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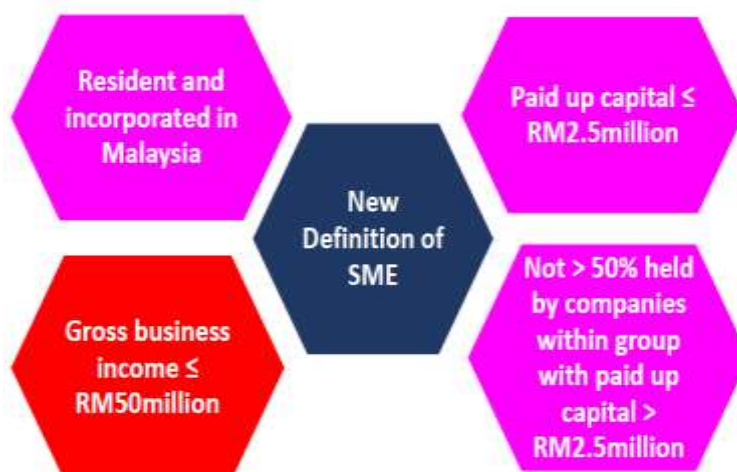
NEW DEFINITION OF SME COMPANY WITH EFFECT FROM YA 2020

KEY BENEFITS OF SME COMPANY

HOW DOES NEW DEFINITION OF SME AFFECTING INVESTMENT HOLDING COMPANY?

Additional condition for Small and Medium Enterprise to enjoy preferential tax rate

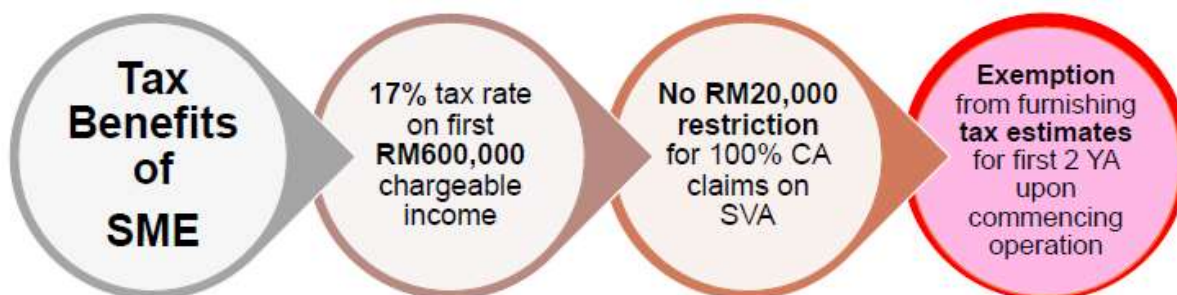
A new condition was introduced with effective from year of assessment (YA) 2020 for company to be categorised as Small and Medium Enterprise (SME) in order to enjoy certain preferential tax treatments under the Income Tax Act (ITA), 1967.



Based on the above diagram highlighted in red, the new condition introduced required SME company to have a gross income from source or sources consisting of a business not exceeding RM50million for the basis period for that YA in addition to the existing conditions.

What are the Key Benefits of SME Company?

The key tax benefits of SME company under the ITA, 1967 are summarised below:



Abbreviation: SVA = Small value asset is asset cost RM2,000 or less

How Does New Definition of SME Affecting Investment Holding Company?

Generally, an investment holding company (IHC) is a company specifically established to hold investments and earning income from passive source such as, rental income, dividend income and interest income. As no business activity is undertaken by an IHC, it will not meet the new condition as a SME company.

Let us explore a practical example below on how does the new definition of SME affect IHC.

A Co – IHC
Paid up capital ≤ RM2.5million



Source of income	RM
Interest income	55,000
Investment - Rental income	550,000
Total gross income	605,000
Permitted expenses (assumption)	5,000

Old definition (SME)

	RM
Gross income	605,000
Less: Permitted expenses	(5,000)
Aggregate income / CI	600,000
Income tax payable 1 st RM600,000 @ 17%	102,000

New definition (Non-SME = No biz income)

	RM
Gross income	605,000
Less: Permitted expenses	(5,000)
Aggregate income / CI	600,000
Income tax payable RM600,000 @ 24%	144,000

Abbreviation: Biz = Business / CI = Chargeable income

Based on the above illustration, under the new definition of SME, A Co does not fulfil the new condition of having a business income. As such, A Co is no longer a SME company and its tax liability has been increased from RM102,000 to RM144,000 as the Company is no longer enjoying the preferential tax rate of 17% on first RM600,000 chargeable income.

In respect of group of companies affected by the above new definition of SME, a restructuring of business activities of the group may be considered in order to meet the new conditions of SME. Please contact us if our assistance is required to advise on the above.

Editor's Comment:

With the introduction of a new condition for SME company to have a gross income from business or businesses of not more than RM50million with effective from YA 2020, it may affect IHC to be qualified as SME company. As a result, IHC may not be eligible to enjoy the preferential tax rate at 17% on the first RM600,000 chargeable income. In view of this, IHC with financial year ending on 31 December 2020 which cannot fulfil the new condition of SME may need to revisit its tax estimate for YA 2020 and to make a revision latest by 30 September 2020 to take into consideration the above changes to the definition of SME in order to avoid potential under-estimation of tax penalty.

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