



**INLAND REVENUE BOARD MALAYSIA**

**PROFESSIONAL INDEMNITY  
INSURANCE**

**PUBLIC RULING NO. 1/2019**

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<b>CONTENTS</b>	<b>Page</b>
1. Objective	1
2. Relevant Provisions of the Law	1
3. Interpretation	1
4. Introduction	1
5. Prerequisite for a Professional to Carry On or to Practise a Profession	1
6. Requirement to purchase Professional Indemnity Insurance	2
7. Tax Treatment on Professional Indemnity Insurance Premium	3
8. Tax Treatment on Insurance Proceeds and Compensation	5
9. Updates and Amendments	8
10. Disclaimer	9

### **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 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 –

- (i) the deductibility of premium paid for a professional indemnity insurance (PII) policy; and
- (ii) the tax treatment on insurance proceeds received and compensation paid in relation to a PII policy.

## 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) relevant to this PR are sections 22 and subsection 33(1).

## 3. Interpretation

The words used in this PR have the following meaning:

- 3.1 "Person" includes a company, a body of persons, a limited liability partnership and a corporation sole.
- 3.2 "Profession" includes the profession of lawyers, accountants, architects, doctors, pharmacists, engineers, surveyors or any other profession where the status of the profession is recognised by a written law or statute in Malaysia.
- 3.3 "Professional" means a person who belongs to a profession and is a member of a professional body or registered with a body which governs the profession.

## 4. Introduction

PII is an insurance policy for a professional which will protect him from liability or the risk of being sued for alleged negligence, error or breach of duty when practising his profession or carrying on his business. The insurance may cover the cost of defending the suit and the cost of compensation.

## 5. Prerequisite for a Professional to Carry On or to Practise a Profession

- 5.1 If a professional is registered with a professional body outside Malaysia, the professional body must be recognised by written law or statute in Malaysia.

### Example 1

Matthew is a pharmacist registered with a professional body in Ireland, the Pharmaceutical Society of Ireland (PSI). PSI is a professional body recognized by the Malaysian Pharmaceutical Board (MPB) under the Pharmacy Registration Act 1951.

Matthew practices his profession in Malaysia and serves in WellHealth Pharmacy. Matthew falls within the meaning of a professional under this PR.

- 5.2 Certain professions require a person to be a member of the professional body which represents the profession to enable the person to practise and maintain his profession. Examples of these professions are accountants, lawyers and engineers.

### Example 2

Nathan is a lawyer who is a member of the Malaysian Bar Council. He practises his profession through a legal firm, Nathan, Ali & Co. Nathan falls within the meaning of a professional under this PR.

- 5.3 However, there are some professions which require a person to be registered with a body corporate which governs the profession and is recognized by the Malaysian Government for purposes of practising and maintaining his profession. The person is not required to be a member of the relevant professional body. Examples of these professions are medical doctors, dentists and architects.

### Example 3

Dr. Maira is a doctor who is registered with the Malaysian Medical Council (MMC) which is a body corporate incorporated under the Ministry of Health. She is not a member of the Malaysian Medical Association (MMA), the professional body which represents her profession. In the year 2017, she practises her profession as a doctor in her own clinic. Dr. Maira falls within the meaning of a professional under this PR.

## 6. Requirement to Purchase Professional Indemnity Insurance

- 6.1 A professional, due to the nature of his work, may be exposed to the likelihood of lawsuits for professional negligence for what he had done or what he had said in the course of carrying out his work.

#### **Example 4**

Voon, an accountant had given advice on a financial transaction to a client who subsequently lost his money after acting on that advice. The client may sue Voon for the money lost in the transaction and may claim compensation from him because he had given advice without due care.

- 6.2 Some professions require their members to purchase PII as provided under the profession's by-laws or rules. Examples of these professions are medical doctors, accountants and lawyers.
- 6.3 Whereas in other professions PII is generally purchased on grounds of prudence and not because it is a requirement under the profession's by-laws or rules. Examples of these professions are engineers and architects.

### **7. Tax Treatment on Professional Indemnity Insurance Premium**

- 7.1 A practising professional is allowed a tax deduction for PII premium if the professional carries on a business related to his profession.

#### **Example 5**

Dr. Steven, a partner in a business of dental practice, operates from a clinic together with his partners. He is registered with the Malaysian Dental Council (MDC) and holds an Annual Practising Certificate. In the year 2017, he purchased a PII policy to cover himself in the event of lawsuits arising from the carrying on of his profession as a dentist.

The premium paid for PII qualifies as a deduction against his gross income from the partnership business since Dr. Steven carries on the business of his profession.

#### **Example 6**

Ir. Lee is a sole-proprietor of an engineering business, Excellent Engineering Consultancy. In the year 2017, he purchased a PII policy and paid a premium totalling RM10,000. He is a member of The Institution of Engineers Malaysia (IEM). The statute or by-laws of IEM does not require its members to purchase a PII policy in order to practise as a professional.

For the year of assessment 2017, the PII premium paid is allowable as a deduction against the gross income from his business because he carries on the business of his profession.

- 7.2 In the case of a professional who is not practising his profession but carries on other business or a professional who is practising his profession but under

employment, the premium paid for PII is not allowed as a deduction against the gross income from that business or employment.

#### **Example 7**

Dr. Aidil is a full-time surgeon employed by a government hospital. He is registered with the MMC and is also a member of the MMA. In the year 2017, he purchased a PII policy and paid a premium of RM2,400.

The PII premium paid for the year 2017 is not eligible for deduction against Dr. Aidil's employment income although he is practising his profession. This is because he is not carrying on a business related to his profession.

#### **Example 8**

Felicia is an accountant who does not practise as an accountant but instead is carrying on a full-time direct-selling business. Felicia purchases a PII policy to maintain her professional status as an accountant.

As Felicia is not carrying a business related to her profession as an accountant, she does not satisfy the requirement needed for deduction of PII premium. Thus, the PII premium paid is not allowed as a deduction from the gross income of the direct-selling business.

### **7.3 PII premium incurred by a company**

Where a particular professional body allows its members to practise the profession in the form of a company and PII is purchased by the company, the PII premium paid by the company is allowed as a deduction against the gross income of the company if the company carries on a business related to that profession.

#### **Example 9**

Senibina Bumi Landskap Sdn Bhd (SBLSB) is a consulting architecture company which provides architectural consultancy and services. The company purchased a PII policy to cover the cost of compensation and defending lawsuits in relation to the construction project of a hotel in Putrajaya.

Since SBLSB which carries on an architectural business purchased a PII policy related to the architect profession, the PII premium paid is allowed as a deduction against the gross income of the company's business

### **7.4 PII premium for a locum**

Where a professional who carries out his duty as a locum purchases a PII, the PII premium paid is not allowed as a deduction from his income as a

locum or any other income. For the purposes of this PR, “locum” means a person who temporarily fulfills the duty of another person carrying out the same profession. For example, a locum doctor may stand in for another doctor in a hospital or a clinic. Income from a locum is taxed as income from an employment.

### **Example 10**

Dr. Merican who carries on a business as a doctor since the year 2015 purchased a PII policy to cover himself against lawsuits in the course of carrying out his profession as a doctor. He paid PII premium amounting to RM2,500 each year since 2015. From January 2017, Dr. Merican also carries out duty as a locum in another private clinic and purchased an additional PII policy to provide protection for his duty as a locum doctor. The PII premium paid in respect of this PII policy is RM1,000 per year.

Dr. Merican is entitled to a deduction of the PII premium amounting to RM2,500 paid in relation to carrying on the business of his profession. However the PII premium amounting to RM1,000 paid in relation to his duty as a locum is not allowed a deduction against his income as a locum or the business income since it is not made in the course of carrying on a business related to his profession.

## **8. Tax Treatment on Insurance Proceeds and Compensation**

- 8.1 Where a professional has been allowed a deduction for the PII premium paid, any proceeds received in connection with the PII would be subject to tax. The proceeds are taxed under subsection 22(2)(a)(ii) of the ITA.
- 8.2 Compensation to a claimant can be made in the following manner –
- (i) the insurance company pays the proceeds to the professional and the professional pays that amount to the claimant; or
  - (ii) the insurance company pays directly to the claimant.

The compensation paid in both of the above manner is allowed a deduction under subsection 33(1) of the ITA as it is incurred in the ordinary course of the business of a professional who is constantly exposed to the risk of being sued by his clients for negligence, error or breach of duty.

### **Example 11**

Mohd Fahrin is an architect who practises his profession in the architectural consulting firm, Arkitek Asyraf & Goh (AAG). AAG purchased a PII policy for him to cover himself against the risk of being sued. In the year 2017, a



dissatisfied client sued AAG for damages to the bungalow caused by faulty design by Mohd Fahrin. The insurance company concerned made a payment of RM200,000 to AAG and AAG then paid the amount as compensation to his client (the claimant).

The proceeds received by AAG totalling RM200,000 would be subject to tax, whilst the amount paid as compensation to the claimant is allowed as a deduction under subsection 33(1) of the ITA against the gross income of the AAG's business.

### Example 12

Same facts as in **Example 11** except that the insurance company made the compensation payment of RM200,000 directly to the claimant.

The compensation amounting to RM200,000 paid directly to the claimant is deemed received in the books of the architectural firm and is subject to tax. The amount of proceeds paid as compensation to the claimant is deemed paid out from the firm's accounts and is allowable as a deduction under subsection 33(1) of the ITA against the gross income of the AAG's business.

- 8.3 A professional would bear the shortfall of compensation if the amount of compensation claimed by the claimant exceeds the amount of proceeds received from the insurer. The amount of shortfall is allowed as a tax deduction under subsection 33(1) of the ITA.

### Example 13

Bernard, the sole-proprietor of a legal firm received proceeds amounting to RM200,000 from an insurance company and this amount could not cover the compensation of RM250,000 to be paid to a customer who had made a claim against him. Therefore, Bernard had to bear on his own RM50,000 to cover the shortfall of compensation payment to the claimant.

Proceeds amounting to RM200,000 would be subject to tax. When the proceeds are paid out as compensation to his client, the amount is allowed as a tax deduction. The compensation totalling RM50,000 incurred by Bernard is also allowable as a deduction from the gross income of his business under subsection 33(1) of the ITA.

- 8.4 Any proceeds received as mentioned in paragraph 8.1 of this PR is not restricted to any expenditure incurred to pay compensation to the claimant. This means that the full amount of the proceeds will be taxed even though the payment of compensation is less than the amount of the proceeds received.

#### Example 14

Mr. Jeremy is an engineer who practices his profession in an engineering company, Premium Engineering Consultancy (PEC). PEC purchased a PII policy for him to cover himself in the event of lawsuits arising from the carrying on of his profession as an engineer.

On 21.11.2018, the insurance company paid the proceeds of RM350,000 to PEC on negligence of advisory services conducted by Mr. Jeremy and PEC then paid RM250,000 as compensation to its client (the claimant).

The proceeds amounting to RM350,000 will be subject to tax in full even though the payment of compensation to the claimant is less than the proceeds received. When the amount of compensation totalling RM250,000 are paid to its client, the amount is allowed as a deduction from the gross income of PEC's business under subsection 33(1) of the ITA.

- 8.5 In a case where a professional chooses not to claim a deduction for the IIP premium expense under subsection 33(1) of the ITA, any proceeds received in connection with the IIP shall be taxed as a gross income of the chargeable professional under subparagraph 22(2)(a)(ii) of the ITA.

#### Example 15

Delisha, the sole-proprietor of a Megastore Pharmaceuticals [MP] business is a registered pharmacist with MPB. She paid PII premium amounting to RM1,200 each year since 2016. However, Delisha did not claim the premium expenses as a deduction under subsection 33(1) of the ITA against the gross income of MP's business.

In 2018, a dissatisfied client (the claimant) sued her for negligence in giving medication instructions. The dosage of the controlled drugs is one tablet daily for five days but Delisha instructed the claimant to take five tablets daily for five days. The insurance company paid the proceeds amounting to RM75,000 to Delisha and she then paid the amount as compensation to the claimant.

Although, Delisha chose not to claim the PII premium as an expense under subsection 33 (1) of the ITA, the proceeds received amounting to RM75,000 would be subject to tax. Meanwhile, the amount of proceeds paid as compensation to the claimant is allowed as a deduction under subsection 33 (1) of the ITA against the gross income of the MP's business.

**9. Updates and Amendments**

	<b>Amendments</b>	
This PR replaces the PR No. 8/2017 dated 19.12.2017.	The contents of this PR have been ammended as follows :	
	Paragraph	
	5.1	Paragraph 5.1 is an additional description and a new example 1.
	5.2	Paragraph 5.1 of the PR No. 8/2017 is amended to become paragraph 5.2 and example 1 is amended to become example 2.
	5.3	Paragraph 5.2 of the PR No. 8/2017 is amended to become paragraph 5.3 and example 2 is amended to become example 3.
	6.1	Example 3 in PR No. 8/2017 is amended to become Example 4.
	7.1	Example 4 and Example 5 in PR No. 8/2017 respectively amended to become Example 5 and Example 6.
	7.2	Example 6 and Example 7 in PR No. 8/2017 respectively amended to become Example 7 and Example 8.
	7.3	Example 8 in PR No. 8/2017 is amended to become Example 9.
	7.4	Example 9 in PR No. 8/2017 is amended to become Example 10.
	8.2	Example 10 and Example 11 in PR No. 8/2017 respectively amended to become Example 11 and Example 12.
	8.3	Example 12 in PR No. 8/2017 is amended to become Example 13.
	8.4	New paragraph and new example 14.
8.5	New paragraph and new example 15.	



**10. Disclaimer**

The examples in this PR are for illustration purposes only and are not exhaustive.

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