Bloomberg BNA

TAX PLANNING INTERNATIONAL

ASIA-PACIFIC FOCUS

International Information for International Business

November 2017

www.bnai.com

Enhanced Tax Incentives in Malaysia's 2018 Budget

Irene Yong
Shearn Delamore & Co., Malaysia

The Malaysia 2018 Budget contains few surprises. Certain business sectors, notably Islamic finance, tourism and health tourism, continue to enjoy enhanced tax incentives, and the abolition of thin capitalization rules is proposed.

Irene Yong is an Advocate & Solicitor, Tax & Revenue Practice Group at Shearn Delamore & Co., Malaysia

The proposed abolition of thin capitalization rules was unsurprising given that the implementation of thin capitalization in Malaysia had been deferred several times prior thereto. Instead, Earning Stripping Rules ("ESR") will be implemented with effect from January 1, 2019 to curb excessive deduction of interest expense incurred on loans made between related parties. Deductibility would be restricted to a specified percentage of the taxpayer's profit before tax. The applicable ratio in Malaysia has yet to be determined by the relevant authorities.

Prior to the 2018 Budget announcement, a stamp duty bill proposed in 2017 was withdrawn. A prior stamp duty bill proposed in 2016 was also withdrawn in early 2017.

Some of the 2018 Budget highlights are discussed below.

Income Tax Rates and Exemptions for Individuals

The income tax rates for tax-resident individuals (who are taxed at progressive rates ranging from 0 percent to a top rate of 28 percent of their chargeable income) will be reduced by 2 percent for certain income bands as follows:

(a) chargeable income from 20,001 ringgit to 35,000 ringgit, tax rate reduced to 3 percent;
(b) chargeable income from 35,001 ringgit to 50,000 ringgit, tax rate reduced to 8 percent; and
(c) chargeable income from 50,001 ringgit to 70,000 ringgit, tax rate reduced to 14 percent.

 TPAF ISSN 1478-5129

Exemption on Rental Income

A 50 percent tax exemption will be given to Malaysian tax-resident individuals on rental income received from renting out residential homes where the monthly rental does not exceed 2,000 ringgit for each residence from YA 2018 to YA 2020.

Tax Incentives and Allowances

Principal Hub Incentive

The Principal Hub Incentive will be extended for another three years. An approved principal hub company is eligible for a three-tiered preferential income tax rates ranging from 0 percent to 10 percent for the specified period subject to meeting the relevant criteria, amongst other exemptions. Applications must be made to the Malaysian Investment Development Authority ("MIDA") by December 31, 2020.

Health Tourism

The tax incentive granted to new and existing companies engaged in expansion, modernization and refurbishment of private healthcare facilities or undertaking a new investment in respect of the same, will be extended for a further three years. This comprises a tax exemption equivalent to investment tax allowance of 100 percent of the qualifying capital expenditure incurred by the company for a period of five years on a qualifying project, which can be set-off against up to 100 percent of its statutory income, subject to meeting the relevant conditions. Applications to MIDA must be submitted by December 31, 2020.

A double deduction can also be claimed in respect of expenditure incurred by companies providing dental and ambulatory healthcare services, in obtaining certification for quality systems and standards. Such companies must be registered with the Malaysia Healthcare Travel Council.

Tourism

2020 has been declared as Visit Malaysia Year. In tandem with that, the investment tax allowance for new 4- and 5-star hotels will be extended from December 31, 2018 to December 31, 2020. This is an exemption equivalent to the amount of the qualifying capital expenditure incurred on investments in new 4- or 5-star hotels within a period of five years which can be set-off against a specified percentage of the hotel operator's statutory income. Applications to MIDA must be submitted by December 31, 2020.

The 100 percent income tax exemption enjoyed by tour operating companies on statutory income derived from operating tour packages within/to Malaysia will also be extended to YA 2020.

Islamic Finance

To further encourage the development of the Malaysian capital market, stamp duty exemption would be granted on contract notes for the trading of Exchange-Traded Funds (which are open-ended investment funds listed and traded on a stock exchange) and Structured Warrants which are executed between January 1, 2018 and December 31, 2020 (both dates inclusive).

A qualifying company providing management services to funds which are managed in accordance with Shariah principles and certified by the Securities Commission of Malaysia ("SC") currently enjoys exemption from income tax until YA 2020 on its statutory income derived from the business of providing fund management services to:

(i) foreign investors in Malaysia;
(ii) local investors in Malaysia; and
(iii) business trusts and real estate investment trusts in Malaysia.

To further promote such services globally, a fund manager managing "Sustainable and Responsible Investment" Funds ("Funds") which are approved by the SC would be exempted from income tax from YA 2018 to YA 2020, on management fees received in connection with the management of conventional and Shariah-compliant Funds.

Goods and Services Tax ("GST")

Under section 64 of the Goods and Services Tax Act 2014, supplies made by the Federal Government and the State Government are treated as out-of-scope supplies and hence not subject to GST. This treatment would also be extended to local authorities so that all supplies of goods or services made by local authorities would not be subject to GST with effect from either April 1, 2018 or October 1, 2018, as determined by the relevant local authority. Local authorities will also be given GST relief on the acquisition of goods other than petroleum, commercial buildings/land and the importation of cars.

With effect from January 1, 2018 to December 31, 2020, cruise operators will be given relief from payment of GST on handling services (such as stevedoring, loading, unloading, reloading and inspection of cargo) provided by sea port operators in Malaysia.

With effect from January 1, 2018, the following will be given relief from GST subject to the conditions and list of items to be issued by the Minister of Finance:

(a) importation of big-ticket items including aircraft, ships and oil rigs by airlines, shipping companies and oil and gas companies;
(b) importation of goods into Malaysia under lease agreements with companies located in the "Designated Areas", namely Labuan, Langkawi and Tioman.

From January 1, 2018, management and maintenance services, including cost recovery of group insurance, quit rent and land assessments, supplied by housing developers to the owners of stratified residential buildings, would be treated as an exempt supply for GST purposes.

GST Appeal Tribunal

GST appeals are currently being heard by the GST Appeal Tribunal, which has jurisdiction to adjudicate upon all GST matters save for the excluded matters set out in the Fourth Schedule to the Goods and Services Tax Act 2014. Matters pertaining to customs and excise duties fall within the jurisdiction of a separate Customs Appeal Tribunal ("CAT").

With effect from January 1, 2019, GST matters would be heard by CAT, instead of the GST Appeal Tribunal. This may mean that taxpayers would no longer be permitted to have legal representation for GST matters as an advocate and solicitor is presently not allowed to represent taxpayers at hearings before the CAT.

Capital Allowance

Accelerated Capital Allowance and Automated Equipment Allowance will be granted on the first 10 million ringgit of qualifying capital expenditure incurred by taxpayers in the manufacturing sector and related services during the basis period for YAs 2018 to 2020. The application must be received by MIDA between January 1, 2018 and December 31, 2020 (both dates inclusive).

From YA 2018, qualifying expenditure incurred on the development of customised software comprising consultation fees, licensing fees and "incidental fees" relating to software development also qualify for CAs at the rate of 20 percent for the initial and annual allowance. However, it is unclear as to what "incidental fees" can be included in the CA claim.

OECD's Taxation Initiatives

Malaysia's commitment to implement the Organisation for Economic Cooperation and Development's initiatives on, amongst others, automatic exchange of information and the Base Erosion and Profit Shifting Action Plan ("BEPS") Initiative was confirmed during the 2018 Budget Speech.

To date, Malaysia has implemented the Automatic Exchange of Information on tax matters, and is a BEPS Associate in the Inclusive Framework to implement BEPS Action Plan, a member of the Forum on Harmful Tax Practices, and party to the Convention on Mutual Administrative Assistance on Tax Matters, Multilateral Competent Authorities Agreement on Country-by-Country Reporting and the Multilateral Competent Authority Agreement on Common Reporting Standards. Malaysia is also an ad hoc member of the Multilateral Instrument Framework.

Irene Yong is an Advocate & Solicitor, Tax & Revenue Practice Group at Shearn Delamore & Co., Malaysia.