employment" means –
 - (a) employment in which the relationship between master and servant subsists;

(b) any appointment or office, whether public or not and whether or not that relationship subsists, for which remuneration is payable.

3.5 "Director" means the director of a company as defined under subsection 75A(2) of the ITA.

3.6 "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 have agreed to combine any of their right, 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, a limited liability partnership and any association which is established pursuant to scheme of financing in accordance with the principles of *Syariah*.

3.7 "Company" means a body corporate and includes any body of persons established with a separate legal identity by or under the laws of a territory outside Malaysia and a business trust.

3.8 "Year of assessment" means the calendar year.

3.9 "Basis period", in relation to a person, a source of his and a year of assessment, means such basis period, if any, as is ascertained in accordance with section 21 or 21A.

4. Tax Treatment

4.1. Loans or advances to directors

Company that provides loans or advances to directors without interest or with interest rate lower than the arm's length rate is deemed to receive interest income from the loans or advances for the basis period for a year of assessment and assessed under paragraph 4(c) of the ITA.

If the company provides loans or advances to directors which are fully funded from internal funds, the company shall be deemed to have a gross income consisting of interest from such loans or advances for that basis period and section 140B of the ITA is applicable.

However, if the loans or advances to directors are financed from external funds or third party, then the provision of section 140B of the ITA is not applicable.

4.2 Funds for loans or advances

Loans or advances to directors of the company may be financed by the following three (3) categories of funds –

4.2.1. Internal funds

Internal funds are surplus funds that may arise from the injection of capital, retained earnings and company reserves.

Example 1

A Sdn Bhd made interest-free loans of RM100,000 to directors of the company funded by the company reserves on 1.3.2014. Loan repayment period set by the company to directors is for 5 years commencing from 1.4.2014. No repayment of loans was made by the directors as at 31.12.2014.

For the purposes of section 140B of the ITA, the company is deemed to receive interest income on loans given to the directors from internal funds from 1.4.2014. Determination of interest income deemed to be received by the company is based on prescribed formula with the Average Lending Rate (ALR) published by Bank Negara Malaysia (BNM) and assessed under paragraph 4(c) of the ITA.

Example 2

B Sdn Bhd (accounts closed on 31December) is a subsidiary of C Sdn Bhd. On 1.5.2012, C Sdn Bhd has injected a capital of RM2 million to B Sdn Bhd to expand the company's business. Part of the capital acquired by B Sdn Bhd was made to a director of the company after being approved at the company's board of directors meeting. Details of the loan to director are as follows:

| Date of Loan | Total Loan | Interest Rate | Tenure |
|--------------|------------|---------------|---------|
| 1.10.2014 | RM300,000 | 2% | 5 years |

The loan made to the director is subject to section 140B of the ITA because it is financed by internal funds of the company. Determination of interest income deemed to be received by B Sdn Bhd is in accordance with the formula prescribed under subsection 140B(2) of the ITA or based on the amount of interest charged by the company, whichever is higher as provided under subsection 140B(3) of the ITA.

Example 3

D Sdn Bhd (accounts closed on 31December) had obtained a bank loan of RM1 million with an interest rate of 4% per annum on 1.2.2014. Loan repayment period is 5 years. The loan was used by

the company to expand its business by opening several new branches and introduced several new products. Based on strategies that have been implemented, the company's profits increased by 20% to 40% in 2014, 2015 and 2016. The company successfully paid off the loan and interest within the specified time frame. On 1.1.2017, at the board of directors meeting the company agreed to provide an interest-free loan of RM200,000 to company directors from retained profits of the company. Loan repayment period by the directors is 5 years.

The loans made to the directors are subject to section 140B of the ITA and the determination of interest income deemed to be received by D Sdn Bhd is in accordance with the prescribed formula with the ALR published by BNM and assessed under paragraph 4(c) of the ITA.

4.2.2. External Funds

External funds refer to financial resources acquired by a company through loans from third parties such as banks or related companies specifically used to finance loans or advances to directors. The decision to acquire loans from external funds can be referred from the board of directors resolution or board of directors meeting minutes.

Example 4

Same facts as in Example 1. On 1.11.2014, A Sdn Bhd once again proposed to made loans to directors of the company amounting to RM100,000 which are funded from external funds. The decision to give the loan has been agreed in the company's board of directors meeting.

The loans to directors on 1.11.2014 are not subject to section 140B of the ITA because the loans are financed by funds from third party.

Example 5

G Sdn Bhd has set a policy to provide funds for loans to directors which are funded from bank loans. For that purpose, the company has obtained a loan of RM1 million from a bank to finance any loan requested by directors within 3 years.

The loans given to directors are not subject to section 140B of the ITA because the financing is obtained from external funds.

4.2.3. Mixed Funds

If loans or advances to director are from internal funds and external funds, the interest income is computed only on the portion related to amount of internal funds. In such circumstances, the company must prove that some / all of the loans or advances are from external funds and not subject to section 140B of the ITA. If the loan from external funds are used partly for business and partly for investment purposes, then interest restriction under subsection 33(2) of the ITA is applicable. Please refer to PR No. 2/2011 dated 7 February 2011 for more information.

Example 6

H Sdn Bhd has 3 directors who hold ordinary shares of the company respectively as follows –

| No | Name of Director | Shareholdings (%) |
|----|------------------|-------------------|
| 1 | Director A | 30% |
| 2 | Director B | 30% |
| 3 | Director C | 40% |

Based on board of directors resolution, the company agreed to provide interest-free loans amounting to RM1 million on 1.11.2014 to all the directors of the company according to the percentage of shareholding of each director. The loans were financed by internal funds of RM600,000 and external funds of RM400,000. Total loans given are as follows –

| No. | Name of Director | Total Loans (RM) | | |
|--------------|------------------|------------------|----------------|------------------|
| | | Internal Funds | External Funds | Total |
| 1 | Director A (30%) | 180,000 | 120,000 | 300,000 |
| 2 | Director B (30%) | 180,000 | 120,000 | 300,000 |
| 3 | Director C (40%) | 240,000 | 160,000 | 400,000 |
| Total | | 600,000 | 400,000 | 1,000,000 |

For the purposes of section 140B of the ITA, interest income on loans made to directors will be calculated on the portion of loans financed by internal funds only.

Example 7

J Sdn Bhd has obtained a bank loan of RM2 million with interest at 4% per annum. The loan is for purposes of business and also loans to directors. Total loans made to directors are RM300,000. Loans to directors are interest-free.

In this case, no interest income is deemed to be received by J Sdn Bhd because the loans are from external funds.

4.3 Loans or advances from external funds to directors who are also employees of a company

If a company obtains a loan from third party to make loans or advances to directors who are also employees, then the amount of perquisites to the directors are the interest costs incurred by the employer to fund the loan facility. Perquisites are employment benefits to the employees concerned and are part of the employees' gross income under paragraph 13(1)(a) of the ITA.

Further information regarding the tax treatment of perquisites received by an employee can be referred to PR No. 2/2013 dated 28 February 2013.

4.4 Loans or advances to directors via a partnership

For loans or advances made by a company to a partnership in which the partners are also directors of the company providing the loan, the loans or advances given are subject to section 140B of the ITA. Partnership is not a separate legal entity. This means management, power, legal action and responsibility for the partnership is on each of the partner. Therefore, a loan given to the partnership is deemed to be given to the directors. The provision only applies to the partner who is also a director of the company. Total loans made to directors are based on the percentage of capital contribution of each partner.

Example 8

On 1.6.2014, K Sdn Bhd lent RM300,000 to XYZ Partnership which is a partnership where the partners are also directors who hold more than 20% of ordinary shares in K Sdn Bhd.

Details of directors' shareholdings and capital contributions in K Sdn Bhd and XYZ Partnership respectively are as follows:

| No. | Name of Director | Shareholdings in K Sdn Bhd(%) | Capital Contribution in XYZ Partnership (%) |
|------------|-------------------------|--------------------------------------|--|
| 1 | Director M | 20 | 20 |
| 2 | Director N | 20 | 20 |
| 3 | Director H | 60 | 60 |

For purposes of section 140B of the ITA, loans made to XYZ Partnership are deemed made to directors of the company since the partners and directors are the same persons.

Example 9

Same facts as in Example 8. However shareholding and capital contribution of each director in K Sdn Bhd and XYZ Partnership respectively are as follows:

| No. | Name of Director | Shareholdings in K Sdn Bhd (%) | Capital Contribution in XYZ Partnership (%) |
|------------|-------------------------|---------------------------------------|--|
| 1 | Director M | 30 | 30 |
| 2 | Director N | 10 | 10 |
| 3 | Director H | 60 | 60 |

Since shareholding of Director N is less than 20%, he is not defined as 'director' under subsection 75A(2) of the ITA. Therefore for the purposes of section 140B of the ITA, only 90% of the loans to XYZ Partnership is taken to compute the interest income deemed to be received by K Sdn Bhd.

Example 10

L Sdn Bhd lent RM700,000 to ABC Partnership with interest rate of 4%. ABC Partnership has 3 partners where two of the partners are also directors of L Sdn Bhd.

Shareholdings and capital contributions by the directors in L Sdn Bhd and in ABC Partnership are as follows-

| No. | Name of Director | Shareholdings In L Sdn Bhd (%) | Capital Contribution In ABC Partnership (%) |
|------------|-------------------------|---------------------------------------|--|
| 1 | Director P | 50 | 30 |
| 2 | Director S | 50 | 30 |
| 3 | Director T | - | 40 |

Capital contributions by Director P and S are 30% each. The total capital contributions from both directors (60%) will be used as the basis for determining the total amount of loans made to directors. Therefore, from the

amount of RM700,000 given to ABC Partnership, an amount of RM420,000 will be subject to section 140B of the ITA and computation will be based on the prescribed formula in subsection 140B(2) of the ITA.

5. Interest Income Computation On Loan Or Advances To Directors of The Company

5.1. Determination of interest income deemed to be received

For the purpose of determining the rate and amount of interest income that is deemed to be received by a company in the basis period for year of assessment, the interest will be computed monthly on the loan balance based on the formula below -

$$\frac{1}{12} \times A \times B$$

where –

A = the total amount of loans or advances outstanding at the end of the calendar month; and

B = ALR of commercial banks published by BNM on interest free loan or advances at the end of the calendar month or other reference lending rate as may be prescribed by the Director General of Inland Revenue if there is no ALR published .

Total loans or advances outstanding at the end of the calendar month refers to balance of loans or advances after deducting repayment of loans or advances and adding any new loans or advances made during that month.

5.2. Effective date of the provision

The provision of section 140B of the ITA is effective from the year of assessment 2014 and subsequent years of assessment. The determination of the interest income deemed to be received by the company will be computed on any loans or advances outstanding at the end of each calendar month. This includes any existing balance on loans or advances made before the year of assessment 2014.

Example 11

M Sdn Bhd made a loan of RM1 million to a director of the company on 10.8.2012 without charging any interest. No repayment has been made by the directors as at 31.12.2014. Interest income for the year of assessment 2014 to M Sdn Bhd is computed as follows –

| Month | Loan Balance (RM) | ALR (%)* | Interest Income Deemed To Be Received (RM) |
|--|-------------------|----------|--|
| Jan 2014 | [b/f] 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Feb 2014 | 1,000,000 | 4.5 | $1,000,000 \times 4.5\% \times 1/12 = 3,750$ |
| Mar 2014 | 1,000,000 | 4.5 | $1,000,000 \times 4.5\% \times 1/12 = 3,750$ |
| Apr 2014 | 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| May 2014 | 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Jun 2014 | 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Jul 2014 | 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Aug 2014 | 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Sept 2014 | 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Oct 2014 | 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Nov 2014 | 1,000,000 | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Dec 2014 | 1,000,000 [c/f] | 4.6 | $1,000,000 \times 4.6\% \times 1/12 = 3,833$ |
| Total Interest Income Deemed To Be Received | | | 45,830 |

* ALR for purposes of illustration only.

Total interest income deemed to be received by the company is RM45,830 and will be assessed under paragraph 4(c) of the ITA.

If a company's basis period for the year of assessment 2014 commenced in the year 2013, then the interest income taken into account is the amount of interest computed on the loans or advances outstanding from 1.1.2014.

Example 12

N Sdn Bhd closes its accounts on 30 April of each year. Accounting period for the year of assessment 2014 was from 1.5.2013 to 30.4.2014. N Sdn Bhd made interest-free loan of RM50,000 to a director of the company on 1.7.2013. No repayment of loans has been made by the director as at the end of the accounting period.

For the purposes of section 140B of the ITA, interest income assessed on the company for the year of assessment 2014 is computed on the loan balance at the end of each calendar month from 1.1.2014 to 30.4.2014 only.

5.3. Determination and the amount of interest income deemed to be received by the company

The amount of interest determined or deemed to be received by the company is subject to the rate of interest charged, namely -

a) Interest-Free

If the loans or advances made by a company to directors are interest-free, then the amount of interest will be computed or determined based on the prescribed formula with ALR published by BNM in the basis year in which the loans or advances are given.

i) No repayment is made by director

Example 13

On 1.10.2014, P Sdn Bhd made advances of RM100,000 to directors for personal purposes. The advances are interest-free and sourced from internal funds. There are no fixed terms of repayment by the company to the directors. No repayments have been made by the directors involved as at 31.12.2014. ALR published by BNM for the period October to December 2014 is 4% per annum.

Computation of interest for the year of assessment 2014 is computed as follows-

| Month | Advances Balance (RM) | Interest Income Deemed To Be Received (RM) |
|--|------------------------------|---|
| Oct 2014 | 100,000 @ 4% x 1/12 | 333 |
| Nov 2014 | 100,000 @ 4% x 1/12 | 333 |
| Dec 2014 | 100,000 @ 4% x 1/12 | 333 |
| Total Interest Income Deemed To Be Received | | 999 |

Example 14

Director A who is also a shareholder of Q Sdn Bhd has obtained an interest-free loan from the company amounting to RM100,000 in

February for the year of assessment 2014.

Director A does not make any payment for the year of assessment 2014 which is supposed to commence from March 2014. Q Sdn Bhd is deemed to receive interest income from the loan based on ALR published by BNM (assuming ALR 3%) for the year 2014.

Interest income deemed to be received by Q Sdn Bhd for the year of assessment 2014 will be assessed under paragraph 4(c) of the ITA and computed according to the formula as follows:

| Year of Assessment 2014 | Loan Balance (RM) | Interest Income Deemed To Be Received (RM) |
|--------------------------------|--------------------------|---|
| Mar – Dec | 100,000 @ 3% x10 /12 | 2,500 |

ii) Repayment made by director

Example 15

Director B who is also a shareholder of R Sdn Bhd has obtained an interest-free loan of RM100,000 for the year of assessment 2014 from the company in February 2014.

In April 2014, Director B made payments totaling RM10,000 for payment due in March 2014. In September 2014, R Sdn Bhd made additional advances of RM30,000 to Director B.

Computation of interest income deemed to be received by R Sdn Bhd for the year of assessment 2014 based on the formula in subsection 140B(2) of the ITA (assuming ALR is 3%) is as follows -

Year of Assessment 2014

| Month | Loan Balance (RM) | Interest Income Deemed To Be Received (RM) |
|--------------|--------------------------------|---|
| Mar | 100,000 @ 3% x 1/12 | 250 |
| Apr | (100,000 – 10,000) @ 3% x 1/12 | 225 |
| May | 90,000 @ 3% x 1/12 | 225 |
| Jun | 90,000 @ 3% x 1/12 | 225 |
| Jul | 90,000 @ 3% x 1/12 | 225 |

| | | |
|--|-------------------------------|--------------|
| Aug | 90,000 @ 3% x 1/12 | 225 |
| Sept | (90,000 + 30,000) @ 3% x 1/12 | 300 |
| Oct | 120,000 @ 3% x 1/12 | 300 |
| Nov | 120,000 @ 3% x 1/12 | 300 |
| Dec | 120,000 @ 3% x 1/12 | 300 |
| Total Interest Income Deemed To Be Received | | 2,575 |

R Sdn Bhd is deemed to receive interest income for the basis period for the year of assessment 2014 amounting to RM2,575 based on the prescribed formula. Interest income deemed to be received by the company is to be assessed under paragraph 4(c) of the ITA.

b) With interest

If a company charges interest on loans or advances to directors, then the amount of interest that is deemed to be received by the company under section 140B of the ITA will be determined by comparing the amount of interest calculated based on -

- (i) interest rates charged by the company; or
- (ii) formula in subsection 140B(2) of the ITA.

The total interest income, whichever is higher will be taken as the interest income deemed to be received by the company in the basis period for a year of assessment.

i) The interest rate charged by the company is higher than the ALR published by BNM

If the amount of interest charged on the loans or advances by the company is more than the interest computed by using the formula in subsection 140B(2) of the ITA, then the interest due and payable by the director to the company will be taken as the interest income of the company for the basis period for a year of assessment and assessed under paragraph 4(c) of the ITA. The provisions of section 140B of the ITA shall not apply in such cases.

Example 16

On 1.3.2014, S Sdn Bhd made an advance of RM100,000 to Director C with an interest rate of 5% compared to ALR published

by BNM of 3%. In April 2014, Director C made a payment totaling RM10,000. In September 2014, S Sdn Bhd made additional advance of RM30,000 to the Director C.

For the determination of interest income on advances given, the amount of interest which is higher will be taken for the computation of interest income to S Sdn Bhd in the year of assessment 2014. The computation is as follows-

Year of Assessment 2014

| Month | Loan Balance (RM) | Interest Charged by Company (5%) (RM) | Interest Income Deemed To Be Received Based On Formula (3%) (RM) |
|------------------------------|---------------------------------|--|---|
| Mar | 100,000 | $100,000 \times 5\% \times 1/12 = 417$ | $100,000 \times 3\% \times 1/12 = 250$ |
| Apr | 90,000 (100,000 - 10,000) | $90,000 \times 5\% \times 1/12 = 375$ | $90,000 \times 3\% \times 1/12 = 225$ |
| May | 90,000 | $90,000 \times 5\% \times 1/12 = 375$ | $90,000 \times 3\% \times 1/12 = 225$ |
| Jun | 90,000 | $90,000 \times 5\% \times 1/12 = 375$ | $90,000 \times 3\% \times 1/12 = 225$ |
| Jul | 90,000 | $90,000 \times 5\% \times 1/12 = 375$ | $90,000 \times 3\% \times 1/12 = 225$ |
| Aug | 90,000 | $90,000 \times 5\% \times 1/12 = 375$ | $90,000 \times 3\% \times 1/12 = 225$ |
| Sept | 120,000 (90,000 + 30,000) | $120,000 \times 5\% \times 1/12 = 500$ | $120,000 \times 3\% \times 1/12 = 300$ |
| Oct | 120,000 | $120,000 \times 5\% \times 1/12 = 500$ | $120,000 \times 3\% \times 1/12 = 300$ |
| Nov | 120,000 | $120,000 \times 5\% \times 1/12 = 500$ | $120,000 \times 3\% \times 1/12 = 300$ |
| Dec | 120,000 | $120,000 \times 5\% \times 1/12 = 500$ | $120,000 \times 3\% \times 1/12 = 300$ |
| Total Interest Income | | 4,292 | 2,575 |

Since the interest charged by the company is higher than that computed by using the prescribed formula, then the amount of interest RM4,292 charged and payable by Director C to the company is the interest income of the company for the year of assessment 2014. Interest income deemed to be received by S

Sdn Bhd using the prescribed formula in subsection 140B(2) of the ITA amounting to RM2,575 is disregarded.

ii) The interest rate charged by the company is lower than the ALR published by BNM

If the amount of interest charged by a company is less than the amount of interest deemed to be received by the company in accordance with the formula under subsection 140B(2) of the ITA, then the interest charged by the company will be disregarded. Interest deemed to be received computed according to the formula under subsection 140B(2) of the ITA applies and the amount will be the interest income of company and assessed under paragraph 4(c) of the ITA.

Example 17

Director D who is also a shareholder of T Sdn Bhd has obtained a loan of RM100,000 from the company in February 2014 with an interest rate of 1%, which is lower than the ALR of 3% in the year of assessment 2014 (assumption only).

In July 2014, Director D made payments totaling RM20,000. In November 2014, T Sdn Bhd made further advances of RM40,000 to Director D. The computation of interest income of the company for the year of assessment 2014 is as follows -

Year of Assessment 2014

| Month | Loan Balance (RM) | Interest Charge By The Company (RM) (1%) | Interest Income Deemed To Be Received Based On formula (RM) (3%) |
|--------------|---------------------------------|---|---|
| Feb | 100,000 | $100,000 \times 1\% \times 1/12 = 83$ | $100,000 \times 3\% \times 1/12 = 250$ |
| Mar | 100,000 | $100,000 \times 1\% \times 1/12 = 83$ | $100,000 \times 3\% \times 1/12 = 250$ |
| Apr | 100,000 | $100,000 \times 1\% \times 1/12 = 83$ | $100,000 \times 3\% \times 1/12 = 250$ |
| May | 100,000 | $100,000 \times 1\% \times 1/12 = 83$ | $100,000 \times 3\% \times 1/12 = 250$ |
| Jun | 100,000 | $100,000 \times 1\% \times 1/12 = 83$ | $100,000 \times 3\% \times 1/12 = 250$ |
| Jul | 80,000 (100,000 - 20,000) | $80,000 \times 1\% \times 1/12 = 67$ | $80,000 \times 3\% \times 1/12 = 200$ |
| Aug | 80,000 | $80,000 \times 1\% \times 1/12 = 67$ | $80,000 \times 3\% \times 1/12 = 200$ |

| | | | |
|------------------------------|---------------------------------|--|--|
| Sept | 80,000 | $80,000 \times 1\% \times 1/12 = 67$ | $80,000 \times 3\% \times 1/12 = 200$ |
| Oct | 80,000 | $80,000 \times 1\% \times 1/12 = 67$ | $80,000 \times 3\% \times 1/12 = 200$ |
| Nov | 120,000 (80,000 + 40,000) | $120,000 \times 1\% \times 1/12 = 100$ | $120,000 \times 3\% \times 1/12 = 300$ |
| Dec | 120,000 | $120,000 \times 1\% \times 1/12 = 100$ | $120,000 \times 3\% \times 1/12 = 300$ |
| Total Interest Income | | 883 | 2,650 |

Since the amount of interest RM883 charged by the company is lower than the amount of interest income that is deemed to be received by the company based on formula in subsection 140B(2) of the ITA, then the amount RM883 is disregarded. The amount of RM2,650 is the interest income deemed to be received by the company for the year of assessment 2014 and will be assessed under paragraph 4(c) of the ITA.

6. Loan Or Advances By A Dormant Company To Directors Of The Company

If a dormant company (inactive) made loans or advances to directors of a company, then the company will be deemed to commence operations as provided under subsection 21A (8) of the ITA. Loans or advances to directors are subject to section 140B of the ITA and the statutory income from the interest income deemed to be received by the company will be assessed under paragraph 4(c) of the ITA.

Example 18

A company has been incorporated with a paid up capital of RM150,000 on 1.5.2012. The Company does not intend to start its business for several years and on 1.3.2014, the company made interest-free loans amounting to RM100,000 to Director E. No repayments are made by the director as at 31.12.2014.

Although the company is dormant, but with the loan made to Director E, the company is deemed to have commenced operation in accordance with subsection 21A(8) of the ITA. Loan made to Director E is subject to section 140B of the ITA and the interest income deemed to be received is to be assessed under paragraph 4(c) of the ITA.

Interest income deemed to be received by the company for the year of assessment 2014 (assuming ALR is 3%) is computed as follows-

| Year Of Assessment 2014 | Loan Balance (RM) | Interest Income Deemed To Be Received (RM) |
|------------------------------------|------------------------------|---|
| Mar – Dec | 100,000 @ 3% x 10/12 | 2,500 |

7. Other Provisions Related To Loan Or Advances To Directors

7.1. Subsection 29(3) of the ITA

For loans or advances from internal funds provided by a company to directors, the provision of subsection 29(3) of the ITA shall not apply even though the loans or advances made involved related parties as defined under subsection 29(3) of the ITA because section 140B of the ITA is a special provision to compute interest income deemed to be received by a company in the basis period for a year of assessment for loans or advances made to directors.

7.2. Subsection 140A(2) of the ITA

For loans or advances to directors who are also shareholders in accordance with subsection 75A(2) of the ITA, the provision of subsection 140A(2) of the ITA is not applicable because the benefits received by the director from the loans or advances have been taxed on the company in accordance with section 140B of the ITA. Companies need not provide any relevant documentation for the purposes of subsection 140A(2) of the ITA.

Example 20

Mr. F, a director of RYZ Sdn Bhd has obtained a loan from the company that is financed from internal funds. Mr. F's shareholding in RYZ Sdn Bhd is 46%. The loan made is subject to section 140B of the ITA. Therefore subsection 140A(2) of the ITA is not applicable to the company.

7.3. Moneylender's Act 1951 (MLA)

The introduction of section 140B of the ITA does not preclude or restrict the business and transactions of a lender as provided under the MLA. Section 140B of the ITA is a provision to determine interest income deemed to be received by a company for loans or advances made to directors which are interest-free or with interest rate lower than arm's length rate.