



Horwath Tax News

The Official Tax Newsletter of Horwath Kuala Lumpur

October 2009 (Special Budget Edition)

Foreword

At a time of financial crossroads where the Malaysian Government is torn between financial prudence due to the rising budget deficits and more government spending to stimulate the economy, the Budget 2010 presented by the Prime Minister and Minister of Finance, YAB Dato' Sri Mohd. Najib Tun Abdul Razak on 23 October 2009 was a fair budget with minimal surprises. There were few tax breaks, substantial cuts in government spending but no new taxes other than the 5% real property gains tax (RPGT) and service tax of RM50 on credit cards.

Major tax changes

The RPGT came at a time when the property market is still soft compared to other nearby countries such as China, Hong Kong and Singapore. The unexpected reinstatement of the tax has caused some consternation when the tax was only suspended not long ago on 1 April 2007. To a certain extent, the RPGT has overshadowed the more favourable tax changes.

One of the more significant tax changes is the reduction in the top individual income tax rate from 27% to 26% for income exceeding RM100,000. No changes were made to the corporate tax rate which stands at 25%.

This change will put more disposable income in the hands of taxpayers together with other favourable measures such as increasing the personal relief for individuals by RM1,000, increasing the life insurance premium and EPF relief by RM1,000 but only for premiums paid for annuity policies, and deduction of RM500 for broadband subscriptions.

Tax incentives

This year, the tax incentives introduced by the Government were understandably few as a wide array of tax incentives are presently available.



Nevertheless, changes were made to industries such as health tourism and the Islamic financial market.

Healthcare providers who offer services to foreign health tourists can now enjoy income tax exemption of 100% on the value of the increased exports instead of the previous 50%. The Islamic financial industry was also the beneficiary of several tax exemptions to promote the industry and to keep it in the forefront of the world Islamic financial market.

In its keenness to promote various issues such as a green environment, research and development and creative industries, the Government has made changes to its spending, provided soft loans and reorganized its administrative practices. In particular, the Government is encouraging green technology for building industry practices by providing certain tax incentives for buildings that are awarded the Green Building Index, a home grown index launched by the Government recently.

Goods and Services Tax (GST)

Finally, the Budget 2010 announced the long-awaited news on the implementation of the GST which the Government said is at the final stage of its study particularly on the social impact of this tax.

It has also indicated that the GST rate would be lower than the current sales tax and service tax rates of 5% and 10% respectively.

Overall, the Budget 2010 proposals seek to lay an essential foundation for a new economic model as the Government has made known its intentions to shift the country from an industrial-based economy to a high-income economy that is based on innovation, creativity and high-value added activities. There will be obstacles ahead and the challenge starts TODAY!

The Horwath Tax Team

InSide

Reintroduction of RPGT	2
Tax Incentives	3
Updates Affecting Individuals and Others	4
Administrative Changes Affecting Companies, Trust Bodies, Co-operatives and Other Taxpayers	5
Change of Assessment System for Upstream Petroleum Companies	6



Reintroduction of Real Property Gains Tax

Introduction

In line with the Malaysian Government's objective to ensure that the Malaysian tax system is equitable and able to generate consistent revenue to fund its development projects, the Malaysian Government has reintroduced the Real Property Gains Tax (RPGT) Act 1976 with effect from 1 January 2010.

History

Previously, a taxpayer is exempted from RPGT on gains arising from the disposal of real property on or after 31 March 2007. The main objective for this measure was mainly to stimulate the growth of the sluggish property market in 2007 by encouraging investors especially the foreigners to acquire real property in Malaysia.

Following the announcement made in the proposed 2010 Budget, it is noted that the window for the tax holiday period which expires on 31 December 2009 is fast closing.

Who will have to pay RPGT?

Any person including an individual (whether local or foreigner), a company, a partnership, a body of persons and a corporation sole is liable to pay RPGT on the chargeable gains accruing from the disposal of real property in Malaysia.

What type of transaction will attract RPGT?

Any disposal relating to real property and shares in a real property company will attract RPGT.



Real property means any land situated in Malaysia and any interest, option or other rights in or over land or shares in a real property company (RPC).

A RPC is defined as one which is a controlled company (a company with less than 20 shareholders and which is controlled by not more than 5 persons) which owns real property situated in Malaysia, the market value of which amounts to 75% or more of the total tangible assets of the company.

Existing legislation		Proposed legislation
(a)	Tax rate	
	The rates range from NIL to 30% depending on the holding period.	The applicable rate is fixed at 5% irrespective of the holding period
(b)	Individual	
	No RPGT shall be taxed on an individual if the holding period is more than 5 years. For a foreigner, the RPGT rate is 30% irrespective of the holding period.	Individuals no longer enjoy full tax exemption even though the holding period is more than 5 years. For foreigners, the RPGT rate is reduced to 5%.
(c)	Interest incurred to finance the acquisition of real property	
	Interest cost is permitted to be included as part of the acquisition price of the real property provided that the cost is incurred during the period of construction of real property.	Interest cost will be excluded from the acquisition price of the real property.
(d)	Compulsory remittance to Director General of money withheld by acquirer	
	The minimal amount to be withheld by the acquirer is restricted to 5% of the total value of the consideration. There is no specific provision to direct the acquirer to remit the amount withheld to the Director General (DG) until a requisition has been served by the DG.	The minimal amount to be withheld has been reduced to 2%. It is a compulsory requirement for the acquirer to remit the amount withheld to the Director General within 60 days from the date of disposal. Failure to withhold and remit such amount will result in a 10% penalty on that sum. The date of disposal is usually the date of the sale and purchase agreement for the property.
(e)	Relief for allowable losses	
	Where there is an allowable loss arising from a disposal of real property, a tax relief equals to the loss multiplied by the applicable tax rate shall be allowed as a setoff against the total tax assessed for the year of assessment in which the disposal was made.	Where there is an allowable loss arising from a disposal of real property, such allowable loss shall be allowed as a deduction against the total chargeable gain from the disposal of real property for the year of assessment in which the disposal was made. Any excess loss due to insufficiency or absence of chargeable gain in the year that the loss arose will be allowed to be carried forward to reduce the total chargeable gain for subsequent years of assessment, until the loss is fully utilised.



Reintroduction of Real Property Gains Tax (Cont'd)

Conclusion

Given the recent highly speculative property market in overseas countries, especially China, Hong Kong and Singapore, this pre-emptive measure could be used as a tool to curb speculation in the Malaysian property market.

However, it may not be timely to reinstate the RPGT Act as the property market of Malaysia is still soft and has yet to fully recover from the global recession in 2008. Compounded by defensive selling by foreigners before the 1 January 2010 deadline, the property market is likely to be dampened in the short term.

Nevertheless, the collection of the 5% RPGT tax and especially the 2% withholding tax upfront from taxpayers may help towards generating more revenue for the Malaysian Government at this time of economic slowdown.

Tax incentives

Enhancing tax incentives for Islamic financial industry

In line with the Government's objective to position Malaysia at the forefront of the global Islamic financial industry, the following measures have been proposed:

- i. Tax exemption on profits derived from overseas operations by banking institutions be extended to insurance and takaful companies;
- ii. Extension of the existing tax incentives as shown in the table below:

Tax incentives to be extended to 2015
Stamp duty exemption of 20% on Islamic financial instruments approved by Bank Negara Malaysia (BNM) or Securities Commission (SC)
Double deduction of expenditure incurred in promoting Malaysia as an International Islamic Financial Centre (MIIFC)
Deduction of expenses incurred for establishment of Islamic stock broking companies
Deduction of expenses incurred for issuance of Islamic securities approved by the SC

- iii. Extension of the existing tax incentives as shown in the table below:

Tax incentives to be extended to Labuan companies
Stamp duty exemption on Syariah financing instruments approved by the Labuan Offshore Financial Services Authority (LOFSA)
Tax exemption on profits from non-Ringggit <i>Sukuk</i> (bonds) approved by LOFSA
Deduction of expenses incurred for issuance of Islamic securities approved by LOFSA
Tax exemption on interest paid or credited on Islamic securities (excluding convertible loan stock) which are issued in non-Ringggit and approved by LOFSA
Tax treatment on special purpose vehicles (SPVs) to be extended to those established under the Offshore Companies Act, 1967 electing to be taxed under ITA. The SPV will not be subject to tax whilst the income received and cost incurred by the SPV will be deemed to be the income and cost of the company that established the SPV.

Incentives for using green technology

The world is moving into a new era of the Go Green Revolution with the result that many countries are generous with their incentive schemes to accelerate the adoption of green technologies. One of the areas is in green building design which is able to save utility costs as well as preserve the quality of the environment. In step with many nations, the Malaysian Government launched its very own Green Building Index (GBI) which is a green rating index for environmentally friendly buildings, on 21 May 2009.



Tax Incentives (cont'd)



Following this, the Government proposed the incentives below for those who adopt green technology in their building design:

- For owners of buildings who are awarded the GBI certificate, tax exemption will be given on capital expenditure incurred to obtain the first GBI certificate in respect of the building. The incentive is applicable for new buildings and upgrading of existing buildings;

- For buyers who buy buildings and residential properties awarded the GBI certificate from real property developers, stamp duty exemption will be given on instruments of transfer of ownership in respect of the additional cost incurred to obtain the GBI certificate; and

- The Government has also established a fund amounting to RM1.5 billion to provide soft loans to companies supplying and utilising green technology. In respect of the interest incurred, 2% shall be borne by the Government with the remaining interest cost to be borne by the applicants. In addition, the Government will provide a guarantee of 60% on the financing amount, with the remaining 40% by the banking institutions.

Together with tax incentives given previously to companies which are engaged in the production of renewal energy or in the conservation of energy, the Government is laying the foundation for a more widespread adoption of green technology in the country.

Enhancing tax incentive for medical tourism industry

Medical tourism involves combining travelling on holiday whilst undergoing medical procedures in a foreign country. This industry has been growing rapidly in Malaysia in recent years as Malaysia offers a competitive healthcare service compared to other countries. Having provided an income tax exemption equivalent to 50% of the value of increased exports in previous years, the Government intends to promote this industry further by increasing the incentive to 100% of the value of increased exports for assessment years 2010 to 2014.

Tax incentive for registration of patents and trademarks for SMEs

Presently, double deduction is only allowed to companies for registration of patents, trademarks and product licensing overseas to promote exports of goods. In an effort to promote innovation and intellectual property development among SMEs, the Government will allow a deduction of the expenses incurred on the registration of patents and trademarks in Malaysia, which currently are treated as non-deductible expenses.

Updates Affecting Individuals and Others

Review of income tax rate

Lagging behind the drop in corporate tax rates which have fallen from 28% in assessment year 2006 to 25% in assessment year 2009, the Government has decided to drop the individual tax rate this year to be more in line with the corporate tax rate. The highest marginal tax rate of 27% is now reduced to 26% for resident individuals whose chargeable incomes exceed RM100,000. The 1% drop in marginal rate which is equivalent to a drop of 3.7% of the 27% rate of tax is a welcomed boon to the higher income group. The overall individual tax rates in Malaysia are however, still not as attractive as those of neighboring countries such as Singapore and Hong Kong but significantly better than those in the developed countries such as Australia and England.

The above change will take effect from year of assessment 2010.

In line with the reduction of tax rates for individuals, the Government has proposed that the co-operative income tax rate for chargeable income exceeding RM500,000 be reduced by 1 percentage point from 27% to 26% with effect from year of assessment 2010.

Increase in personal tax reliefs

In line with the drop in the marginal tax rate for individuals so as to reduce the tax burden of individuals, the Government has proposed to increase the reliefs below for resident individuals:

- The self relief will be increased from RM8,000 to RM9,000 per year (effective from year of assessment 2010);
- The allowable deduction for life assurance relief will be increased from RM6,000 to RM7,000 a year effective from 1 January 2010. However, the additional deduction of RM1,000 will only be applicable to premiums paid for annuity schemes which were contracted after 1 January 2010 or to additional premiums paid for existing annuity schemes where payments commenced from 1 January 2010.

[Continue next page]



Updates Affecting Individuals and Others (Cont'd)

Increase in personal tax reliefs (cont'd)

iii. Deduction will be allowed for broadband subscription fees up to RM500 per year for the years of assessment 2010 to 2012 only. This deduction is also to enhance the usage of broadband.

Tax exemption on certain interest and discounts

Concurrently with incentives given to the Islamic financial industry as mentioned in the other parts of this newsletter, the Government is extending the tax exemption on interest and discounts to include those received from Islamic securities approved by Labuan Offshore Financial Services Authority and the Securities Commission starting from year of assessment 2010.

Tax rate for knowledge workers in Iskandar Malaysia

Iskandar Malaysia (IM) is the special economic zone in South Johore which has been earmarked by the Government for development into an area for creative, health, education and financial services. To attract local and foreign talent to this zone, the Government has proposed to impose a flat rate tax of 15% on the employment income of a resident individual. The conditions for this special rate of tax are that the employee has to be a knowledge worker and engaged in any of the following qualifying activities:

- green technology;
- biotechnology;
- educational services;
- healthcare services;
- creative industries;
- financial advisory and consulting services;
- logistics services; and
- tourism.

This incentive is applicable to workers who apply and commence employment in IM between 24 October 2009 to 31 December 2015 and in respect of income derived from year of assessment 2010 onwards.

Service tax on credit cards and charge cards

To cultivate an attitude of prudent spending, the Government has proposed the charging of service tax on credit cards and charge cards at the rate of RM50 for a principal card and RM25 for a supplementary card, including those issued free of charge starting from 1 January 2010 onwards.

This tax is likely to curtail spending by reducing the credit available to cardholders and in the number of cards held by cardholders with the attendant effect of throttling the business volume of card companies.

Administrative Changes Affecting Companies, Trust Bodies, Co-operatives and Other Taxpayers

Table 1.1 summarises the administrative changes for companies, trust bodies, co-operatives and other taxpayers in the Budget 2010:

Amendment to the law	Effect
An estimate of tax payable is not required to be furnished if the basis period in which the company (non-SME), trust body or co-operative commences operations is less than 6 months	This will ease the administrative burden of the company (non-SME), trust body or co-operative
Penalty for non-estimation of tax by all companies, trust bodies and co-operatives – failure to furnish an estimate of tax payable to the IRB within 30 days before the beginning of the basis period for a year of assessment.	A penalty of 10% of the tax payable shall be due and payable upon furnishing the tax return for that year of assessment (effective from year of assessment 2011)
Penalty on additional tax by any person – failure to furnish a tax return within the stipulated deadline	Additional penalty will be imposed if there is additional tax to be paid where the tax return was not furnished within the stipulated deadline
Returns to be submitted by employers pertaining to employees under Section 83 before 31 March of the following year	Failure to comply will result in a fine of not less than RM200 and not more than RM2,000 or to imprisonment for a term not exceeding 6 months or to both
Employers' responsibilities for tax of employees - An employer will be required to personally bear the tax of an employee if he fails to withhold the taxes of the employee when the employee ceases employment with the employer	Any amount due from the employer for failure to comply shall be a debt due to the Government

The minor changes above are mainly for the purpose of streamlining the law and tightening up compliance requirements under the Self Assessment System so as to deter taxpayers from not complying with their tax obligations.



Change of Assessment System for Upstream Petroleum Companies



History of assessment systems in Malaysia

Upstream petroleum companies are subject to income tax under the Petroleum (Income Tax) Act 1967 (“PITA”), whereas the rest of the taxpayers are subject to income tax under the Income Tax Act 1967 (“ITA”). All taxpayers were then assessed to tax on a preceding year basis under the Official Assessment System. With effect from the year of assessment 2000 (current year basis), the system was changed to the current year basis for all taxpayers except the upstream petroleum companies which were still assessed under the preceding year basis.

Subsequently, in assessment year 2001, the current year basis was changed further to the Self Assessment System. At that time, however, no change had been made to the assessment system under PITA.

Standardisation of assessment systems in Malaysia

In the Budget 2010, it is proposed that the assessment system on income derived from upstream petroleum companies under PITA be changed to the current year basis under the Self Assessment system with effect from the year of assessment 2010. This is to standardise the assessment systems under PITA and ITA in Malaysia, and as a result of this change, the Government will have a better cash flow position.

In the year in which the change takes place, i.e. the year of assessment 2010, the income of the upstream petroleum companies for the financial years ended 2009 and 2010 will be taxed under a single year of assessment, i.e. year of assessment 2010.

Therefore, there will be double collections of tax for the Government in the year of assessment 2010. The amount could be rather significant as the petroleum taxes under PITA contribute significantly to the total direct tax collections by the Government.

However, unlike the change in the assessment system under the ITA back in year 2000 where the Government has waived the income tax of taxpayers for income earned in the year 1999, there is no such similar proposal made for the upstream petroleum companies. Hence, to alleviate the burden of the upstream petroleum companies from paying two years’ taxes in one year, the Government has allowed the income tax for the year of assessment 2010 based on the income received in the financial year 2009 to be paid by installments over 5 years.

