

Client Alert

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Proposed Abolition of GST and Potential Tax Reforms in Malaysia

Introduction

Following the general elections on 9 May 2018, a new Malaysian Government has been formed by the *Pakatan Harapan* coalition ("**Coalition**"), under the stewardship of newly-appointed Prime Minister, Tun Dr. Mahathir Mohamad.

In the run up to the elections, the Coalition published a comprehensive manifesto ("**Manifesto**") outlining the key policies and actions that it is committed to implementing. In this alert, we will discuss some of the key tax changes and reforms included in the Manifesto that will be pertinent for businesses with operations in Malaysia.

Proposed Abolition of the Goods and Services Tax ("**GST**")

In the Manifesto, the Coalition pledged to abolish the GST regime within 100 days of coming into power. In press statements made by Prime Minister Tun Dr. Mahathir Mohamad after the elections, he has re-affirmed the coalition's commitment to abolish GST and to reintroduce the previous sales and services tax ("**SST**").

How will the abolition be carried out?

At current time, no formal details have been announced on the mechanics for the transition from the GST regime to the SST. To implement the reform, the relevant legislation to repeal or suspend the existing GST laws as well as new rules to implement the SST framework will need to be drawn up and passed by Parliament. For administration purposes, the Royal Malaysian Customs would need to ensure that its systems are in place to administer the new SST regime.

There have also been suggestions mooted that the abolition of the GST may be implemented by way of zero-rising the current GST rate (which is currently 6%). Presumably if the GST rate is 0%, there should not be any ability for businesses to claim input tax credits.

At the time of writing, we understand that the new Government is mulling the mechanics of the abolition of the GST and has indicated that more details are expected to be released within the next 100 days.

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What is SST and how is it different from GST?

By way of background, Malaysia used to have a SST regime up until 31 March 2015. This SST regime was repealed and replaced with the GST regime which came into force on 1 April 2015.

GST is a broad-based consumption tax, based on a value-added concept. SST is a single-tiered tax imposed only at the level of production or importation. Some key characteristics of the GST and the previous SST regime are as follows:

	GST	Sales Tax	Service Tax
Type	Multi-tiered consumption tax, imposed at each level of the supply chain	Single-tiered tax, imposed only at one level of production / importation	Single-tiered tax, imposed only at one level of the supply chain
Scope of tax	Broad-based tax i.e. a) taxable supplies of goods and services in Malaysia b) goods imported into Malaysia	Limited to particular category of goods i.e. a) taxable goods manufactured in Malaysia b) taxable goods imported into Malaysia	Limited to particular category of services i.e. taxable services provided by a taxable person in Malaysia
Rate	6%	Generally, 10% (with exceptions of 5% and 20% for certain goods)	6%
Input tax credit set-off	Input tax credits allowed to be claimed for standard-rated and zero-rated supplies	No input tax credit or set-off mechanism	No input tax credit or set-off mechanism
Registration / Licensing	Businesses with an annual turnover exceeding RM 500,000	Businesses with annual sales turnover exceeding RM 100,000	Depending on category of service provider and the taxable service

Implications and considerations for businesses

- **Compliance** - Businesses will need to budget for increased compliance costs to revamp existing accounting and IT systems and processes to cater for the removal of GST, as well as the introduction of the SST. To ensure compliance, staff will need to be re-trained to administer the SST within the business operations.



- **Transitional period** - Given the strong political push for this reform, the timeline for implementation may potentially be fairly short. A short timeline may mean that businesses will have to adapt quickly to embrace the changes. Transitional rules would also be important and would affect how the tax will be applied for transactions and agreements spanning the implementation date for the reform.
- **New contracts, pricing and anti-profiteering** - Businesses will also need to review carefully the terms of any upcoming contracts or agreements, to take into account the removal of GST and introduction of SST. The change may impact business' profitability as there is no mechanism for input tax claims under the SST for taxes paid. Prices of goods and services may also need to be determined carefully as a result of the proposed changes. It is unclear whether anti-profiteering laws may be enforced more rigorously to ensure that overall there is a reduction in prices (to be consistent with the Coalition's promises to reduce costs of living).
- **Ongoing GST audits, disputes and appeals** - It is likely that GST audits, disputes or appeals which have already commenced and are ongoing will not be affected. Liabilities for prior GST non-compliance or offences will continue to be applicable. There could be an increase in GST audits in the short term by the Royal Malaysian Customs for outstanding GST liabilities.
- **GST refunds** - Businesses with outstanding GST refunds would be looking to ensure that all refunds are processed and settled in a timely manner. Potential transitional rules may be required to address and account for GST already paid for existing stocks and inventory.

Holistic Review of National Tax System

The Coalition has pledged to undertake a holistic review of the national tax system, with the aim of making the income tax rates competitive within the ASEAN region. A review of the current corporate and personal income tax rates for small business owners and part-time employees will also be carried out.

Reduction in Excise Duties on Imported Cars

The Manifesto also contains a proposal to reduce the excise duties on imported cars with an engine capacity not exceeding 1,600cc, for first-time car buyers. At present, excise duties of between 60% to 75% are imposed on the importation of foreign-manufactured cars with an engine capacity below 1,600cc.

Tax Incentives

To increase the availability of affordable housing, the Manifesto includes a proposal to grant tax incentives to companies that focus on affordable housing. In particular, the incentives are intended to encourage companies to use the latest cost-efficient technologies such as the Industrialised Building System to reduce the cost of housing.



Preparing for Changes - What should Businesses Do?

The formation of a new government under the Coalition will likely herald in some key changes to Malaysia's current tax landscape, with the proposed GST abolition at the forefront of the tax reform agenda.

Businesses should ensure that they are able to adapt quickly to the changes to ensure minimal disruption to its operations. Specifically in the context of the proposed GST changes, it would be prudent for businesses to consider their potential obligations and requirements if the SST regime is re-introduced. Businesses should also review the potential impact of the SST on long-term agreements and transactions that may span the implementation date. The drafting of new agreements and contracts moving forward should also be considered carefully to address the potential reform to the GST regime. They should also review the impact of the GST's abolition on their business operations and profitability and ensure that staff are well-equipped and prepared to implement the changes within the business.

Proactive steps such as lobbying efforts on particular tax reforms may also be considered, if relevant. Historically, public consultations were rarely conducted prior to the introduction of new tax changes or laws. However, in its Manifesto, the Coalition has committed to provide chambers of commerce, business associations and business networks with direct access to the relevant ministries and agencies, to facilitate meetings between the ministries and members. Hopefully, this will allow businesses to take a more active role in providing input and feedback in the policy-making process.

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