Expanded SST should balance fiscal goals with industry readiness, say tax experts

BY **CHERYL POO**

The proposed expansion of the sales and service tax (SST) that is expected to be gazetted on June 1 is intended to bring more goods and services into the tax net, contributing to government revenue while aligning with broader fiscal reforms.

But given the concerns raised by business groups in the construction and manufacturing sectors over the timing of the legislation, increased costs, lack of clarity and insufficient time for preparation, attention will centre on how the gazettement will tackle implementation, especially whether there will be transitional rules to allow for exemptions on contracts that straddle past the implementation date.

Announced by Prime Minister Datuk Seri Anwar Ibrahim during the tabling of Budget 2025 in October last year, the gazettement of the proposed SST expansion was initially set for May 1. But in April, it was postponed to June 1 by the Ministry of Finance (MoF).

Anwar, who is also finance minister, did not provide specific details on the SST expansion in his budget speech, saying only that the sales tax would be increased on non-essential items, including imported premium goods like salmon and avocado.

The service tax is expected to be expanded to include commercial service transactions between businesses that were previously exempted, especially fee-based services.

MoF reportedly said in April that the guidelines and scope of the SST were being refined to ensure a smooth implementation and that the implementation would be applied at a later date despite the completion of nationwide engagements with industries to finalise the scope of the expansion and the applicable tax rates.

While the intention behind the proposal is understandable from a policy standpoint, tax experts whom *The Edge* spoke with acknowledged the concerns raised by industry players and recommended ways to bridge the transition gap.

Complications in qualifying taxable goods, dealing with existing contracts

Deloitte Malaysia indirect tax leader Tan Eng Yew points out that for the sales tax, a pertinent challenge will be assessing whether the imported or manufactured goods will be impacted by the new tax, especially if the goods were previously not taxable.

In addition, a business undertaking value-added activity would have to consider whether the activity now falls under the definition of "manufacture" for sales tax purpose.

"The definition is very wide. So, if the finished product which was previously not taxable becomes taxable, such as foodstuff, then the business would have to register and put in place processes to ensure compliance such as registration, invoicing and filing of return. [It is similar] with service tax, and it may not be straightforward for some industries," says Tan, who recommends a minimum of three to six months for preparation to ensure sufficient time is given after the law and guidance is released to the public.

The tax experts point out that the expanded SST may pose certain challenges for businesses with existing contracts established prior to the expansion, particularly those that are non-reviewable. Specifically, businesses may find themselves unable to adjust contract terms to reflect the new SST, which could result in reduced profit margins if the tax is not incorporated into the pricing structure.

"On contracts that straddle past implementation, [the Royal Malaysian Customs Department or RMCD] would usually allow a period of exemption, after which the tax has to be accounted for. Businesses are expected to renegotiate contracts, failing which the provider/seller would end up bearing the tax," says Tan.

"As we learnt from the implementation of the goods and services tax (GST) previously, renegotiating contracts is a challenge, resulting in providers/sellers bearing the tax. A more practical and business-friendly approach would be to allow contracts signed before an official date to be exempted until the expiry/renewal without putting a time limit on the exemption."

Jalbir Singh Riar, indirect tax partner at Ernst & Young Tax Consultants Sdn Bhd, emphasises business adaptation with government support, urging businesses to engage in discussions with relevant stakeholders to explore the implications of SST on contracts.

"Although the contracts may be non-reviewable, businesses should communicate with their clients to promote mutual understanding and potentially facilitate renegotiation. If renegotiation proves unfeasible, businesses may need to have certain strategies in place to absorb the additional costs, unless the government considers providing transitional provisions to assist companies with non-reviewable contracts similar to the GST regime," he says.

Jalbir advises that to effectively prepare for and manage the impact of the SST expansion, businesses should conduct a thorough assessment to determine the appropriate SST treatment, identify their SST registration obligations, and update systems and processes as necessary.

He adds that they should also consider the transitional provisions which may be included in the law and review the tax clauses in their contracts to accommodate these updates. Businesses who have undertaken a thorough review and are still uncertain about SST's impact, can consider seeking confirmation/ruling from the RMCD.

As it stands, business associations in the manufacturing and construction industries which are expecting to feel the impact; the Federation of Malaysian Manufacturers (FMM) and Master Builders Association Malaysia (MBAM) have articulated their concerns.

"Generally, the construction industry is already taxed across multiple components of project execution — from building materials to labour and equipment — all of which are subject to various forms of taxation and levies. Construction contracts are typically awarded on a fixed-price and fixed-duration basis. Any new imposition of tax, particularly if applied retrospectively, would significantly disrupt existing contractual terms, project budgets and timelines. This would place an unfair burden on both the contractors and clients, potentially leading to project delays and cost overruns," MBAM president Oliver Wee Hiang Chyn tells *The Edge*.

"Requiring service tax payment before monthly progress claims are certified and paid by clients would exacerbate cash flow constraints. This is especially concerning given that contractors are not in a position to bear tax payments on behalf of clients or to finance these costs in advance. In addition to SST, the industry is already contributing through various existing charges, including foreign workers' Employees Provident Fund contribution, Construction Industry Development Board levies, stamp duty on contracts and HRD Corp levies, and we hope there will not be other future inflationary costs. Given the cumulative burden on the sector, we appeal to the government to reconsider the imposition of SST on construction services."

Meanwhile, FMM president Tan Sri Soh Thian Lai points to the transitional guidelines issued by the RMCD in March, which indicate that goods delivered or invoiced after the gazettement date, regardless of when they were produced, will be subject to the expanded sales tax.

"This treatment overlooks the realities of contract fulfilment, where production, delivery and billing often follow agreed timelines set long before the tax changes were anticipated. Manufacturers operating under fixed-price contracts will be forced to absorb the new tax cost, which could result in margin erosion or outright losses. This issue is especially acute in sectors where prices are locked in months in advance and the ability to pass on added costs is constrained by intense market competition or contractual terms," says Soh, who recommends a deferment of the gazettement and implementation of the sales tax expansion beyond June 1.

More gradual approach recommended

While EY's Jalbir believes it may not be constructive or necessary to have a further delay to the proposed expansion of SST, he points out that there are indeed pros and cons in further delaying the implementation of the expanded tax.

"Implementing SST by June could be practical, with adequate support and resources provided by the government for businesses to transition smoothly. This includes clear guidelines, training for compliance, hand-holding sessions, and possibly phased implementation for certain sectors. However, if significant concerns remain regarding the impact on essential goods and services, it may be prudent to consider a more gradual approach," he says.

He adds that reassessing the taxation of essential goods and providing exemptions for essential sectors, as well as RMCD conducting hand-holding sessions are some ways to ensure effective implementation. "Providing leniency such as not penalising the companies during the first six months of implementation, similar to the relaxation period under the e-Invoicing regime and the previous GST regime, would be helpful," he says.

A case for GST

According to EY, there has been higher SST revenue amounting to about RM5.83 billion since the implementation of SST in September 2018, followed by an expansion of the service tax scope and an increase in service tax rate in March 2024.

And going by the Budget 2025 announcement, MoF is forecasting an additional RM5 billion increase in SST collections from the expansion of the tax.

It is worth noting that, as some of the tax experts point out, Malaysia is among the few countries that have implemented SST while most countries have long moved to GST.

To this end, Deloitte's Tan points to businesses with products and services that will become taxable, leading to clarification of taxable goods and services along with implementation of change. "In principle, this is more a compliance burden, on the basis that this is a tax that is passed on to the customer. For this group, an effective implementation plan would reduce the impact of the tax," he says.

"Broadly speaking, most businesses would be affected by the increase in the cost of doing business, as more goods and services acquired to do business become taxable. This is the point that is most concerning — to what extent will prices be affected. And ultimately, it is the individual consumers who will likely end up carrying the burden, which is why there is a continual call for the government to bring back GST to more effectively address the issue of embedded/snowballing effect of SST that is difficult to quantify."

In any case, Ng Sue Lynn, head of indirect taxes at KPMG in Malaysia, hopes that the legislation for the expanded SST will be gazetted first, followed by a phased implementation with a later effective date. "This approach would offer greater certainty and allow affected stakeholders time to assess the impact on their businesses and to prepare accordingly," she says.

"While taxpayers are generally willing to comply, the compressed timeline may pose significant challenges. In recognition of this, the government could consider a grace period during which penalties are not imposed for genuine errors or unintended non-compliance. Additionally, it would be helpful for the Customs Department to conduct roadshows and provide hands-on guidance to support businesses in implementing the expanded SST scope." E

Deloitte's Tan says a pertinent challenge will be assessing whether the imported or manufactured goods will be impacted by the new sales tax

KPMG's Ng: The government could consider a grace period during which penalties are not imposed for genuine errors or unintended non-compliance

EY's Jalbir advises businesses to conduct a thorough assessment to determine the appropriate SST treatment, identify their SST registration obligations, and update systems and processes as necessary