

# Chapter 4

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## Capital Allowances

### Introduction

Depreciation and amortisation of fixed assets for accounting purposes are not allowable for tax purposes. In their place, tax deductions take the following form:-

- Plant and Machinery Allowances
- Industrial Building Allowances
- Agriculture Allowances
- Forest Allowances

### Plant and Machinery Allowances

Capital Allowances for Plant and Machinery fall under the following categories:-

- Initial allowance (IA) - this is given once, for the Year of Assessment relating to the basis period in which the qualifying capital expenditure is incurred.
- Annual allowance (AA) - this is given each year commencing from the Year of Assessment relating to the basis period in which the qualifying capital expenditure is incurred.
- Balancing allowance - where an asset is disposed of and the disposal proceeds are less than the tax written down value of the asset, the disposer is entitled to claim the difference as a balancing allowance.

- Balancing charge - conversely where an asset is disposed of and the disposal proceeds are more than the tax written down value of the asset, the difference will be imposed on the disposer as a balancing charge. The balancing charge is restricted to the total capital allowances claimed by the disposer.

### ***Persons Entitled to Claim Capital Allowances***

Capital allowances are only granted to a person who is carrying on a business. In other words, capital allowances are only deductible against a business source of income.

### ***Conditions to be Fulfilled***

- The claimant must be carrying on a business;
- The capital expenditure must have been incurred by the claimant;
- The plant or machinery must be in use for the purpose of the claimant's business; and
- The claimant must be the owner (legal or beneficial) of the asset at the end of the basis period.

### ***Capital Allowances in Respect of Motor Vehicles***

The qualifying capital expenditure for a motor vehicle which is not licensed or permitted to be used for the commercial transportation of goods or passengers is restricted to RM100,000 (from 28 October 2000 onwards) if the motor vehicle has not been used prior to purchase and the total on the road cost does not exceed RM150,000. Otherwise, the eligible cost is restricted to RM50,000.

## **Industrial Building Allowance (IBA)**

IBA is granted to a person who incurs qualifying capital expenditure on the construction or purchase of an industrial building or structure for use in a qualifying trade.

Where the industrial building is acquired secondhand, special rules apply in quantifying the amount of IBA available.

Generally a building or structure is regarded as an industrial building if it is used as a factory.

The Income Tax Act 1967 specifically provides that certain special buildings qualify as industrial buildings, such as:-

- Licensed private hospital, maternity home, nursing home;
- Building used for research;
- Building used for industrial, technical and vocational training approved by the Minister of Education;
- Building used solely for the storage of goods for export or for the storage of imported goods which are to be processed and re-exported;
- Building used for an approved service project;
- Building used as living accommodation for employees;
- Building used for a school or an educational institution approved by the Minister of Education;
- Road and ancillary structures for public use;
- Building used as child care facilities;
- Building used solely for the purpose of a hotel and that hotel is registered with the Ministry of Culture, Arts and Tourism regardless whether the hotel is granted pioneer status or investment allowance incentive (effective YA2002);
- Airports; and
- Motor racing circuit.

### ***Expenditure Qualifying for IBA***

The qualifying expenditure refers to the cost of constructing the industrial building or the purchase price of the building. Land cost is specifically excluded.

Apart from the actual cost of construction, the following types of expenditure also qualify for IBA:-

- Architect's fees;
- Costs of digging and laying foundations for drains, water-pipes and electric cables;
- The cost of preparing plans, etc in connection with obtaining approval of the local authority for the erection of the building;
- The cost of demolition of any existing building where the new building is to be constructed on the site of the old building;
- The cost of construction which will include labour, materials, haulage, management, supervision and other overhead charges or 'on cost';
- Incidental expenditure on work which may be separately constructed, eg drainage scheme, installation of water, electricity; and
- Cost of installing fittings forming part of the building.

## **Agriculture Allowance**

This is a form of capital allowance given in respect of qualifying agriculture expenditure incurred in the working of a farm. 'Farm' refers to any land used for the purposes of agriculture.

### ***Qualifying Agriculture Expenditure***

Qualifying agriculture expenditure includes the following:-

- Clearing and preparing land for the purpose of agriculture;
- Planting (but not replanting) of crops;
- Constructing a road or bridge on a farm; and
- Constructing a building on a farm, where the building is used in connection with the working of a farm including that for employee's welfare and accommodation.

***Rates of Allowance***

|   |  |     |
|---|--|-----|
| ■ | Expenditure incurred in the construction of a building not for the welfare of or as living accommodation for employees | 10% |
| ■ | Expenditure incurred in the construction of a building for the welfare of or as living accommodation for employees     | 20% |
| ■ | All other qualifying expenditure   | 50% |

**Forest Allowance**

This is an allowance given to a person who incurs qualifying forest expenditure for the purpose of extracting timber from a forest. A forest is one relating to which a concession or a licence to extract timber therefrom has been granted.

***Rates of Allowance***

|   |  |     |
|---|--|-----|
| ■ | Expenditure incurred in the construction in a forest of a road or building used for the extraction of timber from the forest     | 10% |
| ■ | Expenditure incurred in the construction in a forest of a building provided for the welfare of or as accommodation for employees | 20% |

## Summary of Capital Allowance Rates

The rates generally allowed at present are:-

| <i>Allowance</i>  | <i>Initial<br/>Allowance (IA)</i> | <i>Annual<br/>Allowance (AA)</i> |
|---|-----------------------------------|----------------------------------|
| ■ Industrial Buildings  |                                   |                                  |
| - constructed building  | 10%                               | 3%                               |
| - purchased building  | 10%                               | 3% / permitted<br>fraction       |
| <p>Prior to YA 2002, IA is not given on a purchased building, and AA is computed based on a permitted fraction which is effectively the claimable cost (which need not be the purchase price) divided by 50 years minus the age of the building in the year it is purchased.</p> <p>Effective YA2002, IA is extended to a purchased building and the person can claim the AA on a purchased building at a rate of 3% or the permitted fraction if it is higher than 3%.</p> |                                   |                                  |
| ■ Plant and Machinery   |                                   |                                  |
| furniture and fittings  | 20%                               | 10%                              |
| office equipment  | 20%                               | 10%                              |
| computers/IT equipment  | 20%                               | 40%                              |
| motor vehicles licensed for commercial use  | 20%                               | 20%                              |
| other motor vehicles  | 20%                               | 20%                              |
| (qualifying cost limited to RM100,000 if the motor vehicle has not been used prior to purchase and the total on the road cost does not exceed RM150,000. Otherwise, it is restricted to RM50,000)   |                                   |                                  |
| plant and machinery (generally)   | 20%                               | 14%                              |
| heavy machinery   | 20%                               | 20%                              |
| ■ Warehouse used for storage of goods for export or for the storage of imported goods which are to be processed and distributed or re-exported.   | -                                 | 10%                              |
| ■ Building used for industrial, technical and vocational training approved by the Minister of Education   | -                                 | 10%                              |
| ■ Building used for an approved service project   | 10%                               | 3%                               |
| ■ Building used as living accommodation for employees   | 40%                               | 3%                               |
| ■ Building used for a school or an educational institution approved by the Minister of Education  | -                                 | 10%                              |
| ■ Building used as child care facilities  | -                                 | 10%                              |

|   |   |     |                   |
|---|---|-----|-------------------|
| ■ | Construction of public road and ancillary structures which expenditure is recoverable through toll collection | 10% | 6%                |
| ■ | Hotel registered with the Ministry of Culture, Arts and Tourism (effective YA2002)                            | 10% | 3%                |
| ■ | Assets with a lifespan of not exceeding 2 years   | -   | Replacement basis |

The annual allowance for building is increased from 2% to 3% effective Year of Assessment 2002.

All rates are applied to the original qualifying cost of the relevant fixed assets. If capital allowances in any year are not fully absorbed by adjusted business income, they are carried forward for set off against future income from the same business source only.