INLAND REVENUE BOARD OF MALAYSIA

INCOME FROM LETTING OF REAL PROPERTY

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DIRECTOR GENERAL'S PUBLIC RULING

Section 138A of the Income Tax Act 1967 [ITA] provides that the Director General of Inland Revenue 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 of Inland Revenue may withdraw 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

This Public Ruling (PR) explains:

(a) Letting of real property as a business source under paragraph 4(*a*) of the Income Tax Act 1967 (ITA); and

(b) Letting of real property as a non-business source under paragraph 4(*d*) of the ITA.

2. Relevant Provisions of the Law

The provisions of the ITA related to this PR are paragraphs 4(*a*), 4(*d*), 24(1)(b), 24(1)(c) and subsection 24(1A), 33(1) and 39(1).

3. Interpretation

The words used in this PR have the following meaning:

3.1 "Arm's length basis" refers to the circumstances, decisions or outcomes that would have been arrived at if unrelated or unconnected persons were to deal with each other wholly independently and out of reach of personal influence.

3.2 "Real property" includes any land and any interest, option or other right in or over such land and includes any building on land.

3.3 "Person" includes a company, a co-operative society, a partnership, a club, an association, a Hindu joint family, a trust, an estate under administration and an individual, but excludes a unit trust.

3.4 "Letting of real property" means granting the use of a real property or occupation of a real property under an agreement or a term of contract and includes the letting out of part of the real property that is owned or rented.

3.5 "Management corporation" means a management corporation established under the Strata Titles Act 1985 (Act 318), the Land (Subsidiary Title) Enactment 1972 (Sabah No. 9 of 1972) or the Strata Titles Ordinance 1995 (Laws of Sarawak, Chapter 18).

3.6 “Rent” or "rental income" or “income from letting” includes any amount received for the use or occupation of any real property or part thereof including premiums and other receipt in connection with the use or occupation of the real property.

3.7 “Related company” has the same meaning as provided in subsection 2(4) of the ITA.

4. Letting of Real Property as a Business Source

4.1 Letting of real property is deemed as a business source and the income received from it is charged to tax under paragraph 4(*a*) of the ITA if maintenance or support services are provided in relation to the real property.

4.2 Maintenance or support services should be comprehensively and actively provided.

4.2.1 Maintenance or support services comprehensively provided means services which include:

(a) doing generally all things necessary (eg. cleaning services or repairs) for the maintenance and management of the real property such as the structural elements of the building, stairways, fire escapes, entrances and exits, lobbies, corridors, lifts/escalators, compounds, drains, water tanks, sewers, pipes, wires, cables or other fixtures and fittings; and

(b) doing generally all things necessary for the maintenance and management of the exterior parts of the real property such as playing fields, recreational areas, driveways, car parks, open spaces, landscape areas, walls and fences, exterior lighting or other external fixtures and fittings.

If a person only provides security services or other facilities, that person is not providing maintenance services or support services comprehensively.

4.2.2 Services actively provided means the person who owns or lets out the real property:

(a) provides himself; or

(b) hires another person or another firm to provide

the maintenance services or support services as mentioned under paragraph 4.2.1 of this PR.

Example 1

Suai Sdn Bhd owns three blocks of condominium consisting of 324 units and lets out those units to tenants. Suai Sdn Bhd provides maintenance services of lift, cleaning services, security services, centralized air conditioner and maintenance services of playing fields and car parks.

The letting of the condominium units is treated as a business source of Suai Sdn Bhd since maintenance services and support services are comprehensively and actively provided by Suai Sdn Bhd.

Example 2

Wahida owns a 4-storey building consisting of 32 units that can be used as offices and shop lots. All the units are let out to several tenants. Wahida hires Ali Enterprise to provide maintenance services of the structure of the building, maintenance of lift and cleaning services of the building and area outside the building.

The letting of the units in the building is treated as a business source of Wahida since maintenance services and support services are comprehensively and actively provided by Wahida.

Example 3

Yes Property Sdn Bhd rents one block of office building consisting of 42 units from Zura Sdn Bhd. All the units are let out to a few tenants. Yes Property Sdn Bhd provides cleaning services in and outside of the building area, centralized air conditioner, maintenance of car park and security services.

The letting of the office units is deemed to be a business source of Yes Property Sdn Bhd since maintenance services and support services are comprehensively and actively provided by Yes Property Sdn Bhd.

4.3 As long as maintenance services or support services are comprehensively and actively provided in relation to the real property which is let out, the letting is a business source under paragraph 4(*a*) of the ITA even though the letting is between related parties. However, if rental charged to the tenant is not at an arm's length basis, the Inland Revenue Board Malaysia would adjust the rental payment accordingly.

For the purpose of this PR, "related parties" in relation to:

(a) individuals, mean both individuals are related;

(b) companies, mean both companies are related companies;

(c) a company and an individual, mean one of the parties is in a position to influence or be influenced by the other party, or to control or be controlled by the other party.

4.4 Special treatment for letting of a building to an approved Multimedia Super Corridor (MSC) status company

Under the Income Tax (Industrial Building Allowance) (Approved Multimedia Super Corridor (MSC) Status Company) Rules 2006 [P.U.(A) 202/2006], effective year of assesment (YA) 2006, the letting of building in the Cyberjaya Flagship Zone to an approved MSC status company is regarded as carrying on a business and the income received from it is charged to tax under paragraph 4(*a*) of the ITA.

The building let out:

- has to be a new building that provides a world-class physical and information infrastructure as determined by the Multimedia Development Corporation Sdn Bhd;
- must not have been occupied by any company prior to the YA 2006; and
- does not include building for the purpose of living accommodation.

5. **Letting of Real Property as a Non-Business Source**

5.1 The letting of real property is treated as a non-business source and income received from it is charged to tax under paragraph 4(*d*) of the ITA if a person lets out the real property without providing maintenance services or support services comprehensively and actively.

Example 4

Unggas Property Sdn Bhd lets out one block of office building to a company. Unggas Property Sdn Bhd only provides security services.

The letting of the office building is treated as non-business source since Unggas Property only provides security services. Unggas Property Sdn Bhd does not provide maintenance services or support services comprehensively.

Example 5

Azran Sdn Bhd lets out a 5-storey building to Aloy Sdn Bhd without providing any maintenance services or support services.

The letting of the building is a non-business source since there are no maintenance services or support services provided by Azran Sdn Bhd. Income received from the letting is charged to tax as rental income under paragraph 4(*d*) of the ITA.

Example 6

Facts are the same as in example 3 but maintenance services and support services are provided by Zura Property Sdn Bhd.

The letting of the office units is treated as a non-business source of Yes Property Sdn Bhd since maintenance services and support services are not provided by Yes Property Sdn Bhd but are provided by Zura Property Sdn Bhd which is hired by Zura Sdn Bhd.

5.2 The letting of real property is also treated as a non-business source if a person lets out the real property and maintenance services or support services are passively derived from the ownership of the real property. Income received from the letting of the real property is charged to tax as rental income under paragraph 4(*d*) of the ITA.

Example 7

Azrie owns 2 units of apartment and lets out those units to 2 tenants. The tenants are entitled to use the swimming pool, tennis court and other facilities that are provided in the apartment. All the facilities are provided and maintained by the management corporation of the apartment. Azrie only pays maintenance fees to the management corporation of the apartment.

Services enjoyed by the tenants are merely an extension of Azrie's right as proprietor of the apartment units and are not actively provided by Azrie. Therefore, the letting of the apartment units is a non-business source and the income received from it is charged to tax as rental income under paragraph 4(*d*) of the ITA.

6. Commencement Date of Letting of Real Property

6.1 The date of commencement of letting of real property treated as a source of rental income under paragraph 4(*d*) of the ITA is on the date the real property is rented out for the first time.

Example 8

Nora buys one unit of apartment on 1.10.2017. She renovates and advertises the letting of the apartment on 1.1.2018. The apartment is only let out on 1.7.2018.

The letting of the apartment commences on 1.7.2018 i.e on the date it is rented out for the first time.

6.2 The date of commencement of letting of real property treated as a business source under paragraph 4(*a*) of the ITA is on the date the real property is made available for letting. A real property is made available for letting when the real property is ready to be occupied by tenants and steps to let out the real property have been taken such as advertising the real property for letting or appointing a real property agent to facilitate the letting.

Example 9

Muhibbah Sdn Bhd purchases a 12-storey office building on 1.1.2017. The company advertises the letting of that building on 1.4.2017. The Company provides maintenance services of lift, cleaning services of the building and area outside the building, maintenance services of car park for that building and centralized air conditioner. The building is made available for letting on 1.6.2017 after renovation is completed. The building is only let out on 1.8.2017. The company closes its accounts on 31 December every year.

The letting of the building commences on 1.6.2017 i.e on the date the building is made available for letting.

Example 10

Facts are the same as in Example 9 but the building is only let out on 1.1.2018.

The letting of the building commences on 1.6.2017 that is on the date the building is available for letting. Therefore expenses incurred in the production of rental income for the YA 2017 are allowable and can be carried forward to the YA 2018 (assuming that the company only has this rental business income). However advertisement expenses incurred on 1.4.2017 are not allowable since the expenses incurred are initial expenses to obtain the first tenant.

Example 11

Syazril Property Sdn Bhd owns a complex consisting of an office building in Block A and a shopping centre in Block B. The company provides maintenance services and support services comprehensively and actively in relation to the complex. The company advertises the letting of that complex on 1.6.2017. The office building in Block A is made available for letting and is let out on the same date i.e 1.7.2017. Whereas the shopping centre in Block B is made available for letting on 1.1.2018 but is only let out on 1.2.2018. The company closes its accounts on 31 December every year.

The letting of the office building commences on 1.7.2017. Whereas the letting of the shopping complex commences on 1.1.2018 i.e on the date it is made available for letting.

Example 12

Kengo Sdn Bhd purchases a 10-storey office building in Kuala Lumpur, a shopping complex in Johor Bahru and 5 units of shop house in Kota Bharu in the year 2017. Both buildings in Kuala Lumpur and Johor Bahru are let out and maintenance services and support services are comprehensively and actively provided in relation to those buildings. Whereas the shop houses are let out without maintenance services and support services. The date of advertisement, the date the real properties are made available for letting and the real properties are let out are as follows:

Real Property	Advertisement Date	Date Available for Letting	Date of Letting
Building in Kuala Lumpur	1.6.2017	1.9.2017	1.12.2017
Building in Johor Bahru	1.8.2017	1.11.2017	1.1.2018
Shop houses in Kota Bharu	1.9.2017	1.11.2017	1.2.2018

The commencement date of letting of the real properties are as follows:

Real Properties	Date of Commencement of Letting
Rental business [paragraph 4(*a*)]	
Building in Kuala Lumpur	1.9.2017
Building in Johor Bahru	1.11.2017
Rental [paragraph 4(*d*)]	
Shop houses in Kota Bharu	1.2.2018

7. **Real Properties Grouped as a Single Source**

7.1 Several real properties which are let out can be grouped as one source whether as a business source under paragraph 4(*a*) of the ITA or a non-business source under paragraph 4(*d*) of the ITA. If a person lets out several real properties in a YA and the letting of -

(a) all real properties is a business source, all the real properties can be grouped as one business source under paragraph 4(*a*) of the ITA.

(b) all real properties is a non-business source, all the real properties can be grouped as one non-business source under paragraph 4(*d*) of the ITA.

(c) some of the real properties is a business source and some is a non-business source, income from both sources shall be assessed separately. The income from the business source and the non-business source is assessed under paragraphs 4(*a*) and 4(*d*) of the ITA respectively.

Example 13

AJ Sdn Bhd owns a 4-storey building in Damansara and a 6-storey building in Bangsar. Both buildings are let out since 2008 and the letting of the buildings is treated as a business source under paragraph 4(*a*) of the ITA. The gross income, allowable expenses and capital allowances on the furniture in each building for the YA 2016 are as follows:

Real Property	Gross Income RM	Allowable Expenses RM	Capital Allowances (Furniture) RM
Building in Damansara	60,000	14,000	7,000
Building in Bangsar	10,000	12,000	3,000
Total	70,000	26,000	10,000

The letting of both real properties is a business source. Therefore, both real properties can be grouped as one business source under paragraph 4(*a*) of the ITA. The statutory income of AJ Sdn Bhd from the business of letting of real property for the YA 2016 is calculated as follows:

	RM
Gross income from rental	70,000
Less: Allowable expenses	26,000
Adjusted income	44,000
Less: Capital allowances (furniture)	10,000
Statutory income from rental	34,000

Example 14

Margaret owns several real properties which are let out since 2008 and the letting of the real properties is a non-business source under paragraph 4(*d*) of the ITA. The gross income and allowable expenses for each real property for the YA 2017 are as follows:

Real Property	Gross Income RM	Allowable Expenses RM
Terrace house	12,000	3,000
Apartment	9,000	11,000
Shop house	24,000	8,000
Vacant land	1,500	1,800
Total	46,500	23,800

Margaret's statutory income from the letting of real property for the YA 2017 is calculated as follows:

	RM
Gross income from rental	46,500
Less: Allowable expenses	23,800
Statutory income from rental	22,700

Example 15

Theodore Lim buys an office building and a business building in Taman Anggerik, Ampang in August 2016. The purchases of both buildings are financed by a bank loan. The office building was made available for rent and rented out on 1.1.2017. The business building was made available for rent on 1.1.2018 and only rented out on 1.2.2018. Income from the letting of both buildings is assessed as a business source under paragraph 4(*a*) of the ITA. The gross income and interest expense on loan for each building for the years of assessment 2017 and 2018 are as follows:

Real Property	Gross Income RM		Interest Expense RM	
	YA 2017	**YA 2018**	**YA 2017**	**YA 2018**
Office building	120,000	120,000	45,000	40,000
Business building	-	165,000	55,000	50,000

In the YA 2017, the business building has not commenced as a source because no income has been generated yet. As such, the business building and office building cannot be aggregated as one source. Interest expense in relation to the business building amounting to RM55,000 is not allowed a deduction against the gross income from the letting of office building.

The statutory income from rent for the YA 2017 is computed as follows:

	RM
Gross income from rental [paragraph 4(*a*)]	120,000
Less: Interest expense	45,000
Statutory income from rental	75,000

Note: If rental income from the office building and business building are assessed as a non-business source under paragraph 4(*d*) of the ITA, the same tax treatment applies.

In the YA 2018, the business building can be grouped with the office building as one source as the business building constitutes a source once it has generated income. Although the business building is only rented out on 1.2.2018, the whole interest expense amounting to RM50,000 is allowed a deduction since the rental business source for the YA 2018 exists from 1.1.2018.

The statutory income from rent for the YA 2018 is computed as follows:

	RM
Gross income from rental [paragraph 4(*a*)]	285,000
Less: Interest expense	90,000
Statutory income from rental	195,000

Note: If rental income from office building and business building is assessed as a non-business source under paragraph 4(*d*) of the ITA, interest expenses in respect of the business building has to be adjusted according to the period the building is let out. Therefore interest expense in respect of the period from 1.1.2018 to 31.1.2018 is not allowable as the date of commencement of the business building is 1.2.2018.

Example 16

Facts are the same as in Example 13 with an additional information i.e AJ Sdn Bhd owns and lets out a residential house and one unit of apartment. The letting of the residential house and the apartment unit is a non-business source since maintenance services or support services are not provided. The company is not an investment holding company.

The gross income, allowable expenses and capital allowances on the furniture in each building for the YA 2016 are as follows:

Real Property – Paragraph 4(*a*) Source	**Gross Income RM**	**Allowable Expenses RM**	**Capital Allowances (Furniture) RM**
Building in Damansara	60,000	14,000	7,000
Building in Bangsar	10,000	12,000	3,000
Total	70,000	26,000	10,000
Real Property – Paragraph 4(*d*) Source	**Gross Income RM**	**Allowable Expenses RM**	**Capital Allowances RM**
Residential house	8,000	11,000	-
Apartment	6,000	4,000	-
Total	14,000	15,000	-

The letting of buildings in Damansara and Bangsar is a business source. Therefore, those buildings can be grouped as one business source under paragraph 4(*a*) of the ITA. Whereas the letting of residential house and apartment is a non-business source and can be grouped as one non-business source under paragraph 4(*d*) of the ITA.

The total income of AJ Sdn Bhd for the YA 2016 is computed as follows:

		RM
(i)	Statutory income from rental - paragraph 4(*a*)	
	[70,000 - 26,000 - 10,000]	34,000
(ii)	Statutory income from rental - paragraph 4(*d*)	
	[14,000 - 15,000]	Nil
	Aggregate income/Total income	34,000

The adjusted loss from non-business source amounting to RM1,000 cannot be deducted against statutory income from business of letting and is not allowed to be carried forward to subsequent years of assessment.

7.2 If a person has a business source of letting of real property under paragraph 4(*a*) of the ITA and a business source from other businesses in the same YA, the business source of letting of real property has to be separated from the other business sources.

Example 17

Syarikat MJ Sdn Bhd (SMSB) is carrying on a business of hardware wholesaler. SMSB owns a 4-storey building which is let out and provides maintenance services and support services comprehensively and actively. SMSB also owns a terrace house which is let out without providing maintenance services and support services. Income from letting of the 4-storey building qualifies to be assessed as a business source [paragraph 4(a) of the ITA] whereas rental income from the terrace house is assessed as a non-business source [paragraph 4(*d*) of the ITA] for the YA 2017.

The gross income, allowable expenses and capital allowances on plant and machinery for each source of income of SMSB for the YA 2017 are as follows:

Source of Income	Adjusted income RM	Adjusted Loss RM	Capital Allowances (Plant and Machinery) RM
Business of wholesale	100,000	-	15,000
Letting of 4-storey building [paragraph 4(*a*) of the ITA]	-	10,000	5,000
Letting of terrace house [paragraph 4(*d*) of the ITA]	-	3,000	-

The total income of SMSB for the YA 2017 is computed as follows:

		RM	RM
(i)	Business of wholesale [paragraph 4(*a*) of the ITA]		
	Adjusted income	100,000	
	Less: Capital allowances (plant and machinery)	15,000	
	Statutory income		85,000
(ii)	Letting of real property [paragraph 4(*a*) of the ITA]		
	Adjusted loss	(10,000)	
	Capital allowances (plant and machinery)	5,000	
	Statutory income		Nil
(iii)	Letting of real property [paragraph 4(*d*) of the ITA]		
	Adjusted loss	(3,000)	
	Statutory income		Nil
	Aggregate income		85,000
	Less: Current year loss		10,000
	Total income		75,000

Capital Allowances of RM5,000 in relation to the letting of real property under paragraph 4(*a*) of the ITA which cannot be absorbed in the YA 2017 is carried forward to subsequent years of assessment.

Adjusted loss from the letting of real property under paragraph 4(*d*) of the ITA amounting to RM3,000 cannot be deducted against the aggregate income and cannot be carried forward to subsequent years of assessment.

8. Expense Relating to Income of Letting of Real Property

8.1 An expense wholly and exclusively incurred in the production of income under subsection 33(1) of the ITA and which does not fall under subsection 39(1) of the ITA is allowed as a deduction from income of business of letting of real property charged to tax under paragraph 4(*a*) of the ITA.

8.2 Expense which is allowed a deduction from income of letting of real property charged to tax under paragraph 4(*d*) of the ITA is the direct expense that is wholly and exclusively incurred in the production of income under subsection 33(1) of the ITA. Examples of direct expenses which are deductible from gross income of letting of real property are as follows:

(a) Assessment and quit rent

Annual assessment paid to the local authority and quit rent paid to the land office.

(b) Interest on loan

Interest paid on loan taken to finance the purchase of real property which is rented out.

(c) Fire insurance premium

Fire insurance premium paid in relation to fire insurance policy taken on the real property which is rented out.

(d) Expense on rent collection

Rent collection fee and legal expense incurred to enforce rent collection.

(e) Expense on rent renewal

Expense incurred to renew tenancy or to change tenant.

(f) Expense on repair

Expense on ordinary repair to maintain the real property in its existing state.

8.3 Initial expense

Initial expense is not allowed a deduction from income of letting of real property assessed under paragraph 4(*a*) or paragraph 4(*d*) of the ITA since that expense is incurred to create a source of rental income and not incurred in the production of rental income. Examples of such expense are cost to obtain the first tenant such as advertising cost, legal cost to prepare rental agreement, stamp duty and commission for real property agent.

Example 18

Sarah Property Sdn Bhd buys an office building on 1.9.2016 to be let out. The company incurs RM600 to advertise the letting of the building on 1.1.2017 and legal cost amounting to RM1,800 paid to Reganathan & Co on 12.2.2017 for preparing rental agreement. The building is let out commencing from 1.3.2017 without providing maintenance services or support services. The letting of the office building is a non-business source and the rental income is taxable under paragraph 4(*d*) of the ITA.

The advertising cost amounting to RM600 and the legal cost of RM1,800 are not allowed a deduction from income of letting of office building for the YA 2017 as the expenses incurred are initial expenses to obtain the first tenant.

Example 19

Facts are the same as in example 18 except the building is made available for letting on 1.2.2017 and Sarah Property Sdn Bhd provides maintenance services of lift, security services, cleaning services and maintenance of centralized air conditioner. The letting of the office building is a business source and the rental income is taxable under paragraph 4(*a*) of the ITA.

The advertising cost amounting to RM600 and the legal cost of RM1,800 are not allowed a deduction from income of letting of office building for the YA 2017 as the expenses incurred are initial expenses to obtain the first tenant.

8.4 Expenses during a period the real property is not rented out

8.4.1 Expenses incurred in relation to a real property during a period it is not rented out are not allowable in calculating the adjusted income from the letting of the real property. However, if the period the real property is not rented out occurs after it has been let out and it is clear that it is ready to be let out, then expenses during that period are allowable subject to subsections 33(1) and 39(1) of the ITA.

Example 20

Farhan lets out a double-storey terrace house on 1.1.2017 for RM1,000 a month. On 1.9.2017 the tenant moves out and the house is let out to another tenant on 1.12.2017 for the same amount of rental. Assessment for a year is RM500 while quit rent is RM50 a year. The letting of the house is a non-business source and the rental income is taxable under paragraph 4(*d*) of the ITA.

The adjusted income from rent for the YA 2017 is computed as follows:

	RM	RM
Rental income (gross)		
Period of 1.1.2017 – 31.8.2017 (8 x RM1,000)	8,000	
Period of 1.12.2017 – 31.12.2017	1,000	9,000
Less:		
Assessment	500	
Quit rent	50	550
Adjusted income from rent		8,450

Although the house was not rented out from 1.9.2017 to 30.11.2017, but the house had been let out earlier. The vacant house was ready to be let out again on 1.12.2017. As such, the expenses for assessment and quit rent are allowable in full for the YA 2017 even though the house was not rented out for the period of 1.9.2017 to 30.11.2017.

8.4.2 If the letting ceases temporarily due to the following circumstances:

(a) repair or renovation of the building;

(b) absence of tenants for a period of 2 years after termination of tenancy;

(c) legal injuction or other official sanction; or

(d) other circumstances beyond the control of the person who lets out the real property;

expenses for the period the real property is not let out are allowable provided that the real property is maintained in good condition and is ready to be let out.

Example 21

Sinar Ria Sdn Bhd owns a 4-storey building which is let out to Deena Holding Bhd since 2016. The letting of the real property is treated as a business source. Sinar Ria Sdn Bhd closes its accounts on 31 December every year. On 31.12.2018**,** the letting of the building ends. The company makes an effort to obtain a new tenant but only manages to let out the building to another company on 1.4.2021 (absence of tenants for a period of 27 months).

Expenses during the absence of tenants for a period of 2 years are deductible. Therefore the expenses for the period of 1.1.2019 to 31.12.2020 are allowable. However the expenses for the period of 1.1.2021 to 31.3.2021 are not allowed a deduction since that period exceeds the specified period of 2 years.

Example 22

Syarafina owns 2 houses which are let out since 2016. The rental income is assessed as a non-business source under paragraph 4(*d*) of the ITA. The gross income and allowable expenses for each real property for the years of assessment 2017 and 2018 are as follows:

Real Property	Gross Income RM		Assessment , Quit Rent and Interest Expense RM	
	YA 2017	YA 2018	YA 2017	YA 2018
House I	12,000	12,000	3,550	3,550
House II	9,600	-[1]	2,500	2,500

[1]House II was not rented out as the local authorities had given an instruction to vacate the house from 1.1.2018 to 31.12.2018 so that the hill slopes could be monitored after a landslide had occurred at a nearby area. The house was rented out again on 1.1.2019.

The statutory income from rent for the YA 2017 is computed as follows:

	RM
Rental income [paragraph 4(*d*)]	21,600
Less: Allowable expenses	6,050
Statutory income from rental	15,550

The statutory income from rent for the YA 2018 is computed as follows:

	RM
Rental income [paragraph 4(*d*)]	12,000
Less: Allowable expenses	6,050
Statutory income from rental	5,950

8.5 Expenses before real property is let out

Expenses in respect of a period before the real property is let out is not deductible and has to be adjusted proportionately.

Example 23

Michael lets out a shop house commencing from 1.5.2017 for RM2,500 a month. He pays annual assessment amounting to RM1,200, annual quit rent amounting to RM120 and fire insurance premium of RM600 for year 2017. The letting of the shop house is a non-business source and the rental income is taxable under paragraph 4(*d*) of the ITA.

The adjusted income from rent for the YA 2017 is computed as follows:

		RM
Rental income (gross)		
Period of 1.5.2017 – 31.12.2017 (8 x RM2,500)		20,000
Less:		
Expenses for period of 1.5.2017 – 31.12.2017		
Assessment (8/12 x RM1,200)	800	
Quit rent (8/12 x RM120)	80	
Fire insurance premium (8/12 x RM600)	400	1,280
Adjusted income from rent		18,720

8.6 Restriction on interest expense

If a person takes a loan for business purposes and to finance the purchase of real property that is let out, interest expense allowable against the business source has to be restricted under subsection 33(2) of the ITA. Interest expense on loan to finance the purchase of real property that is let out is deductible from rental income.

Example 24

Azalea Property Sdn Bhd, a property development company closes its accounts on 31 December every year. On 9.6.2016 the company takes a loan of RM2 million from a bank for business purposes and to finance the purchase of a bungalow costing RM450,000. The company claims an interest expense of RM120,000 in the profit and loss account for the year assessment 2017.

The bungalow is let out commencing from 1.1.2017 and income from letting of the bungalow is taxable under paragraph 4(*d*) of the ITA.

Interest restriction is computed as follow:

$$\frac{RM450{,}000}{RM2{,}000{,}000} \times RM120{,}000 = RM27{,}000$$

The amount of RM27,000 is added back in arriving at the adjusted income from business of the company. However the company can claim interest expense of RM27,000 against income from the letting of the bungalow.

Note: Since the cost of the bungalow does not exceed RM500,000, interest restriction under subsection 33(2) of the ITA is calculated based on the end-of-year balance in the balance sheets.

9. Rental Income Received in Advance

9.1 Rental received in advance is treated as gross income for the basis period in which it is received.

9.2 Where the letting of property is a non-business source, rental income received in advance is assessed under paragraph 4(*d*) of the ITA in the basis period in which it is received, any expense incurred in relation to that rental income after that basis period is allowable in the basis period in which the income is assessed. Therefore amendment has to be done to the assessment for the YA concerned.

Example 25

Kelvin Ong lets out a double-storey terrace house for the period of 1.1.2016 to 31.12.2018. Rental for the three years amounting to RM36,000 is received in the year 2016. Expenses incurred on that house are as follows:

Income/Expenses	Year Ended		
	31.12.2016 RM	31.12.2017 RM	31.12.2018 RM
Rental income	36,000	-	-
Expenses incurred	4,000	5,000	3,000

The adjusted income from rent for the YA 2016 is computed as follows:

	YA 2016 RM
Rental income Less: Expenses incurred in the year 2016 Adjusted income	36,000 4,000 32,000

In the year 2017, rental expenses of RM5,000 was incurred and allowable. This sum is allowable against the rental income assessed in the YA 2016 as follows:

	YA 2016 RM
Rental income Less: Expenses incurred in the year 2016 Adjusted income Less: Expenses incurred in the year 2017 Amended adjusted income	36,000 4,000 32,000 5,000 27,000

In the year 2018, rental expenses of RM3,000 was incurred and allowable. This sum is allowable against the rental income assessed in the YA 2016 as follows:

	YA 2016 RM
Rental income Less: Expenses incurred in the year 2016 Adjusted income Less: Expenses incurred in the year 2017 Amended adjusted income Less: Expenses incurred in the year 2018 Amended adjusted income	36,000 4,000 32,000 5,000 27,000 3,000 24,000

9.3 Effective from the YA 2016, paragraph 24(1)(b) of the ITA was amended by the Finance Act 2005 (Act 733) to apply to any services rendered or to be rendered and paragraph 24(1)(*c*) of the ITA was amended to apply to the use or enjoyment of any property dealt with or to be dealt with.

Therefore in a relevant period, where any services rendered or to be rendered at any time in the course of carrying on a business as provided in paragraph 24(1)(b) ITA and any debt is owing in respect of the use or enjoyment of any property dealt or to be dealt withat any time in the course of carrying on a business as provided in paragraph 24(1)(c) the amount of debt is treated as the gross income from a business for the relevant period.

Effective YA 2016 subsection 24(1A) of the ITA was introduced which provides that, "where in the relevant period, any sum is received by a relevant person in the course of carrying on a business in respect of any services to be rendered or the use or enjoyment of any property to be dealt with in the relevant period or in any following basis period, the sum shall be treated as gross income of the relevant person from the business for the relevant period in which the sum is received, notwithstanding that no debt is owing to the relevant person in respect of such services or such use or enjoyment".

In other words, where the letting of property is a business source under paragraph 4(*a*) of the ITA, the rental income received in advance in respect of the future use or enjoyment of any property in the relevant period or in any following basis period is to be taxed in the basis period it is received, notwithstanding that the use or enjoyment of the property has yet to be dealt with.

Where advance rental income in a particular YA has been taxed, any expense incurred after that YA, which is in relation to the advance rental income, would be allowable in accordance with section 33 of the ITA in the basis period of the YA the expense was incurred.

With the introduction of subsection 34(7A) of the ITA by the Finance Act 2005 (Act 733), in a case of a refund of the advance payment to the tenant, a claim for a tax deduction on the amount refunded can be made in the basis period the refund occurs.

Example 26

Same facts as in Example 16 with additional information as follows:

i. AJ Sdn Bhd received advanced rental for 3 years amounting to RM180,000 for the 4-storey building in Damansara in the year 2016.

ii. AJ Sdn Bhd's gross income, allowable expenses and capital allowances on the furniture in each building for the YA 2016 - 2018 are as follows:

Real Property – Paragraph 4(*a*) Source	**YA 2016 RM**	**YA 2017 RM**	**YA 2018 RM**
Building in Damansara			
Gross income	180,000	Nil	Nil
Allowable expenses	14,000	14,000	14,000
Capital allowances	7,000	7,000	7,000

Building in Bangsar Gross income Allowable expenses Capital allowances	 10,000 12,000 3,000	 120,000 12,000 3,000	 120,000 12,000 3,000
Real Property – Paragraph 4(*d*) Source			
Residential house Gross income Allowable expenses	 8,000 11,000	 12,000 6,000	 12,000 8,000
Apartment Gross income Allowable expenses	 6,000 4,000	 6,000 2,000	 6,000 3,000

The total income is computed as follows:

YA 2016		**RM**	**RM**
(i)	Statutory income from rental – paragraph 4(*a*)		
	Rental income (180,000 + 10,000)		190,000
	Less: Allowable expenses (14,000 + 12,000)		26,000
			164,000
	Less: Capital allowances (7,000 + 3,000)		10,000
			154,000
(ii)	Statutory income from rental – paragraph 4(*d*)		
	Rental income (8,000 + 6,000)	14,000	
	Less: Allowable expenses (11,000 + 4,000 = 15,000) Restricted to	14,000	Nil
	Aggregate / Total income		154,000

YA 2017		**RM**	**RM**
(i)	Statutory income from rental – paragraph 4(*a*)		
	Rental income		120,000

	Less: Allowable expenses (14,000 + 12,000)		26,000
			94,000
	Less: Capital allowances (7,000 + 3,000)		10,000
			84,000
(ii)	Statutory income from rental – paragraph 4(*d*)		
	Rental income (12,000 + 6,000)	18,000	
	Less: Allowable expenses (6,000 + 2,000)	8,000	10,000
	Aggregate / Total income		94,000

YA 2018		**RM**	**RM**
(i)	Statutory income from rental – paragraph 4(*a*)		
	Rental income		120,000
	Less: Allowable expenses (14,000 + 12,000)		26,000
			94,000
	Less: Capital allowances (7,000 + 3,000)		10,000
			84,000
(ii)	Statutory income from rental – paragraph 4(*d*)		
	Rental income (12,000 + 6,000)	18,000	
	Less: Allowable expenses (8,000 + 3,000)	11,000	7,000
	Aggregate / Total income		91,000

9.4 In the case where there is more than one real property and rental income from one or several real properties is received in advance, expenses related to that source is deductible from other rental income in the basis period in which the expenses are incurred. This treatment is only applicable to rental income from real properties which are assessed as one source.

Example 27

Fortune Sdn Bhd lets out 2 buildings commencing from 1.1.2016. The company receives rental for 3 years amounting to RM300,000 in 2016 in relation to the first building. The second building is let out for RM10,000 a month. The letting of both buildings is treated as a rental source under paragraph 4(*d*) of the ITA. Income received and the allowable expenses for the building are as follows:

Year Ended	First Building		Second Building	
	Income RM	Expenses RM	Income RM	Expenses RM
31.12.2016	300,000	20,000	120,000	30,000
31.12.2017	-	15,000	120,000	30,000
31.12.2018	-	18,000	120,000	30,000

The adjusted income from rental for the years of assessment 2016 to 2018 are computed as follows:

	YA 2016 RM	YA 2017 RM	YA 2018 RM
Rental income	420,000	120,000	120,000
Less: Expenses	50,000	45,000	48,000
Adjusted Income	370,000	75,000	72,000

Example 28

Facts are the same as in Example 27 but the letting of the first building is treated as a business source under paragraph 4(*a*) of the ITA whereas the letting of the second building is treated as non-business source under paragraph 4(*d*) of the ITA.

The adjusted income from rental for the years of assessment 2016 to 2018 is computed as follows:

Rental source under paragraph 4(*a*) of the ITA

	YA 2016 RM	YA 2017 RM	YA 2018 RM
Rental income	300,000	Nil	Nil
Less: Expenses	20,000	15,000	18,000
Adjusted income / (loss)	280,000	(15,000)	(18,000)

Rental source under paragraph 4(*d*) of the ITA

	YA 2016 RM	YA 2017 RM	YA 2018 RM
Rental income	120,000	120,000	120,000
Less: Expenses	30,000	30,000	30,000
Adjusted income	90,000	90,000	90,000

The current year business loss under paragraph 4(*a*) of the ITA, amounting to RM15,000 and RM18,000 for the YA 2017 and 2018 respectively, can be set off against the aggregate income in the relevant YA. The computation is as follows:

	YA 2016 RM	YA 2017 RM	YA 2018 RM
Statutory rental income [paragraph 4(*a*) of the ITA]	280,000	Nil	Nil
Statutory rental income [paragraph 4(*d*) of the ITA]	90,000	90,000	90,000
Aggregate income	370,000	90,000	90,000
Less: Current year rental loss [paragraph 4(*a*) of the ITA]	Nil	(15,000)	(18,000)
Total income	370,000	75,000	72,000

Note

If the current year rental loss under paragraph 4(*a*) of the ITA cannot be fully absorbed in the relevant YA, the unabsorbed amount can be carried forward to the following YA.

10. Capital Allowances

10.1 If the letting of real property is treated as a business source, capital allowances can be claimed on capital expenditure incurred on plant and machinery. The provisions in Schedule 3 of the ITA relating to capital allowances shall apply to the business of letting of real property.

10.2 If the letting of real property is treated as a business source and the letting of real property ceases temporarily due to the circumstances mentioned in paragraph 8.4.2 of this PR, capital allowances can still be claimed in respect of the period the real property is not let out provided the real property is maintained in good condition and is made available for letting.

Example 29

Saravanan Sdn Bhd let out a shop lots building since 2015. The letting is treated as business source. On 1.4.2017 the building is repaired and cannot be occupied until 31.5.2017. The building is only let out again on 1.6.2017. Capital allowances claimed for the YA 2017 is RM30,000.

Even though the letting of shop lot building ceases from 1.4.2017 to 31.5.2017, the whole amount of capital allowances of RM30,000 can be claimed in the YA 2017 since the letting ceases temporarily due to the repair of the building.

Example 30

Harris Property Sdn Bhd owns a 5-storey building which is let out to Fetty Holding Bhd since 2015. The letting of the real property is treated as business source. Harris Property Sdn Bhd closes its accounts on 31 December every year. On 1.3.2016, the tenancy of the building ceases and Fetty Holding Bhd does not renew the tenancy. The building is left vacant until 31.12.2017 despite the efforts of the company to find a new tenant (including advertising the letting in several newspapers). Harris Property Sdn Bhd only manages to let out the building to another company on 1.1.2018 (absence of tenants for a period of 22 months). Capital allowances have been claimed since 2015.

Even though the letting of building ceases from 1.3.2016 to 31.12.2017, capital allowances can be claimed in the years of assessment 2016 and 2017 since the letting ceases temporarily due to the absence of tenants for a period of less than 2 years.

Example 31

Facts are the same as in Example 30 except that the building is not let out until 31.3.2018. Harris Property Sdn Bhd only manages to let out the building to another company on 1.4.2018 (absence of tenants for a period of 25 months).

Harris Property Sdn Bhd is eligible to claim capital allowances for the years of assessment 2016 and 2017. Harris Property Sdn Bhd is also eligible to claim capital allowance for the YA 2018 if the letting of the building is treated as a business source for that YA.

10.3 If there is a change in tax treatment of the letting of a real property from a business source under paragraph 4(*a*) of the ITA to a non-business source under paragraph 4(*d*) of the ITA in the basis period for a YA, the person who lets out the real property has two sources of income from the same real property in that basis period, i.e a business source under paragraph 4(*a*) of the ITA and a non-business source under paragraph 4(*d*) of the ITA. If as a result of the change:

10.3.1 a company becomes an investment holding company (IHC), the rental income (business source) would be assessed as income under paragraph 4(*d*) of the ITA. Therefore, the company is not entitled to claim for capital allowances on plant and machinery since they are not used for the purpose of a business at the end of the basis period for that YA.

10.3.2 a company does not become an IHC, the company still derives rental income under paragraph 4(*a*) and 4(*d*) of the ITA in respect of the real property. Even though the company is not an IHC, the company would not be entitled to claim for capital allowances on plant and machinery since they are not used for the purpose of a business at the end of the basis period for that YA.

Note: The determination of whether a company is an IHC or not is explained in the PR No. 3/2011 (Investment Holding Company).

10.4 If a company has a business source and a rental source (not necessary to determine whether an IHC or not since its main activity is not the holding of investments) and there is a change in tax treatment of the letting of a real property from a business source under paragraph 4(*a*) of the ITA to a non-business source under paragraph 4(*d*) of the ITA in the basis period for a YA, the company still derives rental income under paragraph 4(*a*) and 4(*d*) of the ITA. The company would not be entitled to claim for capital allowances on plant and machinery since they are not used for the purpose of a business at the end of the basis period for that YA.

Note: In the case where capital allowances cannot be claimed, the residual expenditure of the plant and machinery will be reduced by notional allowances for that YA and subsequent YA.

Example 32

Menara Sdn Bhd owns an office building consisting of 20 units and lets out all the fully furnished units since 2013. The letting is treated as a business source since maintenance services and support services are comprehensively and actively provided by Menara Sdn Bhd. Capital allowance have been claimed on the furnitures in the office building.

However from June 2017, Menara Sdn Bhd did not provide maintenance services and support services. Menara Sdn Bhd closes its accounts on 31 December every year.

Menara Sdn Bhd is not entitled to claim capital allowances on the furnitures in the office building for the YA 2017 since the furnitures are not used for the purpose of a business at the end of the basis period for that YA. Notional allowances will be deducted to arrive at the residual expenditure of the furnitures for the YA 2017 and subsequent YA.

10.5 If more than one real property is let out and there is a change in tax treatment of any of the real properties from a business source under paragraph 4(*a*) of the ITA to a non-business source under paragraph 4(*d*) of the ITA in the basis period for a YA, capital allowances can be claimed on plant and machinery for the real property which remains as a business source under paragraph 4(*a*) of the ITA.

10.6 If there is a change in tax treatment of the letting of a real property from a non-business source under paragraph 4(*d*) of the ITA to a business source under paragraph 4(*a*) of the ITA in the basis period for a YA, the person who lets out the real property has two sources of income from the same real property in that basis period, i.e a non-business source under paragraph 4(*d*) of the ITA and a business source under paragraph 4(*a*) of the ITA. Capital allowances can be claimed on plant and machinery in the real property since they are used for the purpose of a business at the end of the basis period for that YA. For the purpose of computing capital allowances, the qualifying expenditure for the plant and machinery is the market value on the first day they are used in the business.

Example 33

Teguh Sdn Bhd closes its accounts on 31 December every year and its main activity is the holding of investments. The company owns and lets out a fully-furnished 10-storey office building. The letting is treated as a rental source under paragraph 4(*d*) of the ITA. From 1.3.2017 the company provides maintenance services and support services comprehensively and actively. The company is not an IHC in the YA 2017 since the income from holding of investment is less than 80% of its gross income.

Teguh Sdn Bhd is entitled to claim capital allowances on the furnitures in the office building for the YA 2017 since they are used for the purpose of a business at the end of the basis period for that YA. For the purpose of computing capital allowances for the YA 2017, the qualifying expenditure for the furnitures is the market value on 1.3.2017. No initial allowance will be given.

11. Industrial Building Allowance

11.1 If a person owns a building lets out the building and the building is in used as an industrial building, industrial building allowance can be claimed by the owner of the building even though the letting is a non-business source.

11.2 If the letting of real property is given a special treatment as explained in paragraph 4.4 of this PR, the owner of the building is eligible to claim industrial building allowances on the qualifying building expenditure incurred.

12. Replacement Cost of Furnishings

If the letting of a furnished real property is treated as non-business source, cost of replacing furnishings such as furniture and air conditioner can be claimed as a deduction from gross income from that letting.

13. Letting of Part of Building Used in the Business

If a building, whether owned or rented, is used for business purposes and part of the building is let out, the rent arising from the letting is treated as part of income from the existing business source.

14. Updates and Amendments

This PR replaces the PR No. 4/2011 dated 10 March 2011.

No.	Paragraph	Remarks
1.	9.2	Paragraph 9.2 is amended
2.	9.3	New paragraph inserted
3.	9.4	Previous 9.3 renumbered as 9.4

15. Disclaimer

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

Director General of Inland Revenue,
Inland Revenue Board Malaysia.