

Technical e-Newsletter

May 2007 Issue

COMPLIANCE CHECKLISTS & SAMPLE DISCLOSURE NOTES

FRS 117 *Leases*

FRS 124 *Related Party Disclosures*

TECHNICAL DIAGNOSTIC CENTRE

Recognition of Website Development Costs and its Income Tax Treatment

A Monthly e-Newsletter published by the Technical Support Unit of AXP Solutions Sdn. Bhd. (693866-X)



www.myAXP.com

Editors' Notes ~ Leasehold Land ≠ PPE ?

Greetings!!

In this issue of the e-Newsletter, we look into two FRSs which were effective for the annual period beginning on or after 1 October 2006, i.e., **FRS 117** – Leases and **FRS 124** – Related Party Transactions.

One of the most notable changes in FRS 117 is the re-definition of the classification of leases. As a result, leasehold land (*which title does not normally transfer to the lessee by the end of the lease term*) can no longer be classified as “property, plant and equipment”, it shall be classified as “Prepaid lease rental”. However, it is still presented under non-current assets (if the lease is not expired within one year).

Similarly, the proposed Malaysian PERS has the similar clause for the classification of leasehold land. I believe that leasehold land has been classified as “fixed assets” or “property, plant and equipment” since day one. It may be very difficult for the auditors to explain to their clients, especially SMEs, that their leasehold land is not their “fixed assets” anymore.

On the other hand, additional procedures are included in identifying related party disclosure for the FRS 124 as compared to FRS 124₂₀₀₄.

In this month's Technical Diagnostic Centre, we have analysed the financial reporting and income tax treatment for the recognition of website development costs, as the cost of developing and maintaining an entity's website is increasingly important as internet and e-commerce have become more common.

The Compliance Checklists and the Sample Notes to the Financial Statements illustrated in this e-Newsletter are also available in Microsoft Word and Excel. Please feel free to contact us at support@myAXP.com if you wish to obtain these complimentary copies.

Happy reading!

Editors
AXP Technical e-Newsletter
May 2007

Contents

FINANCIAL REPORTING STANDARDS

1 *Sample notes to the financial statements complying with FRS 117 & 124*

FRS 117 Leases

6 *Part I – Summary of Changes*

8 *Part II – Sample Compliance Checklist*

FRS 124 Related Party Disclosure

21 *Part I – Summary of Changes*

23 *Part II – Sample Compliance Checklist*

27 AXP TECHNICAL DIAGNOSTIC CENTRE

27 *Recognition of Website Development Costs and its Income Tax Treatment*

Circulation Notice

AXP Technical e-Newsletter is distributed to AXP's clients and selected accounting and audit practitioners in Malaysia. The views in this e-Newsletter do not necessarily represent those of AXP's. Whilst every effort has been made to ensure accuracy, the extracted compliance checklists and Sample Financial Statements in this e-Newsletter do not necessarily reflect full compliance with FRSs. You are advised not to rely solely on this e-Newsletter.

Contributions & Comments

AXP Technical e-Newsletter welcomes your contributions on contemporary issues encountered by the profession. We also wish to hear from you on how this e-Newsletter can be improved for more timely and useful information. Your contributions or comments may be sent directly to us at:

AXP Technical Support Unit

Corporate Headquarters

83A, Jalan Emas Satu, Taman Sri Skudai, 81300 Johor Bahru, Johor.

Tel: 1300 882 AXP (1300 882 297) Fax: 07-557 7697

Central Malaysia

C-2-16, SME Technopreneur Centre Cyberjaya, 2270, Jalan Usahawan 2, 63000 Cyberjaya, Selangor.

Tel: 1300 882 AXP (1300 882 297) Fax: 03-8315 6198

Singapore

1, Science Centre Road, #09-38 The Enterprise, Singapore 609077.

Tel: 65-6565 0852 Fax: 65-6565 1880

support@myAXP.com
www.myAXP.com

Johor Bahru ♦ Cyberjaya ♦ Singapore

© Copyright 2007 AXP Solutions Sdn. Bhd.

SAMPLE NOTES TO THE FINANCIAL STATEMENTS

COMPLYING WITH *FRS 117 & 124*



EXTRACTS OF NOTES TO THE FINANCIAL STATEMENTS:

1. GENERAL INFORMATION

- 101.126(a) The Company is a public limited company incorporated in Malaysia and listed on the Main Board of the Bursa Malaysia and the Alternative Investment Market (AIM) of the London Stock Exchange. The registered office and principal place of business is located at 83A, Jalan Emas 1, Taman Sri Skudai, 81300 Johor Bahru, Johor.
- 101.126(b) The principal activities of the Company are that of investment holding and provision of management services to its subsidiaries. The principal activities of the subsidiaries are described in Note 10. There have been no significant changes in the nature of the activities during the financial year.
- 101.126(c) The Company is a subsidiary of Be Competent Sdn. Bhd., a company incorporated in Malaysia, which is also regarded by the directors as the ultimate holding company of the Company.
- 124.12**
- 121.8 The financial statements of each entity in the Group are presented in the functional currency, which is the currency of the primary economic environment in which the entity operates. The functional currency of the Company is Ringgit Malaysia (RM) as the sales and purchases are mainly denominated in RM and receipts from operations are usually retained in RM and funds from financing activities are generated in RM. For the purpose of the consolidated financial statements, the results and financial position of each entity are expressed in Ringgit Malaysia, which is the functional currency of the Company, and the presentation currency for the consolidated financial statements.

2. ADOPTION OF NEW AND REVISED FINANCIAL REPORTING STANDARDS (EXTRACT)

In addition, the Group and the Company have adopted FRS 117 Leases and FRS 124 Related Party Disclosures in advance, which are effective for annual periods beginning on or after 1 October 2006. However, the adoption of these FRSs does not have significant impact on the financial statements of the Group and the Company.

3. SIGNIFICANT ACCOUNTING POLICIES (EXTRACT)

Hire Purchase and Finance Lease Payables

- 117.8** Hire purchase and leases of property, plant and equipment, which are classified as finance lease, where substantially all the risks and benefits incidental to the ownership of the assets, but not the legal ownership, are transferred to the Group and the Company.
- 117.27** Assets under hire purchase and finance lease are depreciated on a straight-line basis over the shorter of the hire and lease terms or their useful lives. Hire purchase and lease interest is recognised as an expense in profit or loss over the lease period so as to give a constant periodic rate of interest on the outstanding liability at the end of each accounting period.
- 117.33** All other leases are classified as operating lease and the lease rentals are recognised as an expense in profit or loss on a straight-line basis over the lease periods.

5. PROPERTY, PLANT AND EQUIPMENT (EXTRACT)

116.74(a) The carrying amounts of the property, plant and equipment under hire purchase and finance lease
117.31(a) of the Group and the Company are as follows:

	THE GROUP		THE COMPANY	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Plant and machinery				
Motor vehicles				

132.60(a) **17. TRADE AND OTHER RECEIVABLES (EXTRACT)**

	THE GROUP		THE COMPANY	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
101.74 Trade receivables				
Less: Allowance for doubtful debts				
Net trade receivables				
101.74 Other receivables, deposits and prepayments:				
- Other receivables				
- Deposits				
- Prepayments				
101.74, Amounts due from subsidiaries:				
124.17(b) - trade nature				
- non-trade nature and unsecured				
124.17(c) - Less: Allowance for doubtful debts				

132.60(a) **22. TRADE AND OTHER PAYABLES (EXTRACT)**

	THE GROUP		THE COMPANY	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
101.74 Trade payables				
101.74 Other payables and accruals:				
- Other payables				
- Accruals				
111.41(b) - Advances received from contract customers				
101.74, Amounts due to subsidiaries:				
124.17(b) - trade nature				
- non-trade nature and unsecured				

24. HIRE PURCHASE AND FINANCE LEASE PAYABLES (EXTRACT)

	THE GROUP		THE COMPANY	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
117.31(b) Minimum lease payments				
- not later than 1 year				
- later than 1 year and not later than 5 years				
- later than 5 years				
Future finance charges				
Present value of hire purchase and finance lease payables				

	THE GROUP		THE COMPANY	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
117.31(b) Present value of hire purchase and finance lease payables is analysed as follows:				
- not later than 1 year				
- later than 1 year and not later than 5 years				
- later than 5 years				

117.31(e) The Group obtains finance lease and hire purchase facilities to finance certain of its plant and machinery and motor vehicles. The average remaining lease term is 3 years as at 31 December 2006. Implicit interest rate of the finance lease and hire purchase are fixed at the date of the agreement, and the amount of lease payments are fixed throughout the lease period. The Group has the option to purchase the assets at the end of the agreement with minimum purchase considerations. There is no significant restriction clauses imposed by lease arrangements.

36. PROFIT BEFORE TAX (EXTRACT)

a) Profit before tax is stated after charging / (crediting):-

	THE GROUP		THE COMPANY	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Allowance for doubtful debts				
- related parties				
124.17(d) - other than related parties				
117.31(c) Contingent rents				

CA-9-1(o) **124.16** Employees benefit expenses including the following remunerations paid to the directors, who are also the key management personnel, of the Company:

	THE GROUP		THE COMPANY	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Salaries, bonus and allowances				
Directors' fees				
Contribution to defined contribution plan				
Other emoluments and benefits				

124.17(a) 44. RELATED PARTY TRANSACTIONS

THE GROUP		THE COMPANY	
2006	2005	2006	2005
RM'000	RM'000	RM'000	RM'000

124.18(a) Holding Company
Dividend paid to Be Competent Sdn. Bhd.

124.18(c) Subsidiaries
Dividend income from AE R & D Sdn. Bhd.
Property rental income from AXP Holdings Sdn. Bhd.
Management fee income from:
 AXP Land Sdn. Bhd.
 AXP Property Sdn. Bhd.
 AXP Building Sdn. Bhd.

124.18(g) Companies in which directors of the Company have interests
Sales of goods to SLT Sdn. Bhd. (*Ser L. T. is a substantial shareholder and director*)
Licence fee income from Ran Brothers Sdn. Bhd. (*Ran H. P. and persons related to him are shareholders and directors*)
Property rental income from:
 LKK Holdings Sdn. Bhd. (*Lian K. K. is a substantial shareholder and director*)
 LT & JQ Sdn. Bhd. (*Ser L. T. and Gi J. Q. are shareholders and directors*)

124.21 The directors are of the opinion that all the transactions above have been entered into in the normal course of business and have been established on terms and conditions that are not materially different from that obtainable in transactions with unrelated parties.

49. LEASE COMMITMENT

117.35(a) & (d) The total minimum lease payments under non-cancellable operating leases of the Group for the leasing of certain of the office premises, with an average lease term of 8 years, is as follows:

THE GROUP		THE COMPANY	
2006	2005	2006	2005
RM'000	RM'000	RM'000	RM'000

Within one year
Later than one year and not later than five years
Later than five years

FRS 117 LEASES

PART I - SUMMARY OF CHANGES

WHAT'S NEW?

Scope

- ✚ It requires the finance lease accounting methodology set out in FRS 117 to be used for investment properties held under leases.

Classification of Leases

- ✚ Consider the land and buildings elements separately when classifying a lease of land and buildings.
 - ✓ Minimum lease payments are allocated between the land and buildings elements in proportion to the relative fair values of the leasehold interests in the land and buildings elements of the lease.
 - ✓ Land element → normally classified as an operating lease **UNLESS** title passes to the lessee at the end of the lease term.
 - ✓ Buildings element → classified as operating or finance lease by applying the classification criteria in FRS 117.

Initial Direct Costs

- ✚ Lessors (*except for manufacturing or dealer lessors*) include in the initial measurement of finance lease receivables the initial direct costs incurred in negotiating a lease.
- ✚ Manufacturing or dealer lessors recognise costs of this type as an expense when the selling profit is recognized.
- ✚ Initial direct costs incurred by lessors in negotiating an operating lease → added to the carrying amount of the leased asset and recognised over the lease term on the same basis as the lease income.
- ✚ Not permit initial direct costs of lessors to be charged as expenses as incurred.

Transitional Provisions

- ✚ If an entity previously applied FRS 117₂₀₀₄ → apply the amendments made by FRS 117 retrospectively for all leases.
- ✚ If FRS 117₂₀₀₄ was not applied retrospectively → apply the amendments made by FRS 117 for all lease entered into since its first applied FRS 117₂₀₀₄.

WHAT HAVE BEEN CLARIFIED?

Definition

- ✚ Interest rate implicit in the lease → discount rate that results in the present value of the minimum lease payments and any unguaranteed residual value equalling the fair value of the leased asset plus initial direct costs of the lessor.
- ✚ Distinguish between the inception of the lease (*when leases are classified*) and the commencement of the lease term (*when recognition takes place*).
- ✚ Unearned finance income / net investment in the lease → simplified and articulated more explicitly to complement the changes relating to initial direct costs and change in the definition of the interest rate implicit in the lease.

PART II - SAMPLE COMPLIANCE CHECKLIST

REF.	COMPLIANCE CHECKLISTS	EXAMPLE / SAMPLE DISCLOSURES NOTES
117.2	<p><u>SCOPE</u></p> <p>FRS 117 shall be applied in accounting for all leases OTHER THAN:</p> <ul style="list-style-type: none"> (a) Leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources; and (b) Licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights. <p>However, FRS 117 shall not be applied as the basis of measurement for:</p> <ul style="list-style-type: none"> (a) Property held by lessees that is accounted for as investment property; (b) Investment property provided by lessors under operating leases; (c) Biological assets held by lessees under finance leases; or (d) Biological assets provided by lessors under operating leases. 	
117.4	<p><u>Lease</u></p> <p>An agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.</p> <p><u>Finance lease</u></p> <p>Lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred.</p> <p><u>Operating lease</u></p> <p>A lease other than a finance lease.</p> <p><u>Non-cancellable lease</u></p> <p>A lease that is cancellable only:</p> <ul style="list-style-type: none"> (a) Upon the occurrence of some remote contingency; (b) With the permission of the lessor; (c) If the lessee enters into a new lease for the same or an equivalent asset with the same lessor; or (d) Upon payment by the lessee of such an additional amount that, at inception of the lease, continuation of the lease is reasonably certain. <p><u>Inception of the lease</u></p> <p>The earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease.</p> <p>As at this date:</p> <ul style="list-style-type: none"> (a) A lease is classified as either an operating or a finance lease; and (b) In the case of a finance lease, the amounts to be recognised at the commencement of the lease term are determined. 	

Commencement of the lease term

The date from which the lessee is entitled to exercise its right to use the leased asset.

The date of initial recognition of the lease.

Lease term

Non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

Minimum lease payments

The payments over the lease term that the lessee is or can be required to make, excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with:

- (a) for a lessee, any amounts guaranteed by the lessee or by a party related to the lessee; or
- (b) for a lessor, any residual value guaranteed to the lessor by:
 - (i) the lessee;
 - (ii) a party related to the lessee; or
 - (iii) a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.

If the lessee has an option to purchase the asset at a price that is expected to be sufficiently lower than fair value at the date the option becomes exercisable for it to be reasonably certain → at the inception of the lease, that the option will be exercised, the minimum lease payments comprise the minimum payments payable over the lease term to the expected date of exercise of this purchase option and the payment required to exercise it.

Fair value

Amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Economic life

Either:

- (a) the period over which an asset is expected to be economically usable by one or more users; or
- (b) the number of production or similar units expected to be obtained from the asset by one or more users.

Useful life

The estimated remaining period, from the commencement of the lease term, without limitation by the lease term, over which the economic benefits embodied in the asset are expected to be consumed by the entity.

Guaranteed residual value

- (a) for a lessee → that part of the residual value that is guaranteed by the lessee or by a party related to the lessee; and
- (b) for a lessor → that part of the residual value that is guaranteed by the lessee or by a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.

Unguaranteed residual value

That portion of the residual value of the leased asset, the realization of which by the lessor is not assured or is guaranteed solely by a party related to the lessor.

	<p><u>Initial direct costs</u> Incremental costs that are directly attributable to negotiating and arranging a lease, except for such costs incurred by manufacturer or dealer lessors.</p> <p><u>Gross investment in the lease</u> The aggregate of: (a) minimum lease payments receivable by the lessor under a finance lease, and (b) any unguaranteed residual value accruing to the lessor.</p> <p><u>Net investment in the lease</u> Gross investment in the lease discounted at the interest rate implicit in the lease.</p> <p><u>Unearned finance income</u> Difference between: (a) gross investment in the lease, and (b) net investment in the lease.</p> <p><u>Interest rate implicit in the lease</u> Discount rate that, at the inception of the lease, causes the aggregate present value of: (a) minimum lease payments, and (b) unguaranteed residual value to be equal to the sum of : (i) fair value of the leased asset, and (ii) any initial direct costs of the lessor.</p> <p><u>Lessee’s incremental borrowing rate of interest</u> Rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset.</p> <p><u>Contingent rent</u> That portion of the lease payments that is not fixed in amount but is based on the future amount of a factor that changes other than with the passage of time.</p>
	<p><u>CLASSIFICATION OF LEASES</u></p>
117.7	<p>Based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee.</p> <p>Risk → possibilities of losses from idle capacity or technological obsolescence and of variations in return because of changing economic conditions.</p> <p>Rewards → may be represented by the expectation of profitable operation over the asset’s economic life and of gain from appreciation in value or realization of a residual value.</p>

<p>117.8, 10 - 19</p>	<p>A lease is classified as a finance lease → if it transfers substantially all the risks and rewards incidental to ownership.</p> <p>A lease is classified as an operating lease → if it does not transfer substantially all the risks and rewards incidental to ownership.</p>	<p>Whether a lease is a finance lease or an operating lease → depends on the substance of the transaction rather than the form of the contract.</p> <p><i>Example of situations lead to a lease being classified as a finance lease:</i></p> <ul style="list-style-type: none"> (a) lease transfers ownership of the asset to the lessee by the end of the leased term; (b) lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised; (c) lease term is for the major part of the economic life of the asset even if title is not transferred; (d) at the inception of the lease, the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset; and (e) lease assets are of such a specialized nature that only the lessee can use them without major modifications. <p><i>Indicators of situations lead to a lease being classified as a finance lease:</i></p> <ul style="list-style-type: none"> (a) if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee; (b) gains or losses from the fluctuation in the fair value of the residual accrue to the lessee; and (c) lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent. <p>The above lists are not conclusive. If other features that the lease does not transfer substantially all risks and rewards incidental to ownership → classified as operating lease.</p> <p><u>Change of provisions of the lease other than by renewing the lease</u></p> <p>If the provisions are changed in a manner that would have resulted in a different classification of the lease if the changed terms had been in effect at the inception of the lease → regarded as a new agreement over its term.</p> <p>Changes in estimates or circumstances → do NOT give rise to a new classification of a lease for accounting purposes.</p> <p><u>Leases of land and buildings</u></p> <p>Lease of land and buildings, considered separately, are classified as operating or finance leases in the same way as leases of other assets.</p> <p>Characteristic of land → has an indefinite economic life and, if title is not</p>
---------------------------	--	--

expected to pass to the lessee by the end of the lease term → lessee normally does not receive substantially all of the risks and rewards incidental to ownership → OPERATING LEASE.

→ prepaid lease payments that are amortised over the lease term.

If title to both elements is expected to pass to the lessee by the end of the lease term → BOTH elements are classified as a finance lease, UNLESS it is clear from other features that the lease does NOT transfer substantially all risks and rewards incidental to ownership of one or both elements.

When the land has an indefinite economic life → normally classified as an operating lease UNLESS title is expected to pass to the lessee by the end of the lease term.

Minimum lease payments of lease of land and buildings

Allocated between the land and buildings elements in proportion to the relative fair value of the leasehold interest in the land element and building element of the lease at the inception of the lease.

If the lease payments CANNOT be allocated reliably between two elements → entire lease is classified as a finance lease UNLESS it is clear that both elements are operating leases → entire lease is classified as an operating lease.

Amount of land element is immaterial

Lease of land and buildings in which the amount that would initially be recognised for the land element is IMMATERIAL → land and buildings may be treated as a single unit for the purpose of lease classification and classified as a finance or operating lease → economic life of the buildings is regarded as the economic life of the entire leased asset.

Lessee's interest classified as an investment property and adopt fair value method

→ Separate measurement is NOT required.

Detailed calculations are required for this assessment ONLY IF the classification of one or both elements is otherwise uncertain.

Classify a property interest held under an operating lease as an investment property → accounted for as if it were a finance lease and the fair value model is used for the asset recognized.

		<p>Lessee shall continue to account for the lease as a finance lease, EVEN IF a subsequent event changes the nature of the lessee’s property interest so that it is no longer classified as investment property,</p> <p><i>Example, the lessee:</i></p> <p>(a) occupies the property, which is then transferred to owner-occupied property at a deemed cost equal to its fair value at the date of change in use; or</p> <p>(b) grants a sublease that transfer substantially all of the risks and rewards incidental to ownership of the interest to an unrelated third party → accounted for by the lessee as a finance lease to the third party, although it may be accounted for as an operating lease by the third party.</p>
<p>117.20 ~ 24</p>	<p><u>FINANCE LEASES IN THE FINANCIAL STATEMENTS OF LESSEES ~ Initial Recognition</u></p> <p>At the commencement of the lease term, lessees shall recognise finance leases as assets and liabilities in their balance sheets at amounts equal to the -</p> <ul style="list-style-type: none"> ✓ fair value of the leased property, or ✓ if lower, the present value of the minimum lease payments each determined at the inception of the lease. <p>Discount rate to be used in calculating the present value of the minimum lease payments -</p> <ul style="list-style-type: none"> ✓ if this is practicable → interest rate implicit in the lease; ✓ if this is not practicable → lessee’s incremental borrowing rate. <p>Any initial direct costs of the lessee are added to the amount recognised as an asset.</p>	<p><u>Substance over legal form</u></p> <p>Finance lease</p> <ul style="list-style-type: none"> → legal form – lessee may acquire no legal title to the leased asset → substance and financial reality → lessee acquires to economic benefits of the use of the leased asset for the major part of its economic life in return for entering into an obligation to pay for that right an amount approximating, at the inception of the lease, the fair value of the asset and the related finance charge. <p><u>Amounts to be recognised</u></p> <p>At the commencement of lease term → asset and liability for the future lease payments are recognised in the balance sheet at the same amounts EXCEPT FOR any initial direct costs of the lessee that are added to the amount recognised as an asset.</p> <p>Liabilities of leased assets → not appropriate to be presented in the financial statements as a deduction from the leased assets.</p>
<p>117.25 ~ 26</p>	<p><u>FINANCE LEASES IN THE FINANCIAL STATEMENTS OF LESSEES ~ Subsequent Measurement</u></p> <p>Minimum lease payments → apportioned BETWEEN the finance charge AND the reduction of the outstanding liabilities.</p> <p>Finance charge → allocated to each period during the lease term so as to produce a</p>	<p>In allocating the finance charge to periods during the lease term, a lessee may use some form of approximation to simplify the calculation.</p>

	<p>constant periodic rate of interest on the remaining balance of the liability.</p> <p>Contingent rents → charged as expenses in the periods in which they are related.</p>	
117.27, 29 ~ 30	<p>A finance lease gives rise to depreciation expense for depreciable assets as well as finance expense for each accounting period.</p> <p>Depreciation policy depreciable leased assets → consistent with that for depreciable assets that are owned. Depreciation recognised shall be calculated in accordance with FRS 116 & FRS 138.</p> <p>If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term → fully depreciated over the SHORTER of the lease term AND its useful life.</p>	<p>The sum of the depreciation expense for the asset and the finance expense for the period is rarely the same as the lease payments payable for the period → it is inappropriate simply to recognise the lease payments payable as an expense.</p> <p>Asset and the related liability are unlikely to be equal in amount after the commencement of the lease term.</p> <p>Applies FRS 138 to determine whether a leased asset has become impaired.</p>
117.31 ~32	<p>In addition to the requirements of FRS 132, lessees shall disclose:</p> <ul style="list-style-type: none"> (a) The net carrying amount at the balance sheet date for each class of asset; (b) A reconciliation between the total of future minimum lease payments at the balance sheet date, and their present value. In addition, the total of future minimum lease payments at the balance sheet date, and their present value, for each of the following periods: <ul style="list-style-type: none"> (i) not later than 1 year; (ii) later than 1 year and not later than 5 years; and (iii) later than 5 years. (c) Contingent rents recognised as an expense in the period. (d) Total of future minimum sublease payments expected to be received under non-cancellable subleases at the balance sheet date. (e) A general description of the lessee's material leasing arrangements including, but not limited to, the following: <ul style="list-style-type: none"> (i) Basis on which contingent rent payable is determined; (ii) Existence and terms of renewal or purchase options and escalation clauses; and (iii) Restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing. <p>In addition, the disclosure requirements in accordance with FRS 116, 136, 138, 140 and IAS 41 apply to lessees for assets leased under finance leases.</p>	
	<u>OPERATING LEASES IN THE FINANCIAL STATEMENTS OF LESSEES</u>	

117.33	Lease payments under an operating lease → recognise as an expense on a straight-line basis over the lease term UNLESS another systematic basis is more representative of the time pattern of the user's benefit.
117.35	<p>Lessees shall disclose:</p> <ul style="list-style-type: none"> (a) Total of future minimum lease payments under non-cancellable operating leases for each of the following periods: <ul style="list-style-type: none"> (i) Not later than 1 year; (ii) Later than 1 year and not later than 5 years; and (iii) Later than 5 years. (b) Total of future minimum sublease payments expected to be received under non-cancellable subleases at the balance sheet date. (c) Lease and sublease payments recognised as an expense in the period, with separate amounts for minimum lease payments, contingent rents, and sublease payments. (d) General description of the lessee's significant leasing arrangement including, but not limited to, the following: <ul style="list-style-type: none"> (i) Basis on which contingent rent payable is determined; (ii) Existence and terms of renewal or purchase options and escalation clauses; and (iii) Restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing.
<p><u>FINANCE LEASES IN THE FINANCIAL STATEMENTS OF LESSORS - Initial Recognition</u></p>	
117.36	<p>Lessors shall recognise assets held under a finance lease in their balance sheets and present them as a receivable at an amount equal to the net investment in the lease.</p> <p><u>Recognition of lease payment receivable</u> Lease payment receivable is treated by the lessor as repayment of principal and finance income to reimburse and reward the lessor for its investment and services.</p> <p><u>Initial direct costs</u> Initial direct costs are often incurred by lessors and include amounts that are incremental and directly attributable to negotiating and arranging a lease. They exclude general overheads.</p> <p>For finance leases other than those involving manufacturer or dealer lessors, initial direct costs are included in the initial measurement of the finance lease receivable and reduce the amount of income recognised over the lease term.</p> <p>Interest rate implicit in the lease → initial direct costs are included automatically in the finance lease receivable; there is no need to add them separately.</p>

		Costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease → excluded from the definition of initial direct costs → excluded from the net investment in the lease and are recognised as an expense when the selling profit is recognised (normally at the commencement of the lease term).
	<u>FINANCE LEASES IN THE FINANCIAL STATEMENTS OF LESSORS - Subsequent Measurement</u>	
117.39 ~ 41A	Recognition of finance income → based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease.	<p>Lease payments relating to the period (excluding costs for services) are applied against the gross investment in the lease to reduce both the principal and the unearned finance income.</p> <p>Estimated guaranteed residual values used in computing the lessor's gross investment in a lease are reviewed regularly.</p> <p>Reduction in the estimated unguaranteed residual value → income allocating over the lease term is revised and any reduction in respect of amounts accrued is recognised immediately.</p> <p>Asset under a finance lease (classified as held for sale or included in a disposal group that is classified as held for sale) → accounted for in accordance with FRS 5.</p>
117.42 ~ 46	<p>Manufacturer or dealer lessors → recognise selling profit or loss in the period, in accordance with the policy followed by the entity for outright sales.</p> <p>If artificially low rates of interest are quoted → selling profit shall be restricted to that which would apply if a market rate of interest were charged.</p> <p>Costs incurred in connection with negotiating and arranging a lease → recognised as an expense when the selling profit is recognized.</p>	<p>A finance lease of an asset by a manufacturer or dealer lessor gives rise to two types of income:</p> <p>(a) Profit or loss equivalent to the profit or loss resulting from an outright sale of the asset being leased, at normal selling prices, reflecting any applicable volume or trade discounts; and</p> <p>(b) Finance income over the lease term.</p> <p><u>Sales revenue recognised at the commencement of the lease term</u></p> <ul style="list-style-type: none"> ✓ Fair value of the asset, or, ✓ If lower, the present value of the minimum lease payments accruing to the lessor, computed at a market rate of interest. <p><u>Cost of sale recognised at the commencement of the lease term</u></p> <ul style="list-style-type: none"> ✓ Cost, or ✓ If different, carrying amount of the leased property less the present value of the unguaranteed residual value.

		<p><u>Selling profit</u> Difference between the sales revenue and the cost of sale → recognised in accordance with the policy for outright sales.</p> <p><u>Artificially low rates of interest</u></p> <ul style="list-style-type: none"> ✓ Result in an excessive portion of the total income from the transaction being recognised at the time of sale. ✓ Selling profit is restricted to that which would apply if a market rate of interest were charged. <p><u>Costs incurred in connection with negotiating and arranging a finance lease</u> Recognised as an expense at the commencement of the lease term because they are mainly related to earning the selling profit.</p>
117.47	<p>Lessors shall disclose (in addition to the requirements of FRS 132):</p> <p>(a) Reconciliation between the gross investment in the lease at the balance sheet date, and the present value of minimum lease payments receivable at the balance sheet date.</p> <p>In addition, the gross investment in the lease and the present value of minimum lease payments receivable at the balance sheet date, for each of the following period:</p> <p>(i) Not later than 1 year; (ii) Later than 1 year and not later than 5 years; (iii) Later than 5 years.</p> <p>(b) Unearned finance income. (c) Unguaranteed residual values accruing to the benefit of the lessor. (d) Accumulated allowance for uncollectible minimum lease payments receivables. (e) Contingent rates recognised as income in the period. (f) General description of the lessor’s material leasing arrangements.</p>	<p>It is often useful to disclose the gross investment less unearned income in new business added during the period, after deducting the relevant amounts for cancelled leases.</p>
	<u>OPERATING LEASES IN THE FINANCIAL STATEMENTS OF LESSORS</u>	
117.49	Lessors shall present assets subject to operating leases in their balance sheets according to the nature of the asset.	
117.50 ~ 51	<p>Lease income from operating leases → recognised in income on a straight-line basis over the lease term, UNLESS another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished.</p>	<p><u>Costs incurring in earning the lease income</u> Recognised as an expense</p> <p><u>Lease income</u> Recognised on a straight-line basis over the leased term even if the receipts are</p>

		not on such a basis.
117.52	Initial direct costs incurred by lessors in negotiating and arranging an operating lease → added to the carrying amount of the leased asset and recognised as an expense over the lease term on the same basis as the lease income.	
117.53 ~ 55	Depreciation policy for depreciable leased assets → consistent with the lessor's normal depreciation policy for similar assets, calculated in accordance with FRS 116 & 138.	Apply FRS 136 to determine whether the leased asset has become impaired. Selling profit on entering into an operating lease Not recognised → it is not the equivalent of a sale.
117.56 ~ 57	Lessors shall disclose (in addition to the requirements of FRS 132): (a) Future minimum lease payments under non-cancellable operating leases in the aggregate and for each of the following periods: (i) Not later than 1 year; (ii) Later than 1 year and not later than 5 years; (iii) Later than 5 years. (g) Total contingent rates recognised as income in the period. (h) General description of the lessor's material leasing arrangements.	In addition, the disclosure requirements in FRS 116, 136, 138, 140 and IAS 41 apply to lessors for assets provided under operating leases.
<u>SALES AND LEASEBACK TRANSACTIONS</u>		
117.58		Sales and leaseback transactions ✓ Sale of an asset and the leasing back of the same asset. ✓ Lease payment and sale price are usually interdependent since they are negotiated as a package. ✓ Accounting treatment depends on the type of lease involved.
117.59	If it results in a finance lease → any excess of sales proceeds over the carrying amount shall NOT be immediately recognised as income by a seller-lessee. Instead, it shall be deferred and amortised over the leased term.	
117.61	If it results in an operating lease, AND it is clear that the transaction is established at fair value → any profit or loss shall be recognised immediately. If the sale price is below fair value → any profit or loss shall be recognised immediately except that, if the loss is compensated for by future lease payments at below market price → deferred and amortised in proportion to the lease payments over the period for which the asset is expected to be used.	

	<p>If the sale price is above fair value → excess over fair value shall be deferred and amortised over the period for which the asset is expected to be used.</p>
117.63	<p>For operating leases, if the fair value at the time of a sale and leaseback transaction is less than the carrying amount of the asset → a loss equal to the amount of the difference between the carrying amount and fair value → recognised immediately.</p> <p>Finance lease No such adjustment UNLESS there has been an impairment in value → FRS 136.</p> <p>Disclosure requirements For lessees and lessors apply equally to sale and leaseback transactions.</p> <p>The required description of material leasing arrangements leads to disclosure of unique or unusual provisions of the agreement or terms of the sale and leaseback transactions.</p> <p>Sale and leaseback transactions may trigger the separate disclosure criteria in FRS 101.</p>
	<p><u>TRANSITIONAL PROVISIONS</u></p>
117.67	<p>Subject to FRS 117.68, retrospective application of FRS 117 is encouraged but not required.</p> <p>If FRS 117 is not applied retrospectively, the balance of any pre-existing finance lease is deemed to have been properly determined by the lessor and → accounted for thereafter in accordance with FRS 117.</p>
117.67 A	<p><u>Leasehold land previously classified as finance lease</u> Lease of land was previously classified as finance lease and had recognised the amount of prepaid lease payments as property within its property, plant and equipment → on adoption of FRS 117, treat such a lease as an operating lease, with the amortised carrying amount classified as prepaid lease payments.</p> <p><u>Leasehold land had been revalued previously</u> Retain the unamortized revalued amount as the surrogate carrying amount of prepaid lease payments → amortised over the lease term in accordance with FRS 117.33 → disclose the date of the last revaluation.</p> <p>The effect of this change shall be applied retrospectively.</p>
117.67B	<p>An entity need NOT disclose information required under FRS 108.30(b) prior to the effective date of FRS 117.</p>
117.68	<p>An entity that has previously applied FRS 117₂₀₀₄ → shall apply the amendments</p>

AXP Technical e-Newsletter - May 2007 Issue

	made by FRS 117 retrospectively for all leases If FRS 117 ₂₀₀₄ was not applied retrospectively → shall apply the amendments for all leases entered into since it first applied FRS 117 ₂₀₀₄ .
	<u>EFFECTIVE DATE</u>
117.69	Annual periods beginning on or after 1 October 2006. Earlier application is encouraged → disclose that fact.

FRS 124 RELATED PARTY DISCLOSURES

PART I - SUMMARY OF CHANGES

WHAT'S NEW?

Scope

- ✦ Requires disclosure of the compensation of key management personnel.

Definitions

- ✦ Definition of “related party” has been expanded by adding:
 - ✓ Parties with joint control over the entity; and
 - ✓ Joint ventures in which the entity is a venturer.

Disclosure

- ✦ Classification of amounts payable to, and receivable from, related parties into different categories of related parties.
- ✦ Name of the entity’s parent and, if different, the ultimate controlling party. If neither of these two parties produces financial statements available for public use, the name of the next most senior parent that does so is required.

WHAT HAVE BEEN CLARIFIED?

Definition

- ✦ Clarifies that two venturers are not related parties simply because they share joint control over a joint venture.

Disclosure

- ✦ Clarifies the disclosure requirements about:
 - ✓ Outstanding balances with related parties together with their terms and conditions including whether they are secured, and the nature of the consideration to be provided in settlement.
 - ✓ Details of any guarantees given or received.
 - ✓ Provisions for doubtful debts.
 - ✓ Settlement of liabilities on behalf of the entity or by the entity on behalf of another party.
- ✦ Clarifies the disclosures of the terms of related party transactions are equivalent to those prevail in arm’s length transactions only if such terms can be substantiated.

WHAT HAVE BEEN REMOVED?

Purpose of related party disclosures

- ✚ Removes the discussions on the pricing of transactions and related disclosures between related parties → FRS 124 not apply to the measurement of related party transactions.

PART II - SAMPLE COMPLIANCE CHECKLIST

REF.	COMPLIANCE CHECKLISTS	EXAMPLE / SAMPLE DISCLOSURES NOTES
	<u>SCOPE</u>	
124.2	FRS 124 applies to: (a) Identifying related party relationships and transactions; (b) Identifying outstanding balances between an entity and its related parties; (c) Identifying the circumstances in which disclosure of the items of (a) and (b) is required; and (d) Determining the disclosures to be made about those items.	
124.3 ~ 4	FRS 124 requires disclosure of related party transactions and outstanding balances in the separate financial statements of a parent, venturer or investor presented in accordance with FRS 127.	Transactions and balances with other entities in a group → disclosed in an entity's financial statements. Intragroup transactions and balances → eliminated in the consolidated financial statements of the group.
	<u>DEFINITIONS</u>	
124.9 ~ 11	<u>Related party</u> A party is related to an entity if: (a) Directly, or indirectly through one or more intermediaries, the party: (i) Controls, is controlled by, or is under common control with, the entity (including parents, subsidiaries and fellow subsidiaries); (ii) Has an interest in the entity that gives it significant influence over the entity; or (iii) Has joint control over the entity; (b) The party is an associate of the entity; (c) The party is a joint venture in which the entity is a venturer; (d) The party is a member of the key management personnel of the entity or its parent; (e) The party is a close member of the family of any individual referred to in (a) or (d); (f) The party is an entity that is controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or (g) The party is a post-employment benefit plan for the benefit of employees of the	The following are not necessarily related parties: (a) Two entities simply because they have a director or other member of key management personnel in common, notwithstanding 124.9 (d) and (f). (b) Two venturers simply because they share joint control over a joint venture. (c) (i) providers of finance; (ii) trade unions; (iii) public utilities; and (iv) government departments and agencies; simply by virtue of their normal dealings with an entity; and (d) a customer, supplier, franchisor, distributor or general agent with whom an entity transacts a significant volume of business, merely by virtue of the resulting economic dependence.

entity, or of any entity that is a related party of the entity.

Related party transactions

Transfer of resources, services or obligations between related parties, regardless of whether a price is charged.

Close members of the family

His or her spouse, parent, child (including adopted child and step-child), brother, sister and the spouse of his or her child, brother or sister.

Compensation

All employee benefits →

- ✓ All forms of consideration paid, payable or provided by the entity, or on behalf of the entity, in exchange for services rendered to the entity.
- ✓ Consideration paid on behalf of a parent of the entity in respect of the entity.

Compensation includes:

- (a) Short-term employee benefits;
- (b) Post-employment benefits;
- (c) Other long-term employee benefits;
- (d) Termination benefits; and
- (e) Share-based payments.

Control

Power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Joint control

Contractually agreed sharing of control over an economic activity.

Key management personnel

Those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.

Significant influence

Power to participate in the financial and operating policy decisions of an entity, but is not control over those policies. Significant influence may be gained by share ownership, statute or agreement.

DISCLOSURE

AXP Technical e-Newsletter - May 2007 Issue

124.12, 15	<p>Relationship between parents and subsidiaries → disclose irrespective of whether there have been transactions between those related parties.</p> <p>To disclose:</p> <ul style="list-style-type: none"> ✓ name of the entity's parent and, ✓ if different, the ultimate controlling party. <p>If neither the entity's parent nor the ultimate controlling party produces financial statements available for public use → to disclose the name of the next most senior parent (<i>the first parent in the group above the immediate parent that produces consolidated financial statements</i>) that does so.</p>	
124.16	<p>To disclose key management personnel compensation in TOTAL and for each of the following categories:</p> <ul style="list-style-type: none"> (a) Short-term employee benefits; (b) Post-employment benefits; (c) Other long-term employee benefits; (d) Termination benefits; and (e) Share-based payments. 	
124.17, 20	<p>If there have been transactions between related parties → to disclose:</p> <ul style="list-style-type: none"> ✓ Nature of the related party relationship; ✓ Information about the transactions; and ✓ Outstanding balances <p>necessary for an understanding of the potential effect of the relationship on the financial statements, in addition to the requirements of FRS 124.16.</p> <p>At a minimum, disclosures shall include:</p> <ul style="list-style-type: none"> (a) Amount of transactions; (b) Amount of outstanding balances and <ul style="list-style-type: none"> (i) Their terms and conditions (<i>including whether they are secured</i>), and the nature of the consideration to be provided in settlement; and (ii) Details of any guarantees given or received; (c) Provisions for doubtful debts related to the amount of outstanding balances; and (d) The expense recognised during the period in respect of bad or doubtful debts due from related parties. 	<p>Disclosure of FRS 124.17 shall be made separately for each of the following categories:</p> <ul style="list-style-type: none"> (a) Purchases or sales of goods; (b) Purchases or sales of property and other assets; (c) Rendering or receiving of services; (d) Leases; (e) Transfers of research and development; (f) Transfers under licence agreements; (g) Transfers under finance arrangements (including loans and equity contributions in cash or in kind); (h) Provision of guarantees or collateral; and (i) Settlement of liabilities on behalf of the entity or by the entity on behalf of another party.
124.18, 19	<p>Disclosure of FRS 124.17 shall be made separately for each of the following categories:</p> <ul style="list-style-type: none"> (a) The parent; (b) Entities with joint control or significant influence over the entity; 	<p>The categories are extended to provide a more comprehensive analysis of related party balances and apply to related party transactions.</p>

AXP Technical e-Newsletter - May 2007 Issue

	<ul style="list-style-type: none"> (c) Subsidiaries; (d) Associates; (e) Joint ventures in which the entity is a venturer; (f) Key management personnel of the entity or its parent; and (g) Other related parties. 	
124.21		Disclosures that related party transactions were made on terms equivalent to those prevail in arm's length transactions are made ONLY IF such terms can be substantiated.
124.22	Items of a similar nature may be disclosed in aggregate except when separate disclosure is necessary for an understanding of the effects of related party transactions on the financial statements of the entity.	
	<u>TRANSITIONAL PROVISION</u>	
124.22 A	Entity need NOT disclose information required under FRS 108.30(b) prior to the effective date of FRS 124.	
	<u>EFFECTIVE DATE</u>	
124.23	Apply FRS 124 for annual periods beginning on or after 1 October 2006. If earlier application → disclose the fact.	



AXP TECHNICAL DIAGNOSTIC CENTRE

*Recognition of Website Development Costs and
Its Income Tax Treatment*



Issue

Since the advent of the internet and electronic mail, the e-business activities have increased tremendously. Remember in 1980s, rarely people believe in Automated Teller Machine (ATM) offered by the bankers.

The scenario has definitely been changed, virtually all types of transactions can be performed via internet, from online bookstore, grocery shops, auction, to paying household bills, performing research and so on.

From accounting points of view, the advent of the internet gives rise to the issue of recognising the cost of developing website, as most of the company need one to do business to ensure that they are known to the world. The costs incurred for Website, including development and maintenance, may be substantial.

Reporting Standard Reference

Interpretation Committee's (IC) Interpretation 132 (*which is adopted by MASB*) concludes that the website development costs represent an internally generated intangible asset that is subject to the requirements of FRS 138 Intangible Assets.

The key criteria for determining whether such costs can be recognised as an internally generated intangible asset are:

1. the development costs can be separately identified;
2. the use of the website is controlled by the entity as a result of its past actions and events;
3. future economic benefits can be expected to flow to the entity; and
4. website development costs can be measured reliably.

Thus, it is important for an entity to demonstrate that the website developed is capable of promoting its products or services as well as generating future probable economic benefits to the business.

If the entity is not able to demonstrate this, all the costs incurred for developing the website shall be expensed off as and when incurred.

The following table presents the various types of expenditures that may be incurred when developing a website, and their accounting treatments:

Nature of Expenditure	Accounting Treatment
<p>Planning Stage</p> <ul style="list-style-type: none">✓ feasibility studies;✓ defining hardware and software specifications;✓ evaluating alternative products and suppliers; and✓ selecting preferences.	Recognise as an expense.

<p>Application and infrastructure development on acquisition of tangible asset, such as purchasing and developing hardware</p> <p>Other application and infrastructure development</p> <ul style="list-style-type: none">✓ obtain domain name;✓ developing operating software;✓ developing code for the application;✓ installing developed applications on the web server; and✓ stress testing. <p>Graphical design development</p> <ul style="list-style-type: none">✓ designing the appearance of website. <p>Content development</p> <ul style="list-style-type: none">✓ creating, purchasing, preparing and uploading information on the web site before the completion of the web site's development. <p>Operating Costs</p> <ul style="list-style-type: none">✓ updating graphics and revising content;✓ adding new functions;✓ registering the web-site with search engines;✓ backing up data;✓ reviewing security access; and✓ analyzing usage of the website.	<p>Apply FRS 116 Property, Plant and Equipment.</p> <p>Recognise as an expense, UNLESS the conditions prescribed by FRS 138 are met → capitalise as an intangible asset.</p> <p>Recognise as an expense, UNLESS the conditions prescribed by FRS 138 are met → capitalise as an intangible asset.</p> <p>Recognise as an expense to the extent that the content is developed to advertise and promote the entity's own products and services. Otherwise, recognise as an expense, UNLESS the conditions prescribed by FRS 138 are met → capitalise as an intangible asset.</p> <p>Recognise as an expense, UNLESS, in RARE circumstances, the conditions prescribed by FRS 138 are met → capitalise as an intangible asset.</p>
--	---

<p>Other costs</p> <ul style="list-style-type: none">✓ selling and administrative overhead unless it can be directly attributed to preparation of website for use✓ initial operating losses and inefficiencies incurred before the website achieves planned performance; and✓ training costs of employees to operate the website.	<p>Recognise as an expense.</p>
--	---------------------------------



Income Tax Treatment

Under the Income Tax (Deduction for Cost of Developing Website) Rules 2003, if a business resident in Malaysia incurred the cost of developing a website which is **electronic commerce enabled**, a tax deduction of 20% of the qualifying cost per year is allowed in ascertaining the adjusted income.

“Electronic commerce enabled” means a system of processes where transaction involving the transfer of information, products, services or payments can be made through electronic networks for an electronically confirmed consideration as verified by the Malaysian Communications and Multimedia Commission (MCMC).

The application for the deduction of the website development costs shall be made to MCMC by using the prescribed form ~ “Application Form for Certification of E-Commerce Website” with a processing fee of RM100.00. Once the MCMC has issued the certificate, the certificate shall be accompanying the income tax return for submission to IRB.

However, before the taxpayers submit the application to MCMC, please take note that the following are the minimum requirements which must be met before MCMC grants the approval:

1. The applicant must have a website.
2. The website must be hosted on a web server that is located in Malaysia.
3. There must be server software or applications that supply information to the web server on request. There must be:
 - (a) Shopping cart or any programs that facilitates the collection of information.

The program is a way to let web shoppers select the products or services they want, preview the sale amounts, delete items if they change their minds about, enter their payment and shipping information, and then cancel the order completely if they want.

- (b) Security capabilities that will allow the encryption of data during the transfer of customer information.
4. The collection of payment may be made online or offline. If the collection of payment is carry-out online, there must be:
- (a) Software to process transactions and send information to all of the involved parties (seller's bank, customer's bank, etc.).
 - (b) Security capabilities that will allow the encryption of data during the transfer of customer information.



Conclusion

There are differences between the accounting and tax treatment in respect of the website development costs in Malaysia, inevitably, deferred tax impact will arise. Thus, it is vital for the entity to have a proper accounting system to trace the website development costs.

Based on the prevailing tax law in Malaysia, the tax incentive available for the website development costs are very restrictive. As we are moving towards k-economy, we hope that in near future, the law makers can extend this tax incentive to include the following:

1. all types of website development, as long as the website are used to promote an entity's products or services;
2. verification by the MCMC should be exempted; and
3. minimum requirements, including the website must be hosted on a web server that is located in Malaysia, shall be removed.