

TAX IMPLICATIONS FOR EMPLOYERS AMIDST COVID-19

The adverse impact of COVID-19 to businesses has been severe in most cases. This has forced employers to seek for alternatives to how they manage their human resources.

We share some thoughts on the tax implications for some of the possible scenarios.

1. Participation in Wage Subsidy Programme (WSP)

Employers who are approved for the WSP with Social Security Organization (SOCSO) may receive subsidies of up to a certain amount for the salary of a number of its employees.

Tax implication

Section 22(2) of the Income Tax Act, 1967 provides the following:

The gross income of a person from a source of his for the basis period for a year of assessment shall include any sums receivable or deemed to have been received for that basis period in relation to that source by way of-

(a) insurance, indemnity, recoupment, recovery, reimbursement or otherwise-

(b) where such sums are in respect of the kind of outgoings and expenses deductible in ascertaining the adjusted income of that person from that source.

Salary cost is generally a deductible expense of the employer in ascertaining the adjusted income of its business. As the subsidy received by the employer may be considered as a recoupment/reimbursement of its salary cost, it should be treated as part of its taxable business income. While such income may be exempted under Income Tax (Exemption) (No.22) Order 2006, the

corresponding amount of subsidized salary expense would not be allowable for tax deduction.

2. Participation in Employment Retention Program (ERP)

Where employees agreed to take no pay leave with their employers and participate in the ERP, each qualifying employee may receive financial assistance of RM600 for up to 6 months. The funds are channelled from SOCSO to the employees through the employer's account

Tax implication

As the employee agreed to be on no pay leave, the employer should not be obligated to pay the employee. Thus, the monthly RM600 received by the employee under ERP should not be seen as being akin to a wage subsidy. As such, this amount should not be taxable to the employer.

3. PTPTN Loan Payment Deferment

PTPN monthly loan repayments are given deferment for a total 6 months starting from 19 March 2020 until 30 September 2020.

Tax implication

Currently, employers who repay the PTPTN loans on behalf of its employees are given a special tax deduction under the Income Tax (Deduction for Payment of Educational Loan of



Perbadanan Tabung Pendidikan Tinggi Nasional by Employers on behalf of Employees) Rules 2019. The Income Tax (Deduction for Payment of Educational Loan of Perbadanan Tabung Pendidikan Tinggi Nasional by Employers on behalf of Employees) (Amendment) Rules 2019 extends the special tax deduction for payments made until 31 December 2021.

In cases where the deferment of payment of loan results in a certain amount of instalments being payable after 31 December 2021, the employer may lose out on that amount of special tax deduction claimable.

4. Pay cut/ Reduction in salaries paid.

As business are affected by cash flow during this MCO period, employers are looking to reducing cost which may come in the form of pay cut/ reduction in salary.

Tax implication

Any pay cut/ reduction in salary is a reduction of expense to the employer. Accordingly, there would be lesser tax deduction claimable by the employer. It should be noted that even if there is insufficient income to absorb these expenses, resulting in a loss, the unabsorbed loss may be carried forward to be utilised in future years of assessment (but no more than for 7 consecutive years of assessment).

5.Redundancy payment

Businesses may be forced to retrench its employees due to market conditions.

Tax implication

Redundancy payments or retrenchment benefits made on cessation of a business have been held to be not tax deductible for the employer with reference to cases R Rubber Estate Bhd v DGIR; and Ampat Tin Dredging Ltd v DGIR.

Where, however, compensation is paid which results in the increase or retention of a source of income, it is a deductible expense for the employer per the case DGIR v Kulim Rubber Plantation Ltd.

Employer's responsibility on retrenchment /redundancy exercise

The employer must give the affected employees a notice of retrenchment. The notice period is based on the employment contract or collective agreement, and employees who fall within the scope of the Employment Act (EA) – generally these are employees whose monthly earnings are not more than RM2,000 – are entitled to the minimum notice period in the EA.

It's advisable to consult or inform employees of a potential retrenchment as soon as possible.

Employers are also required to submit a written notification (**PK Form**) to the nearest Department of Labour at least 30 days before conducting a retrenchment exercise.

The right of an employee to a termination benefit upon retrenchment depends whether or not he is covered by the EA.

An employee who **falls within the scope of the EA** is entitled to termination benefits if he has been employed for at least 12 months. The termination benefits payable are as follows (or the amount in the employment contract if it is higher):

- 10 days' wages for every year of employment if he has been employed for less than two years;
- 15 days' wages for every year of employment if he has been employed for two years or more but less than five years; or
- 20 days' wages for every year of employment if he has been employed for five years or more.

An employee who is **not covered by the EA** is only entitled to termination benefits if it is provided in his employment contract. If the contract is silent, then it is up to the employer whether or not to pay termination benefits, and how much to pay.



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The Code of Conduct for Industrial Harmony – a guide for employers considering retrenchment

Although it is not legally-binding, the Industrial Court encourages employers to comply with the Code of Conduct for Industrial Harmony which was issued in 1975 because it is a good practice.

The Code recommends that, where redundancy is likely, an employer should take positive steps to avert or minimise reductions of workforce by adopting appropriate measures such as –

- limitation on recruitment;
- restriction of overtime work;
- restriction of work on weekly day of rest;
- reduction in number of shifts or days worked a week;
- reduction in the number of hours of work;
- re-training and/or transfer to other department/work.

Where a retrenchment becomes necessary, the Code encourages employers to take the following measures:

- Giving early warning to the affected employees.
- Introducing schemes for voluntary retrenchment and retirement and for payment of redundancy and retirement benefits.
- Retiring workers who are beyond the retirement age.
- Assisting workers to find alternative employment.
- Spreading the termination of employment over a longer period.
- Ensuring that the employees are informed or consulted before a formal announcement is made.

Tax treatment – Employee

Please note that compensation for loss of employment may consist of the following:-

- Salary or wages in lieu of notice
- Compensation for breach of a contract for service
- Payments to obtain release from a contingent liability
- Ex-gratia/ contractual payments – redundancy payments, severance pay
- Payment in consideration of a covenant, arrangement restricting the activities of the employee to engage in similar kind of employment after termination

Payment of compensation for loss of employment made to the employee may be given exemption of up to RM10,000 for each complete year of service with the same employer or with companies in the same group.

The employer is required to comply with the following:

- To file a Form CP 22A [Notification of cessation of employment] to Inland Revenue Board (IRB) branch handling the income tax file of the employee.
- The employer is required to withhold money payable to the employee until they receive a letter of clearance letter from IRB.

Employee Provident Fund (EPF)

It should be noted that any payment paid by the employer to its employee as compensation for loss employment is not subject to the EPF.

Note: The EPF has announced that the due date for employers to remit their mandatory contribution for salary month of March 2020 has been extended to 30 April 2020.

Should you have any queries or require more information, please do not hesitate to contact us.



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