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Global Tax Alert

Malaysia releases 2019 Budget

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Executive summary

On 2 November 2018, Malaysia released its 2019 budget (the Budget). The Budget seeks to invigorate the economy and implement institutional reforms to strengthen fiscal administration, manage government debt and raise government revenue.

This Alert summarizes the key proposals of the Budget. Unless otherwise specified, the proposals are intended to be effective on or after 1 January 2019.

Detailed discussion

Special Voluntary Disclosure Program

For the period from 3 November 2018 to 30 June 2019, a Special Voluntary Disclosure Program (the Special Program) will be offered to encourage taxpayers to voluntarily disclose, for Malaysian tax purposes, any unreported income, including income maintained in offshore accounts. The Special Program is also applicable to cases under tax audit/investigation.

Under the Special Program, the reduced penalty rates for income tax, petroleum income tax and real property gains tax are as follows:

- For disclosures made between 3 November 2018 and 31 March 2019: 10%

Building a better working world

- For disclosures made between 1 April 2019 and 30 June 2019: 15%
- For disclosures made after 30 June 2019: 80% to 100%/300%[1]

In addition, the Special Program applies to failure to stamp dutiable instruments that are more than six months overdue, in the following manner:

- For disclosures made between 3 November 2018 and 31 March 2019: 10% of stamp duty
- For disclosures made between 1 April 2019 and 30 June 2019: 15% of stamp duty

Introduction of a loss and allowance carryforward period

Currently, tax losses and unutilized allowances (i.e., capital allowances, reinvestment allowances, investment allowances and investment tax allowances) can be carried forward indefinitely, with limited exceptions (i.e., substantial change of shareholders of a dormant company).

The Budget proposes a seven-year carryforward period, effective for the year of assessment 2019.[2]

Other corporate tax proposals

- The current year group tax loss sharing provisions have been tightened. Companies can only surrender their current-year losses for three consecutive years, from the year of business commencement. In addition, the claimant company would be ineligible for the group relief if the claimant has unutilized investment tax allowances or pioneer losses.[3]
- Introduction of limitation on interest deductibility in connection with or on any financial assistance in a controlled transaction. Detailed rules will be released later.
- The scope of taxation to include business income attributable to a place of business in Malaysia, including a branch and an office and certain supervisory activities, conclusion of contract and fulfillment of orders.

Labuan tax regime

Under the Budget, the following changes are proposed:

- Labuan entities are allowed to carry on activities in Ringgit Malaysia and/or with Malaysian residents, and still fall within the scope of the Labuan tax regime.
- The flat RM20,000 (US$5,000) tax will be repealed; consequently, Labuan companies carrying out a Labuan trading activity will be taxed at 3% of net audited profits.
- Income generated from intellectual property (IP) assets held by a Labuan entity will be subject to tax under the *Malaysian Income Tax Act 1967* and can no longer be taxed under the Labuan tax.
- Malaysian residents will only be allowed a 3% deduction on any payment made to Labuan entities.
- Labuan activities will be subject to substantive conditions as determined by a committee.

Real property gains tax and stamp duty

The Budget includes the following changes (previous rates are in parentheses):

- The real property gains tax rates for disposal in the sixth year or thereafter will be revised as follows:
  - Companies and non-citizen and non-permanent resident individual: 10% (5%)[4]
  - Others – 5% (0%)
- A 4% (3%) stamp duty will be assessed on the transfer of property in excess of RM1 million (US$250,000).
- Tightening the conditions to obtain stamp duty relief in the case of reconstruction or amalgamation, amalgamation of companies, or transfer of property between associated companies.

Indirect tax

The Budget includes the following indirect tax proposals:

- Service tax on imported services
- Service tax on digital products and services from 1 January 2020
- Prevention of cascading effect of sales tax and service tax in certain circumstances
- Introduction of excise duty on sweetened beverages beginning 1 April 2019 at the rate of RM0.40 (US$0.10) per liter based on sugar content exceeding certain levels

Tax incentives

- Some tax incentives for Industry 4.0:[5]
  - Up to RM27,000 (US$6,750) of tax deduction on expenses incurred for Industry 4.0 readiness assessment paid to Malaysian Productivity Corporation, from years of assessment 2019 to 2021.
  - Double deduction on expenses incurred by a company in implementing Industry 4WRD Vendor Development Program[6] for three consecutive years of assessment,

subject to a cap of RM1 million (US$250,000) per year for Memorandum of Understanding signed between the company and Ministry of International Trade and Industry from 1 January 2019 to 31 December 2021.

- Tax deduction for equipment and machinery contributed to Skills Development Centers, Polytechnics or Vocational Colleges, effective from 1 January 2019 to 31 December 2021.

- **Currently, an existing Principal Hub company extending its incentives will be given a five- or ten-year 100% tax exemption only on value-added income. It is proposed that such companies be eligible for a concessionary 10% income tax rate on overall statutory income for a period of five years.**
- Green technology incentives and environmentally-friendly incentives:
  - Pioneer status of 70% or investment allowance of 60% for five years to companies that produce environmentally-friendly plastics based on bio-resin and biopolymer.
  - An investment tax allowance of 100% of qualifying capital expenditure incurred on green technology assets through the year of assessment 2020 against 70% of statutory income.
  - Allocation of RM2 billion (US$500 million) for Green Technology Financing Scheme (GTFS) will be made available at selected commercial banks. The interest cost will be subsidized by 2% for the first five years.
- Termination of tax exemption for wholesale money market funds for companies.
- Two-year extension on double deduction on additional issuance cost of retail sukuk under certain Islamic principles and retail bonds.
- RM30 million (US$7.5 million) allocation for the Film in Malaysia Incentive and additional RM100 million (US$25 million) for film productions at the Pinewood Studios in Iskandar Johor, Malaysia.

Endnotes

1. Where no prosecution has been instituted, the maximum penalty rate of 300% applies to taxpayer who fails to submit the tax returns; whereas the penalty rate of 100% applies to taxpayer who fails to report the correct income.
2. Generally, the year of assessment for a company corresponds with its financial reporting period.
3. Investment tax allowance is an additional depreciation on the qualifying fixed assets. Pioneer losses refer to the losses incurred during the tax relief period by companies granted with the Pioneer Status tax incentive.
4. This category would mainly apply to Malaysian citizen and permanent resident individuals.
5. The fourth industrial revolution, also known as Industry 4.0, uses a range of technologies to transform various activities including manufacturing, maintenance, monitoring and supply chain operations.
6. Vendor Development Program is generally a program implemented by a company in developing new suppliers or strengthening the development of existing suppliers.

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