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Service Tax on Imported Digital Services

Introduction

In line with the Malaysian Government's intention of levelling the playing field between local and foreign suppliers, it was announced during the 2019 Budget that, with effect from 1 January 2020, Malaysia will be imposing service tax on digital services that are imported by consumers in Malaysia under a Business-to-Consumer ("**B2C**") regime. This is also an avenue for the Malaysian Government to impose taxes on the digital economy, following the heels of other countries in the world which have already implemented similar digital taxes.

On 8 April 2019, the Lower House of Parliament passed the Service Tax (Amendment) Bill 2019 ("**Bill**"), which seeks to amend the Service Tax Act 2018 ("**STA**") to introduce this new B2C service tax regime. The Bill will become law, once it is passed by the Upper House of Parliament and receives the Royal Assent.

Who and what is caught under the B2C service tax regime?

Under the new B2C regime, service tax will be imposed, at the rate of 6%, on any digital service that is provided by a foreign service provider ("**FSP**") to any consumer in Malaysia. The 6% service tax is to be imposed on the value of the digital service that is charged by the FSP.

For such purposes:

- "Digital service" means any service that is delivered or subscribed over the internet or other electronic network and which cannot be obtained without the use of information technology and where the delivery of the service is essentially automated. This may potentially include streaming of music, videos, cloud storage services, provision of software online and digital advertising services, amongst others.
- A "foreign service provider" means any person who is outside Malaysia providing any digital service to a consumer. This includes any person who is outside Malaysia operating an online platform for buying and selling goods or providing services (whether or not such person provides any digital services) and who makes transactions for provision of digital services on behalf of any person.
- A "consumer" means any person who fulfils any two of the following:
    - makes payment for digital services using credit or debit facility provided by any financial institution or company in Malaysia;

- acquires digital services using an internet protocol address registered in Malaysia or an international mobile phone country code assigned to Malaysia; or
- resides in Malaysia.

How will Malaysia be implementing the B2C service tax regime?

FSPs who meet the mandatory registration threshold in respect of the provision of digital services to consumers in Malaysia are required to register for service tax with the Royal Malaysian Customs Department ("**RMCD**"). It has been announced in Parliament during the debate for the passing of the Bill, that the mandatory registration threshold is likely to be set at MYR 500,000 per annum of digital services provided to Malaysian consumers. It has also been mentioned that registration can be done online.

Once registered with the RMCD, the FSP would be required to:

- charge 6% service tax on the digital service that is provided to consumers in Malaysia at the time when the payment for the digital service is received by the FSP;
- issue an invoice or document containing certain prescribed particulars to the consumer in respect of the digital service transaction (whether electronically or in paper form);
- in respect of each taxable period[1], file a prescribed service tax return and remit the service tax collected (if any) to the RMCD, by the last day of the month following the end of the taxable period[2]; and
- maintain complete, true and up-to-date records of all transactions which affect or may affect its liability to service tax for a period of seven years.

How will the B2C service tax regime impact consumers in Malaysia?

- **Potential double taxation for businesses in Malaysia**

  "Consumer" is currently defined to be very broad. It appears sufficiently broad to include a business that fulfills any two of the three criteria as set out under the definition of "consumer".

  As such, where a particular service falls within (i) the scope of the "imported taxable service"[3] under the Business-to-Business ("**B2B**") regime; and (ii) the scope of "digital service" under this new B2C

[1] The taxable period is a period of three months ending on the last day of any month of any calendar year, unless the Director General of Customs approves a varied taxable period.
[2] For example, the service tax return and service tax payable for the taxable period of January 2020 to March 2020 would be due to the RMCD by 30 April 2020.
[3] "Imported taxable service" means any taxable service acquired by any person in Malaysia from any person who is outside Malaysia.

regime, the service could potentially be subject to double taxation, given that there is no input tax credit mechanism under the service tax regime. This is since (i) the business in Malaysia (as the service recipient) would be required to account for 6% service tax on the imported taxable service via the reverse charge mechanism; and (ii) the FSP would be required to charge service tax on the digital service it provides to the business in Malaysia.

This does not appear to be consistent with the Malaysian Government's intention of levelling the playing field between local and foreign suppliers. Instead, it is expected that businesses in Malaysia will be required to incur higher costs when importing services which falls under both the B2B and B2C regimes.

- **Higher prices for imported digital service for individual consumers**

  As digital services imported by individual consumers in Malaysia is currently not within the Malaysian service tax net, it is expected that individual consumers in Malaysia may face higher prices for digital services which are imported from FSP.

How can FSPs start preparing now?

In light of the short lead time before the implementation of the new B2C service tax regime in Malaysia, foreign businesses should undertake an assessment of the services which they sell into Malaysia to determine if their services would fall within the ambit of "digital services", as soon as possible.

Foreign businesses that provide digital content including music, videos and e-books, cloud computing storage subscription, software, or online platform services would likely be regarded as providing digital services for purposes of the STA.

Additionally, foreign businesses who expect to meet the mandatory registration threshold in 2020 should ensure that they register themselves with RMCD before the registration deadline of 31 September 2019.

Lastly, foreign businesses should also start considering the steps for implementing this new B2C service tax regime, e.g., whether internal systems need to be updated to cater for this new service tax regime, in order to ensure that they are able to comply with their legal obligations under the STA come 1 January 2020. For example, foreign businesses should relook into their invoicing systems and templates in light of the invoicing requirements under the B2C regime. Additionally, foreign businesses who provide in-scope and out-of-scope services should also have a system in place to internally track the transactions that would be caught under this B2C regime so that service tax can be collected and remitted to the RMCD accordingly.

Additionally, there may be areas of concerns which businesses may wish to clarify with RMCD, in order to ease compliance.

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