



INLAND REVENUE BOARD MALAYSIA

ENTERTAINMENT EXPENSE

PUBLIC RULING NO. 3/2008

Translation from the original Bahasa Malaysia text.

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DIRECTOR GENERAL'S PUBLIC RULING

A Public Ruling as provided for under section 138A of the Income Tax Act 1967 is issued for the purpose of providing guidance for the public and officers of the Inland Revenue Board Malaysia. It sets out the interpretation of the Director General of Inland Revenue in respect of the particular tax law, and the policy and procedure that are to be applied.

A Public Ruling may be withdrawn, either wholly or in part, by notice of withdrawal or by publication of a new ruling which is inconsistent with it.

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

1. This ruling explains:
 - (a) the tax treatment of entertainment expense as a deduction against gross income of a business; and
 - (b) steps to determine the amount of entertainment expense allowable as a deduction.
2. The related provisions are section 18, subsection 33(1) and paragraph 39(1)(l) of the Income Tax Act 1967 (ITA).
3. The words used in this ruling have the following meanings:
 - 3.1 “Immediate family members” means an employee’s wife or wives and his children or an employee’s husband and her children.
 - 3.2 “Child” means a legitimate child or step-child of an employee, his wife or her husband or a child proved to the satisfaction of the Director General to have been adopted by the employee, his wife or her husband in accordance with any law.
 - 3.3 “Entertainment” includes:
 - (a) the provision of food, drink, recreation or hospitality of any kind; or
 - (b) the provision of accommodation or travel in connection with or for the purpose of facilitating entertainment of the kind mentioned in paragraph (a) above,by a person or an employee of his in connection with a trade or business carried on by that person.
 - 3.4 “Entertainment related wholly to sales” means entertainment directly related to sales provided to customers, dealers and distributors but excluding suppliers.
 - 3.5 “Employer”, in relation to an employment, means:
 - (a) the master, where the relationship of master and servant subsists;
 - (b) where the relationship of master and servant does not subsist, the person who pays or is responsible for paying any remuneration to the employee who has the employment, notwithstanding that that person and the employee may be the same person acting in different capacities.

3.6 "Employee", in relation to an employment, means:

- (a) the servant, where the relationship of master and servant subsists;
- (b) where the relationship of master and servant does not subsist, the holder of the appointment or office which constitutes the employment.

3.7 "Employment" means:

- (a) employment in which the relationship of master and servant subsists;
- (b) any appointment or office, whether public or not and whether or nor that relationship subsists, for which remuneration is payable.

3.8 "Recreation and hospitality" would include:

- (a) a trip to a theme park or a recreation centre;
- (b) a stay at a holiday resort;
- (c) tickets to a show or theatre; and
- (d) gifts and give-aways.

4. General provision for deduction

Generally, under subsection 33(1) of the ITA, an expense wholly and exclusively incurred in the production of gross income from a source is allowable as a deduction against gross income from that source. However, the allowable expense under subsection 33(1) of the ITA is subject to the specific prohibition under subsection 39(1) of the ITA.

5. Deduction for entertainment expense

An entertainment expense that is wholly and exclusively incurred in the production of gross income under subsection 33(1) of the ITA is not allowed a deduction of fifty percent (50%) unless the entertainment expense falls within any of the specified categories in proviso (i) to (viii) of paragraph 39(1)(l) ITA, then it qualifies for a deduction of one hundred percent (100%).

6. Principles in determining the allowable entertainment expense

In determining whether an entertainment expense can be allowed as a deduction and the amount to be allowed, the following steps have to be adhered to:

- (a) Determine whether the expense falls within the definition of entertainment as provided under section 18 of the ITA. No deduction is allowed as entertainment expense if the expenditure does not fall within the definition of entertainment.

Example 1:

Syarikat Megah Jaya held an annual dinner for its employees and incurred a cost of RM10,000.

The expense amount of RM10,000 incurred by the Syarikat Megah Jaya is an entertainment expense under section 18 of the ITA.

- (b) If the expense amount falls within the definition of entertainment provided under section 18 of the ITA, determine whether the expense is wholly and exclusively incurred in the production of gross income under subsection 33(1) of the ITA. If the expense is not wholly and exclusively incurred in the production of gross income, then the expense is not allowed a deduction. The test under subsection 33(1) of the ITA is also applicable to entertainment expense as it is applicable to other expenses.

Example 2:

Wendy Sdn Bhd gave its customer a microwave oven as a wedding gift.

The expense incurred on the wedding gift is an entertainment expense but is not allowed a deduction because it is not wholly and exclusively incurred in the production of gross income under subsection 33(1) of the ITA.

Example 3:

A property sales agent made an appointment with Mr. Ravi at a restaurant to discuss the purchase of a house proposed by the agent. The agent incurred the whole cost of lunch for himself and his potential customer, Mr. Ravi.

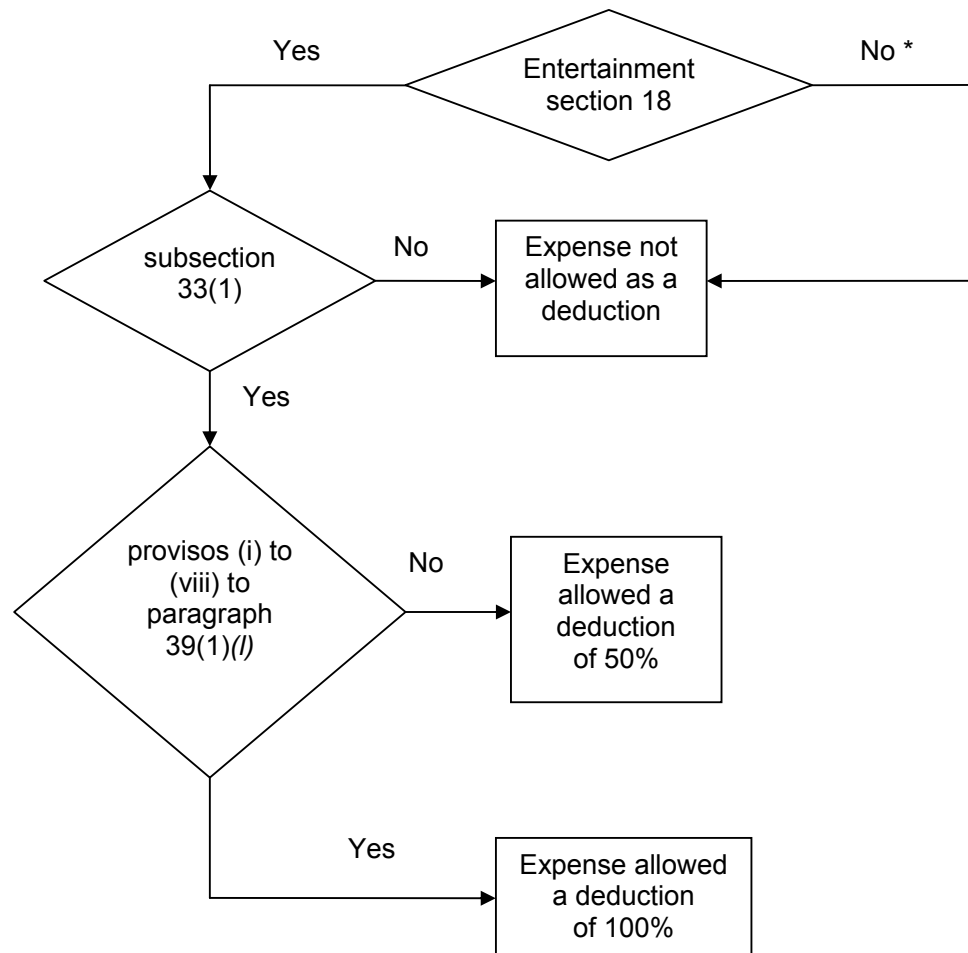
The expense incurred on lunch provided is an entertainment expense. However no deduction is allowed in relation to the entertainment provided to a potential customer because it is not wholly and exclusively incurred in the production of gross income under subsection 33(1) of the ITA.

- (c) If the expense is allowable under subsection 33(1) of the ITA, determine whether that expense is included under any of the categories of entertainment expense specified under proviso (i) to (viii) to paragraph 39(1)(l) of the ITA. If the expense is included under any of those provisos, a deduction of one

hundred percent (100%) against gross income is allowed. The remaining entertainment expense which does not fall within the mentioned provisos is allowed a fifty percent (50%) deduction against gross income.

- (d) Diagram 1 illustrates the steps to be taken in determining whether an expense qualifies as a deduction under entertainment expense and the amount allowable as a deduction.

Diagram 1:



* Expense is not allowed a deduction as entertainment expense. Expense can be identified to see whether it falls under any other kind of expenditure allowable under subsection 33(1) of the ITA.

7. Entertainment expense which qualifies for a one hundred percent (100%) deduction - proviso (i) to (viii) to paragraph 39(1)(f) of the ITA.

Entertainment expense which is wholly and exclusively incurred in the production of gross income under subsection 33(1) of the ITA and falls within the provisos (i) to (viii) to paragraph 39(1)(f) of the ITA is fully allowable. The categories of entertainment expense are as follows:

7.1 The provision of entertainment to employees - proviso (i) to paragraph 39(1)(f)(i) of the ITA

Expenditure on food, drink and recreation provided to employees except where such expenditure is incidental to the provision of entertainment for others.

Examples of such entertainment expense are expenses on free meals and refreshment, annual dinners, outings, family day or club membership for employees.

Example 4:

Duyong Emas Sdn Bhd entertains its employees at an annual dinner on 10 December 2008 and some of its suppliers are also present. The cost of the dinner is RM25,000.

The purpose of the annual dinner is to entertain the employees of Duyong Emas Sdn Bhd and the entertainment to its suppliers is only incidental to the provision of entertainment to its employees. As such, the whole amount of entertainment expense incurred amounting to RM25,000 is allowable.

7.2 The provision of entertainment for payment in the ordinary course of business - proviso (ii) to paragraph 39(1)(f) of the ITA

Expenditure on entertainment provided to customers in the normal course of business where the payment is imposed for providing that entertainment.

Examples of such entertainment are:

- (i) Providing cultural shows by restaurants or hotels at their premises to entertain their customers.
- (ii) Meals provided by airlines or other transportation business to its passengers.

7.3 The provision of promotional gifts at trade fairs or trade exhibitions or industrial exhibitions outside Malaysia - proviso (iii) to paragraph 39(1)(l) of the ITA

Expenditure incurred on promotional gifts at trade fairs or trade exhibitions or industrial exhibitions held outside Malaysia for the purpose of promoting exports from Malaysia.

Examples of such entertainment expense are expenditure incurred on samples of products of the business, small souvenirs, bags, and travel tickets provided as gifts to customers or visitors at the trade fairs or trade exhibitions or industrial exhibitions held outside Malaysia.

7.4 The provision of promotional samples of products of the business - proviso (iv) to paragraph 39(1)(l) of the ITA

Expenditure incurred on promotional samples of products of the business for the purposes of advertising that product.

Examples of such entertainment expense are free samples of products of the business given to schools or for certain other functions.

Example 5:

Syarikat Fatimah Sdn Bhd which manufactures health drinks gave free samples of the health drink to all visitors at a sporting event held at a housing estate.

The expenditure on the promotional samples is fully allowable since it falls within proviso (iv) to paragraph 39(1)(l) of the ITA.

7.5 The provision of entertainment for cultural or sporting events open to members of the public wholly to promote the business - proviso (v) to paragraph 39(1)(l) of the ITA

Expenditure incurred on providing entertainment for cultural or sporting events which are open to members of the public for the purpose of promoting the business. Cultural or sporting events which are only open to members cannot be considered as being open to the public.

Examples of cultural or sporting events and the entertainment expense related to such events are as follows:

Events	Examples of activities	Entertainment expense
Cultural	Promotion of arts such as painting, sculpture, music, drama and dance.	Cost of passage, accommodation, food and drink for the artistes.
Sports	Badminton tournaments, golf tournaments, motor racing and swimming events.	Sponsorship for food, drink, sports attire and sports equipment for sportsmen.

Cultural event under this proviso means an event which is specifically held to promote arts activities. If the event held is not a cultural event, then the provision of entertainment such as music and dance performances as part of that event do not fall within this proviso. For example, the National Day Parade is not considered a cultural event.

7.6 The provision of promotional gifts within Malaysia of articles incorporating the logo of the business - proviso (vi) to paragraph 39(1)(l) of the ITA

Expenditure on promotional gifts within Malaysia consisting of articles incorporating a conspicuous advertisement or logo of the business. Articles given away as promotional gifts need not necessarily be the products of the business. The logo could either be affixed or embossed on those articles. Logo of the business refers to the company's logo or the logo of its products.

The promotional gifts should be given to the public on a non-discriminatory basis. Expensive gifts given to selected persons or to persons who do not have business relationship with the giver is not considered as promotional gifts under this proviso.

7.7 The provision of entertainment related wholly to sales arising from the business - proviso (vii) to paragraph 39(1)(l) of the ITA

Expenditure incurred on entertainment which is related wholly to sales arising from the business.

Examples of such expenditure are as follows:

- (a) Expenses on food and drink for launching of a new product.

Example 6:

A property sales agent provides food and drinks during the launching of a new housing project to existing and potential buyers.

The expenditure on food and drinks provided is fully allowable since it falls within proviso (vii) to paragraph 39(1)(l) of the ITA.

- (b) Redemption vouchers given for purchases made.
- (c) Cash vouchers, discount vouchers, shopping vouchers, meal vouchers, concert or movie tickets.
- (d) Free gifts for purchases exceeding a certain amount.
- (e) Redemption of gifts based on a scheme of accumulated points.
- (f) "Free" maintenance/service charges or contribution to sinking fund by property developers .
- (g) Lucky draw prizes given to customers for purchases made.
- (h) Expenditure on trips given as an incentive to dealers for achieving sales target.
- (i) Expenditure incurred on refreshment given to its customer while waiting for their cars to be serviced.

Example 7:

Syarikat Arif Auto Service carrying on a car servicing business provides light refreshments such as tea, coffee, sandwiches to its customers while waiting for their cars to be serviced. The customers are not charged for the light refreshments provided.

The entertainment expense incurred on the light refreshments by Syarikat Arif Auto Service is allowed a deduction since it is related wholly to sales arising from the business of Syarikat Arif Auto Service.

7.8 The provision of leave passage benefit provided by an employer to its employees - proviso (viii) to paragraph 39(1)(l) of the ITA

Expenditure on leave passage benefit provided by an employer to its employees to facilitate a yearly event within Malaysia which involves the employer, employee and immediate family members of that employee.

Example 8:

Era Gemilang Sdn Bhd provided a family day trip for its employees to Pulau Manukan, Sabah to foster family values among its employees. The total cost incurred amounted to RM70,000 comprising cost of travel totalling RM40,000 and cost of food, drinks and accommodation totalling RM30,000.

Era Gemilang Sdn Bhd is allowed the following deductions:

- (a) *RM40,000 for the cost of leave passage by virtue of proviso (viii) to paragraph 39(1)(l) of the ITA; and*
- (b) *RM30,000 for the cost of food, drinks and accommodation by virtue of proviso (i) to paragraph 39(1)(l) of the ITA.*

8. Entertainment expense which qualifies for a fifty percent (50%) deduction - entertainment expense which does not fall within the provisos (i) to (viii) to the paragraph 39(1)(l) of the ITA

Entertainment expenditure which is wholly and exclusively incurred in the production of gross income under subsection 33(1) of the ITA but do not fall within any of the categories of entertainment expense specified in the provisos (i) to (viii) to paragraph 39(1)(l) of the ITA only qualifies for a fifty percent (50%) deduction against gross income.

Example 9:

Restu Sdn Bhd held a dinner to entertain its suppliers on 30 April 2008 and incurred a cost of RM30,000. Some of the company's employees were also present.

Since the purpose of the entertainment is to entertain the suppliers of Restu Sdn Bhd, the entertainment expense does not fall within any of the categories mentioned in the provisos to paragraph 39(1)(l) of the ITA. Fifty percent (50%) of the entertainment expense of RM30,000 is not allowed a deduction whilst the balance of fifty percent (50%) is allowed a deduction.

Example 10:

Matrix Sdn Bhd spent RM15,000 to provide hampers for its customers in conjunction with the Chinese New Year celebration to maintain existing business relationship.

Since the entertainment expense to provide hampers to its customers does not fall within any of the categories mentioned in the provisos to paragraph 39(1)(l) of the ITA, fifty percent (50%) of the entertainment expense of RM15,000 is not allowed a deduction whilst the balance of fifty percent (50%) is allowed a deduction.

Example 11:

A customer of Top Designer Sdn Bhd expands its business by opening a new branch in Shah Alam. In conjunction with the occasion, Top Designer Sdn Bhd gave flowers to its customer.

Since the entertainment expense to provide gift of flowers to its customer does not fall within any of the categories mentioned in the provisos to paragraph 39(1)(l) of the ITA, fifty percent (50%) of the entertainment expense is not allowed a deduction whilst the balance of fifty percent (50%) is allowed a deduction.

9. Steps to determine allowable entertainment expense

The principles mentioned in paragraph 6 should be applied in determining the amount of allowable entertainment expense. Table 1 illustrates the tax treatment for several examples of entertainment expense:

Table 1:

No	Types of entertainment	Allowed a deduction of		Not allowed a deduction of		ITA Provision
		100%	50%	100%	50%	
1	Entertainment given to a potential customer in a closed transaction			—/		Not wholly and exclusively incurred under subsection 33(1) of the ITA
2	Entertainment given to potential or existing customers during the launching of company's new product	—/				Proviso (vii) to paragraph 39(1)(l) of the ITA
3	Wedding gift to customer			—/		Not wholly and exclusively incurred under subsection 33(1) of the ITA
4	Entertainment to employees of related companies			—/		Not wholly and exclusively incurred under subsection 33(1)

No	Types of entertainment	Allowed a deduction of		Not allowed a deduction of		ITA Provision
		100%	50%	100%	50%	
						of the ITA
5	Entertainment for annual general meeting of company			—/		Not wholly and exclusively incurred under subsection 33(1) of the ITA
6	Cash contribution for customer's annual dinner			—/		Not wholly and exclusively incurred under subsection 33(1) of the ITA
7	Annual dinner to employees	—/				Proviso (i) to paragraph 39(1)(f) of the ITA
8	Gift with business logo for customer's annual dinner	—/				Proviso (vi) to paragraph 39(1)(f) of the ITA
9	Gift without business logo for customer's annual dinner		—/		—/	Not included under provisos (i) to (viii) to paragraph 39(1)(f) of the ITA
10	Free trip as an incentive to sales agent for achieving the sales target	—/				Proviso (vii) to paragraph 39(1)(f) of the ITA
11	Gift of flower for customer's opening of new outlet		—/		—/	Not included under provisos (i) to (viii) to paragraph 39(1)(f) of the ITA
12	Entertainment to suppliers		—/		—/	Not included under provisos (i) to (viii) to paragraph 39(1)(f) of the ITA



ENTERTAINMENT EXPENSE

INLAND REVENUE BOARD MALAYSIA

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No	Types of entertainment	Allowed a deduction of		Not allowed a deduction of		ITA Provision
		100%	50%	100%	50%	
						the ITA
13	Hampers for customers during festive seasons		_ /		_ /	Not included under provisos (i) to (viii) to paragraph 39(1)(l) of the ITA

10. Tax payers are required to keep records in respect of entertainment expense incurred.
11. This Ruling is effective from the year of assessment 2008 and subsequent years of assessment. This Ruling supersedes Public Ruling No. 3/2004 issued on 8 November 2004 and Addendum to Public Ruling No. 3/2004 issued on 23 August 2007.

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