Limited Liability Partnership

1

Limited Liability Partnership(LLP)

- Accounts are not required to be audited and the Company secretary is not required
- Partners and LLP are separate legal entities and end with 'PLT'
- LLP can be sued on its own capacity
- Partners will be assessed under Section 4(b) on employment income
- LLP will be given deduction for such remuneration provided it is stated under the LLP agreement
- Basis period can be 31.12 or non 31.12

2

Limited Liability Partnership(LLP

- Income from an LLP will be taxed at LLP level
- Definition of "person' includes PLT->Provisions of ITA, exemption orders and income tax rules applicable but not specific incentives provided to a company

Limited Liability Partnership(LLP)

	Deductible	**Non deductible**
Restriction on partner's salary deduction	Basic salary & fixed allowances	EPF, SOSCO, insurance in general
	Must be documented in the LLP agreement as evidence	Not specified or provided for in the LLP agreement
Incorporation expenses	Capital contribution ≤ RM2.5million	

Eg 49.2 pg 526

Conventional Partnership & LLP

	Conventional P/ship	LLP
Interest income	Taxed at the respective partners' level, aggregated together with their share of divisible income and constitute the adjusted income of the partner from the partnership business	Taxed at LLP
Partners' salaries	Taxed at the respective partners' level, aggregated together with their share of divisible income and constitute the adjusted income of the partner from the partnership business	Allowed as deduction when arriving at LLP's CI to the extent provided under the LLP agreement . Employment income for the partners
Distribution of profits Eg 49.3 pg 529	Share of divisible income =share of p/ship profits to be taxed at partners' level	Paid at LLP's level Subsequent distribution = exempt from income tax

Conversion to LLP

- **Company to LLP**

  ->all the shareholders of the SB are also the partner of LLP

  ->the assets of the SB are not subject to any charge at the time of conversion.

  Transfer of assets = control transfer

Unabsorbed CA/Losses= allowed to be carry to LLP and deducted in arriving at the AI for a YA following the relevant year of conversion.

Sep/Dec 2021 Q(1)(a),comparison between Co & partnership

Conversion from P/ship to Co

7 December 2021

1. Three years ago, college friends Ali, Anand and Ah Lian started an equal partnership business, MurahBestMost (MBM), to provide takeaway and delivery of whole food meals in the Klang Valley, Malaysia. Their mission is to make tasty nutritious food widely available so that '*Everyone can eat well!*'
2. The partners are now ready to expand their business to the rest of Malaysia by setting up branches progressively in every state.
3. Ali, Anand and Ah Lian have foregone remuneration in the past three years, but going forward, they hope to be able to draw a fixed salary each. MBM does not have many assets as the partners have been operating out of their parents' homes.
4. The partners are now considering whether to incorporate a company to replace the partnership and, assuming a company is incorporated, how to go about the expansion:
   - Whether to have a single company for all the branches including Klang Valley, or
   - One company for Klang Valley and one company for each state which will hold the branch business for that state.

   Initial costs of setting up each branch will be minimal and each branch is expected to be profitable from the start of operation.
5. In future, some of the branches outside Klang Valley may be sold, but the Klang Valley operation is likely to be retained.
6. As the partners do not intend to tie up capital in real property, they plan to rent premises for all their operations.

Conversion from P/ship to Co

7. They also plan to set up:
   - A well-equipped central kitchen under the Klang Valley operation at a cost of RM1·7 million;
   - A management company to manage finance, accounting and human resource functions at a fee based on time-cost; and
   - A holding company to hold all the companies and to receive dividends from them.

   The three partners think there is potential for the central kitchen to take on other ventures in future.
8. At every outlet, including the Klang Valley operation, there will be a counter to serve free meals to the homeless and the poor.

7 December 2021

Please prepare a report for our new client, MurahBestMost (MBM). The report should address the following issues:

Conversion from P/ship to Co

Please prepare a report for our new client, MurahBestMost (MBM). The report should address the following issues:

(a) **From partnership to company**

(i) Explain the differences between a partnership and a limited liability company from the perspective of:

- The personal liability of each partner or director-shareholder;
- The tax deductibility for the business of remuneration and contributions to the Employees' Provident Fund in respect of the partners or director-shareholders;
- The taxability of remuneration paid in the hands of the partners or director-shareholders; and
- The taxability of the profits distributed in the hands of the partners or director-shareholders.

You should present your analysis in a table format in an appendix.

(ii) Based on your analysis above, explain why MBM should incorporate a new limited liability company to take over the partnership business.

Conversion from P/ship to Company

1 **Report to MurahBestMost**

From Tax Firm
To Partners, MurahBestMost
Date 8 December 2021

Expansion of MurahBestMost (MBM) business

We refer to our meeting on 7 December 2021, and your request for our assistance in respect of the proposed expansion of MBM's business from the Klang Valley to the rest of Malaysia. We have identified the tax issues MBM should be mindful of and have made recommendations as to your next steps.

(a) **From partnership to company**

We note that in the past three years, the partnership of Ali, Anand and Ah Lian under MBM has been operating the business of whole food meals for takeaway and delivery. You have done well in the Klang Valley; and now you are ready for expansion to the rest of Malaysia.

You are considering incorporating a company to replace the partnership.

We have explained below the reasons why MBM should incorporate a new limited company to take over the partnership business.

Under a company structure:

- each shareholder has a limited personal liability, except for the director's personal liability for the company's tax,
- remuneration paid to a director-shareholder is tax deductible for the company although taxable in a director-shareholder's hands,
- the Employee Provident Fund (EPF) contributions are deductible for the company and not taxable on the director-shareholder, and
- dividends distributed to a director-shareholder are tax exempt.

To support our advice, we have appended a table at appendix A showing the differences between a partnership and a limited liability company in respect of the above aspects.

Conversion from P/ship to Company

b) One company for each state

Assuming some of the branches outside Klang Valley will be sold in future, briefly explain:

- Why it is preferable to incorporate a company to hold the branch business in each state, rather than incorporate a single company for all the branches.
- The tax treatment of the gains arising on the future sale of the shares in these state companies compared with a sale of assets under a single company, branches structure.

(b) One company for each state

- In view of the likelihood of disposing of the branches in the other states of Malaysia, it is advisable to hold each branch operation under a separate company. This will facilitate a clean exit by disposing of the shares in the particular company, rather than selling the branch business assets. It also affords the flexibility of selling the whole or part of the operation by selling 100%, 51%, or 49% of the shareholding to achieve the intended outcome.
- Another benefit is that each company can potentially avail of the dual tax rate regime.
- Selling business assets will invariably lead to balancing adjustments where capital allowances have been claimed, while selling of shares has no income tax exposure, neither will there be real property gains tax as the companies will not be real property companies.

Conversion from P/ship to Company

Appendix A

Comparison of partnership and company

	Partnership	Company
Personal liability.	Unlimited liability.	Limited to the share of equity, except for the director's liability for the company's tax.
Deductibility of remuneration and EPF contributions for partners or director-shareholders.	The partnership is not a taxable entity. The provisional adjusted income relating to each partner is taxable in the partner's name. Remuneration and EPF contributions are not deductible in arriving at the provisional adjusted income of the partner.	Remuneration and EPF contributions are fully deductible in arriving at the adjusted income of the company, which is the taxable entity.
How remuneration is treated in the hands of partners or director-shareholders.	In the hands of the partner, remuneration paid to them is treated as part of their share of profits from the partnership and is taxable in their personal capacity as business income.	In the hands of the shareholder, remuneration received by a director-shareholder is taxable as director's remuneration in their personal capacity as employment income.
How profits allocated/received are treated in hands of partners or director-shareholders.	Profit allocated to each partner, whether or not actually distributed, is taxable in the hands of the partner.	Dividends received by each shareholder are specifically exempt [paragraph 12B, Schedule 6, Income Tax Act 1967] in the hands of the shareholder.

Limited Liability Partnership(LLP) -CA

- An LLP is not entitled to claim capital allowances on assets that have been transferred during the conversion of partnership or company to the LLP if the capital allowances have been claimed by a partner or a company in the same year of assessment where changes to the entity occurs.

  Eg 6 PR 5/2015
- LLP is entitled to claim CA on the assets used in the business despite changes in the partners (Eg 14 -16, PR5/2014)

Limited Liability Partnership(LLP)

- Distribution of profits to partners are exempt from tax and no WHT on profits paid, credited or distributed to the partners
- Partners are not liable to tax on their share of income from LLP (whether distributed or not). They will be taxed on remunerations, perquisites and benefits-in-kind received from the LLP.
- Submission of tax estimate must be complied with
- Distinction between a limited liability p/ship, a p/ship and a company – pg 5 of PR5/2015

June 2022 Q4(a)(i)(ii)

June 2022 Q4(a)(i)(ii)

- The limited liability partnership (LLP) agreement of RSH PLT has the following terms:
  - It was agreed that each partner would contribute RM800,000 to the LLP. Randhill and Sue each contributed RM800,000 in cash while Hanita contributed an office lot to be used as the office premises. The market value of the office lot was RM1 million. No interest is payable on the capital contributions.
  - Each partner is entitled to an equal distribution of RSH PLT's profits.
  - All partners are paid a fixed salary of RM120,000 annually. Hanita is provided with a new passenger car costing RM200,000.
- RSH PLT will close its accounts to 30 April annually. For its first financial year of 1 May 2022 to 30 April 2023, RSH PLT is projected to be profitable with an estimated revenue of RM2 million.
- Hanita is tax resident in Malaysia while both Randhill and Sue are tax resident in Singapore. All partners' meetings are to be held in Malaysia.
- Verbally, it has been agreed that where a partner wins a court case, the partner will receive a special allowance of RM20,000 from RSH PLT.
- On 1 June 2022, Sue transferred four used laptops from her previous sole proprietor legal practice into RSH PLT for a consideration of RM10,000. The laptops were acquired on 1 January 2020 at a total cost of RM15,000.

For the financial year ending 30 April 2023, RSH PLT is expected to have fees from the provision of legal services of RM2 million.

As its accounting department has spare capacity, RSH PLT will also earn accounting fees of RM100,000 from Banyak Macam Sdn Bhd (BMSB), a company in which Randhill has a substantial shareholding.

June 2022 Q4(a)(i)(ii)

4 (a) **Income tax treatment of RSH PLT**

(i) **Taxable person, residence status and how RSH PLT's profits are to be taxed**

RSH PLT is a limited liability partnership (LLP). An LLP is regarded as a taxable person and, therefore, the profits derived by the LLP are taxed at the LLP level.

In determining the residence status of RSH PLT, the tax residence status of the partners is not relevant. The residence status of the LLP is determined based on where the management and control of the business are being exercised. Management and control refer to the authority in deciding policies to be followed by the LLP and are considered to be exercised in the place where the partners meet to discuss management of the business of the LLP. As all the partners' meetings are to be held in Malaysia, RSH PLT should be a tax resident in Malaysia.

First basis period of RSH PLT, submission of tax estimates and tax instalments

The basis period of RSH PLT will be based on its accounting period. As RSH PLT commenced its business on 1 May 2022 and will close its accounts on 30 April 2023, the first basis period will be from 1 May 2022 to 30 April 2023.

June 2022 Q4(a)(i)(ii)

As a taxable person, RSH PLT is required to submit its first tax estimate within three months from the commencement of operation, i.e. by 31 July 2022. The first tax instalment will be payable in the sixth month of the basis period, by 15 October 2022, followed by 11 monthly instalments thereafter until September 2023.

Applicable tax rate

As a resident LLP, the applicable tax rate would depend on whether RSH PLT can meet the small and medium enterprise (SME) definition to qualify for a preferential tax rate. This would depend on whether the total capital contribution of the LLP exceeds RM2·5 million. For RSH PLT, each partner is required to make a capital contribution of RM0·8 million, giving a total of RM2·4 million (RM0·8 million x 3). However, in the case of Hanita's contribution via transfer of property, the market value of the property of RM1 million should be used instead. If the value of the capital contribution of Hanita is substituted with the market value of the property, the total contribution of the LLP would be RM2·6 million ((RM0·8 million x 2) + RM1 million). In which case, it cannot avail of the preferential tax rate under SME. Hence, the applicable tax rate would be 24%.

June 2022 Q4(a)(i)(ii)

(ii) **Tax treatment of arrangements between partners and RSH PLT**

Capital contribution

The capital contribution is a capital transaction and, therefore, should not have income tax implications for either the partners or RSH PLT.

Profit distribution

The profits paid, credited or distributed to partners of the LLP are exempt from income tax. There is no withholding tax on the profit distribution.

From RSH PLT's perspective, the profit distribution is not a tax deductible expense.

Fixed salary to partners

The fixed salary payable to partners which is stipulated in the LLP agreement should be an allowed tax deduction against the business profits of RSH PLT.

The salary will be taxed as employment income of the partners.

New passenger car provided to Hanita

As this is a benefit-in-kind provided to the partner, RSH PLT will be eligible to claim capital allowance restricted to qualifying expenditure of RM50,000, being a non-commercial motor vehicle.

Tutorial note: *The applicable initial and annual allowance rates of 20% each are available.*

Hanita will be subject to tax on the car benefit, being a benefit-in-kind which forms part of her employment income.

Special allowance

The special allowance given to the partners on the successful win of court cases is a verbal agreement not stipulated in the LLP agreement. In this case, the special allowance payable would not be eligible for a tax deduction at the LLP level.

Notwithstanding that the special allowance is not tax deductible, it would still be regarded as part of the taxable employment income of the partners.

Transfer of laptops from Sue

As Sue is only entitled to one-third of the profit distribution of RSH PLT, Sue cannot be said to have control over it. Therefore, the controlled transfer provisions are not applicable. RSH PLT will be able to claim capital allowances based on the purchase consideration of the laptop of RM10,000 at an accelerated initial and annual allowance of 20% each.

For Sue, in relation to her sole proprietorship business, she would need to compute balancing adjustments in relation to the disposal of the laptops.