



Capital Gains Tax

What do you need to consider?



January 2024 (updated in March 2024)

KPMG in Malaysia

Capital Gains Tax

A new tax has emerged

Following the repeal of the income tax exemption on foreign sourced income received in Malaysia by a resident person since year 2022, a new tax called Capital Gains Tax (“CGT”) has emerged effective from 1 January 2024, to further broaden the tax revenue for the government.

CGT is incorporated as part of the MITA. The class of income on which tax is chargeable under the MITA has been expanded by introducing a new subsection 4(aa) gains or profits from the disposal of a capital asset to be subject to CGT.

CGT is imposed on gains made by **companies, LLPs, trust bodies and co-operative societies** (regardless of whether incorporated in or outside Malaysia) from:

- 1) a disposal of shares in companies incorporated in Malaysia not listed on the stock exchange;
- 2) a disposal of shares of a controlled company incorporated outside Malaysia which owns real property situated in Malaysia or shares of another controlled company, subject to meeting the 75% threshold conditions (“Section 15C shares – see details below”); and
- 3) a disposal of capital assets situated outside Malaysia, when the gains are received in Malaysia.

“Disposal” means to sell, convey, transfer, assign, settle or alienate whether by agreement or by force of law and includes a **reduction of share capital** and **purchase by a company of its own shares**. It is interesting to note from the MIRB’s response to the CGT questions posted in NTS 2023 that a redemption of preference shares and winding up or strike off of a company are regarded as a disposal. It should be considered whether or not a gain arises from the redemption of preference shares and winding up / strike off of a company, and if no gain arises, there should be no tax impact apart from the administrative filing of CGT return.

The “shares” for CGT purposes are defined as:

- a) stock and shares in a company;
- b) loan stock and debentures issued by a company or any other corporate body incorporated in Malaysia;
- c) a member’s interest in a company not limited by shares whether or not it has a share capital; or
- d) any option or other right in, over or relating to shares as defined in paragraphs (a) to (c).

Based on the MIRB’s Guidelines on CGT for Shares Not Listed on the Stock Exchange (“CGT Guidelines”) issued on 1 March 2024, at present, only “shares” with equity characteristics would fall within the ambit of CGT. For instance, ordinary shares, preference shares, redeemable preference shares, convertible bonds or long term loans with equity characteristics. The equity characteristics include:

- a) rights to receive non-fixed dividends;
- b) the shareholder's interest in the remaining assets ranks after all the claims from other parties in the event of a liquidation;
- c) no maturity date; and



d) rights to vote.

Observation:

- The MIRB's position that a liquidation constitutes a CGT event, does not accord with the legal position that a liquidation involves a company disposing of its own assets then using those proceeds to settle claims from creditors and then finally returning the remaining proceeds (capital and retained earnings, if any) to the shareholders. There is no disposal event at the shareholder level. To impose CGT on a liquidation would be to impose CGT on the disposal of a Malaysian company of its Malaysia situated assets, which is treated as exempt under the current legislation. Further evaluation and clarification from the MIRB is required for readily accepting this position.
- The MIRB's position on instruments with equity characteristics poses the question, if an instrument has a combination of debt and equity characteristics, does having a single equity characteristic cause the instrument to be 'equity' for CGT purposes, even though for accounting purposes it may be classified as debt due to its dominant debt characteristics? Given this uncertainty, further clarification is needed from the MIRB as to whether an instrument would be viewed as "shares" for CGT purposes as long as it has any one of the "equity" features as listed in the CGT Guidelines.
- It is not defined in the MITA what constitutes "received in Malaysia" for CGT purposes. The MIRB has, in its Guidelines on Tax Treatment in relation to Income Received from Abroad (Amendment) ("FSI Guidelines"), defined "received in Malaysia" as "transferred or brought into Malaysia, whether in the form of cash or through electronic funds transfer; or both". It appears that the MIRB has taken a literal approach in defining "received in Malaysia", which does not cover constructive receipt.

While it remains to be seen if the same definition will be adopted for CGT purposes, consideration needs to be taken as to whether the following constitutes 'received in Malaysia':

- a) Shares of a foreign entity are exchanged with shares in a Malaysian entity, under a share swap arrangement
- b) Constructive receipt (e.g. disposal proceeds from outside Malaysia are transferred directly to a property developer to purchase any property in Malaysia)
- c) Disposal consideration is settled by way of issuance of promissory notes to the disposer in Malaysia

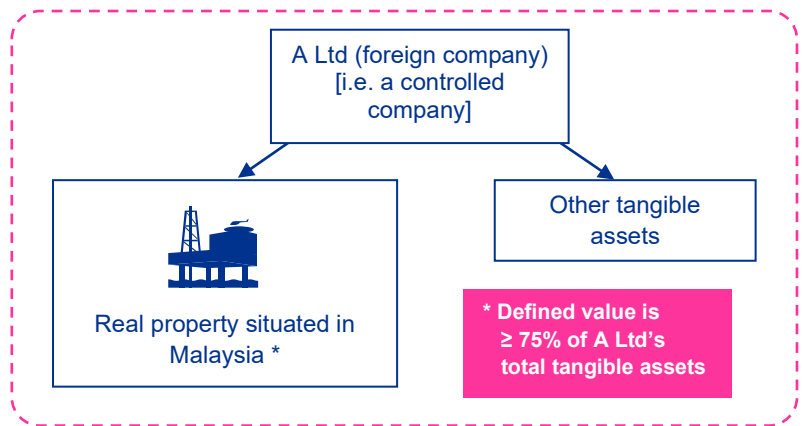
Disposal of shares of a controlled company incorporated outside Malaysia – Section 15C shares

Pursuant to Section 15C of the MITA, gains from the disposal of shares of a controlled company (a company having not more than 50 members and controlled, in the manner described by Section 139 of the MITA, by not more than 5 persons) incorporated outside Malaysia under the following scenarios would be **deemed to be derived from Malaysia**:

1 Disposal of shares in a foreign company that owns real property situated in Malaysia

Condition:

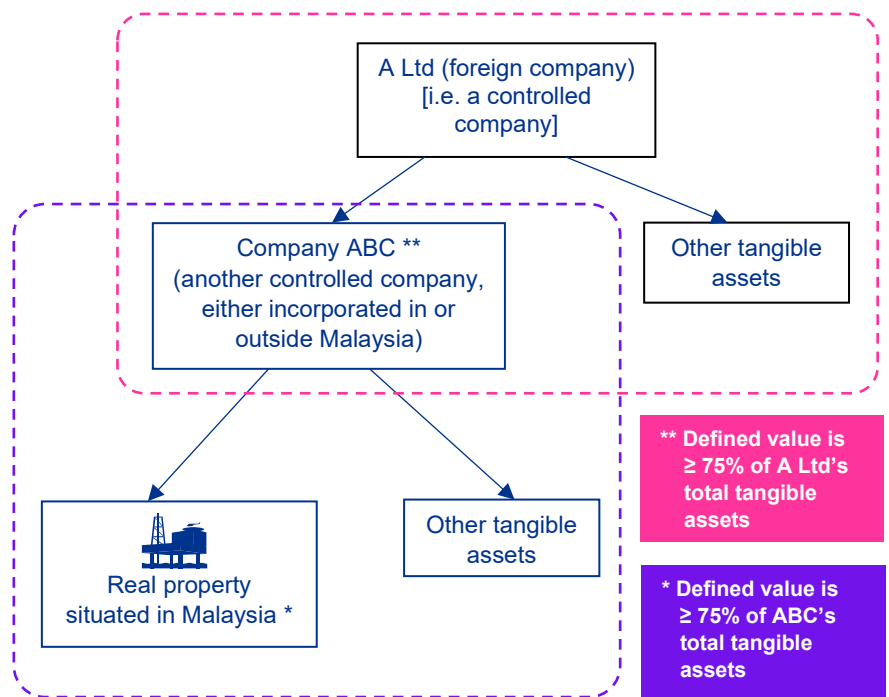
The defined value of the real property situated in Malaysia (including any right or interest thereof) owned by the foreign company is not less than 75% of the value of its total tangible assets



2 Disposal of shares in a foreign company that owns shares in another controlled company which owns real property situated in Malaysia

Conditions:

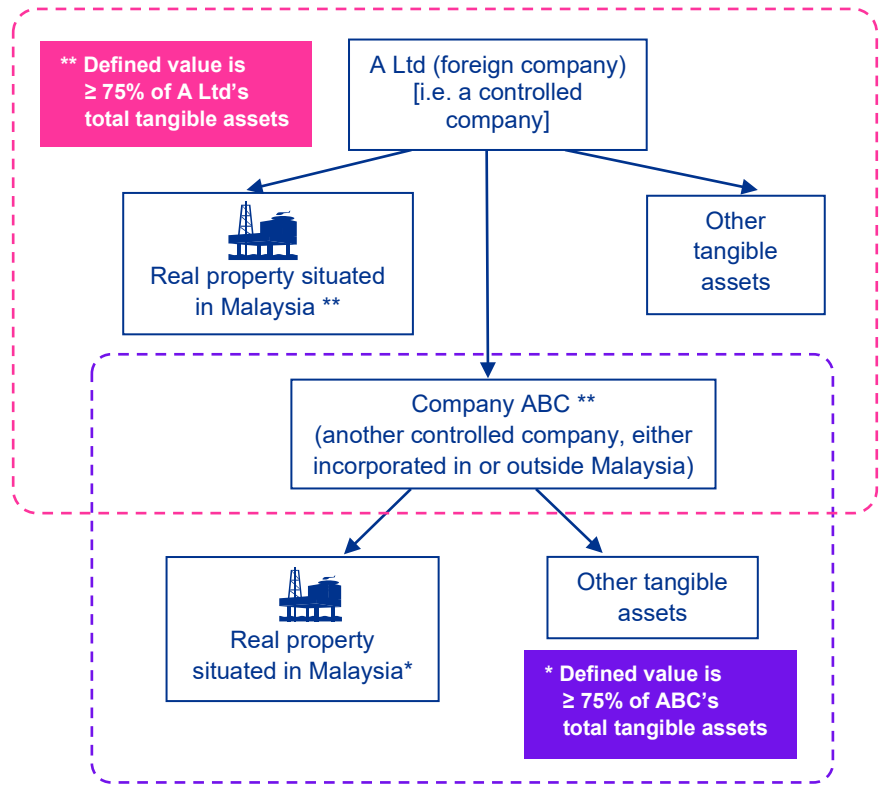
- Another controlled company owns real property situated in Malaysia, where the defined value of the real property is not less than 75% of the value of its total tangible assets; and
- The foreign company, which is a controlled company, owns shares in another controlled company, where the defined value of the shares is not less than 75% of the value of its total tangible assets



3 Disposal of shares in a foreign company that owns real property situated in Malaysia and shares in another controlled company

Condition:

The defined value of the real property situated in Malaysia and shares of another controlled company, owned by the foreign company, is not less than 75% of the value of its total tangible assets



Once the 75% threshold condition above is met and a disposal of shares of the controlled company incorporated outside Malaysia falls within the ambit of Section 15C of MITA (i.e. 'Section 15C shares'), gains from the disposal of such shares will be deemed as Malaysian-sourced. This is notwithstanding that at the time of disposal of such shares, the defined value of the real property and/or shares in another controlled company may have dropped below 75% of the controlled company's total tangible assets.

Before CGT was introduced, Malaysia has already had in place RPGT, which is a tax imposed on the disposal of real property situated in Malaysia and RPC shares.

With the introduction of CGT, the RPC provision in the RPGTA is no longer applicable to CGT-in scope taxpayers i.e. companies, LLPs, trust bodies and co-operative societies, effective from 1 January 2024. As a policy decision, the IRB has indicated in its CGT Guidelines that the existing shares in RPC under the RPGTA (acquired before 1 January 2024) would automatically be regarded as Section 15C shares for CGT-in scope taxpayers.

Observation:

- Gains from the disposal of shares of a controlled company incorporated outside Malaysia are not automatically treated as a foreign-sourced. However, a Section 15C test needs to be performed. This is done by using a bottom-up approach of testing, at every level of shareholding up to the ultimate holding company, as to whether the 75% threshold condition is met. If the 75% threshold condition is met, the shares shall be treated as Section 15C shares i.e. deemed as Malaysian-sourced, instead of foreign-sourced shares.
- **The MIRB has clarified in its CGT Guidelines that:**
 - a) Where the shares in a controlled company outside Malaysia have not met the 75% threshold condition, Section 15C test needs to be performed whenever the controlled company acquires real property situated in Malaysia and/or shares in another controlled company.
 - b) The Section 15C shares status can be removed, if at any time of the disposal of real property situated in Malaysia and/or shares in another controlled company, the defined value of the real property and/or shares in another controlled company drops below 75% of the controlled company's total tangible assets.

This seems to follow the timing of performing an RPC test under the RPGTA.

Tax exemption for CGT

Domestic exemption

Several tax exemptions have been proposed since the issuance of the 2024 Budget, which are summarised as follows:

Capital assets	Tax exemptions
Capital assets situated outside Malaysia	<p>Exemption in force:</p> <ul style="list-style-type: none"> • Disposal of capital assets situated outside Malaysia (apart from intellectual property rights) which is received in Malaysia from 1 January 2024 to 31 December 2026, provided that the qualifying disposers comply with the conditions imposed by the MOF as specified in the guidelines to be issued by the Director General of MIRB under Section 134A of the MITA, which shall include the economic substance requirements. Any deduction in relation to the income exempted shall be disregarded in ascertaining the chargeable income for that YA. A person who is carrying out the business of banking, insurance, sea transport or air transport is not eligible for the said exemption. [Income Tax (Exemption) (No. 3) Order 2024] <p>Proposed (exemption order has yet to be gazetted):</p> <ul style="list-style-type: none"> • Unit trust funds will be exempted from CGT for the period from 1 January 2024 until 31 December 2028

Capital assets	Tax exemptions
<p>Capital assets situated in Malaysia / deemed derived from Malaysia:</p> <ul style="list-style-type: none"> • Shares of an unlisted company incorporated in Malaysia • Section 15C shares 	<p>Exemption in force:</p> <ul style="list-style-type: none"> • Disposal of shares of an unlisted company incorporated in Malaysia during the period from 1 January 2024 until 29 February 2024 [Income Tax (Exemption) (No. 7) Order 2023] • Disposal of Section 15C shares during the period from 1 January 2024 until 29 February 2024 [Income Tax (Exemption) (No. 2) Order 2024] <p>Proposed (exemption order has yet to be gazetted):</p> <ul style="list-style-type: none"> • Approved initial public offering • Internal group restructuring • Venture capital companies • Unit trust funds will be exempted from CGT for the period from 1 January 2024 until 31 December 2028

Observation:

- To-date, the guidelines on economic substance requirements for the CGT exemption have yet to be issued by the MIRB. Based on the MIRB's FSI Guidelines, the MIRB does not impose any minimum threshold and thus it is the taxpayers' burden to prove that it has met the economic substance requirements. It remains to be seen whether the same concept will be imposed for CGT purposes. In particular, it needs to be clarified as to whether, for investment holding entities, a local board of directors making relevant investment decisions would, without any additional employees, assets or operations, be sufficient to satisfy the economic substance requirements.

Interaction with tax treaties

As CGT is incorporated as part of the MITA and treated as "income" for tax purposes, the existing DTAs can be relied upon for treaty exemption, or bilateral relief if the same gains are subjected to tax in Malaysia as well as in a foreign jurisdiction, in the event that such gains are not eligible for any domestic exemption.

Observation:

- In applying the provisions in a DTA, taxpayers may need to consider the following in sequence:
 - a) Is there a CGT Article in the DTA, or is any other article relevant to the scenario?
 - b) Is there any exemption provided in that CGT Article / other Article?
 - c) If no exemption is available, and the capital gains are taxed in Malaysia as well as the foreign jurisdiction, is there any bilateral relief available in the DTA?
- If the tax treaty exemption and bilateral relief is not available, unilateral relief under Schedule 7 of the MITA may be considered. However, unilateral relief is more restrictive in the following ways:
 - a) Malaysian-sourced income is not eligible for unilateral relief.
 - b) The unilateral credit allowed shall not exceed half of the foreign tax payable on that income.
- For the purpose of applying DTA benefits, based on current practice, a taxpayer is only required to furnish a copy of the COR of the non-resident. The MIRB has yet to issue guidelines to clarify on the mechanism and the conditions (if any) to claim DTA relief for CGT purposes. As such, it is unclear as to whether the current practice of only supplying a COR will also be sufficient for Malaysian CGT exemption purposes or whether a more challenging set of tests and conditions will be required, as is increasingly the case in other jurisdictions that apply CGT to foreign shareholders.



Tax rates

The tax rates imposed on gains from the disposal of a capital asset are as follows:

Capital assets	YA 2024 onwards
Capital assets situated outside Malaysia	<ul style="list-style-type: none"> • Prevailing income tax rate on chargeable income
Capital assets situated in Malaysia / deemed derived from Malaysia (i.e. Section 15C shares):	
<ul style="list-style-type: none"> • which were acquired before 1 January 2024 	<ul style="list-style-type: none"> • 10% on chargeable income / 2% of gross on disposal price (at the option of the disposer)
<ul style="list-style-type: none"> • which were acquired on or after 1 January 2024 	<ul style="list-style-type: none"> • 10% on chargeable income

Tax compliance

Taxpayers do not need to take into account gains from the disposal of capital assets which fall under CGT in their annual estimate of tax payable, under Section 107C of the MITA.

The disposer is obliged to furnish a prescribed form (i.e. CGT return form) to the MIRB electronically for each taxable disposal of capital assets, within 60 days from the date of disposal. Any tax payable is due on the same day.

Observation:

- Based on the MIRB's CGT return form filing programme and its guide notes, CGT filing is not required for the disposal of shares made during the period from 1 January 2024 until 29 February 2024, which is exempted from CGT.
- It is theoretically possible for a foreign corporate seller to obtain a Malaysian Tax Identification Number for the purposes of performing such tax payment and filing, but whether this is generally expected to be done by the foreign entity or local agents and how the MIRB will ensure compliance (or pursue any non-paid / underpaid taxes) given that there is no withholding obligation by either the buyer or the target of the transfer, is not yet clear.
- Gains from the disposal of capital assets situated outside Malaysia is subject to CGT upon remittance. As the law is silent, clarification is needed as to whether the 60-days filing requirement applies to such disposal.
- Our current understanding is gains from the disposal of capital assets situated outside Malaysia would need to be reported in the annual income tax return, in the YA of remittance.

Date of disposal

Date of disposal is important as it triggers the CGT provisions and its filing requirement. The determination of date of disposal is summarised as follows:

Scenarios	Date of disposal
<u>There is written agreement</u> <ul style="list-style-type: none"> Disposal or acquisition is subject to Government or State Government approval Conditional agreement (which require Government or State Government approval) Cases other than the above 	<ul style="list-style-type: none"> The date of such approval The date when last of all such conditions is satisfied Date of the written agreement
There is no written agreement	The date of completion: <ul style="list-style-type: none"> Date of ownership of the capital asset is transferred by the disposer; or The date on which the whole of amount or value of the consideration for the transfer has been received by the disposer, whichever is earlier.
Transfer of capital assets to trading stocks (deemed disposal)	The date taken into trading stock

Certain disposal shall be deemed to be transacted at market value

In general, the disposal price shall be taken to be the value of the consideration for the disposal less the prescribed allowable expenditure. However, there are circumstances where the consideration shall be deemed to be equal to the market value of the capital asset at the time of the disposal, amongst others:

- 1) Where the capital asset is acquired / disposed of otherwise than by way of a bargain made at arm's length, in particular, by way of gift;
- 2) Where the capital asset is acquired / disposed of wholly or partly for a consideration that cannot be valued; or
- 3) Where the transaction is between connected persons.

A question would then arise: How do we value shares in a company that is not listed on a stock exchange?

Based on the CGT Guidelines, the MIRB has allowed taxpayers to use any reasonable and appropriate valuation method in determining the market value of the unlisted shares. Among the possible methods is the Net Tangible Asset method calculated based on the company's financial statements.

Losses from the disposal of capital assets

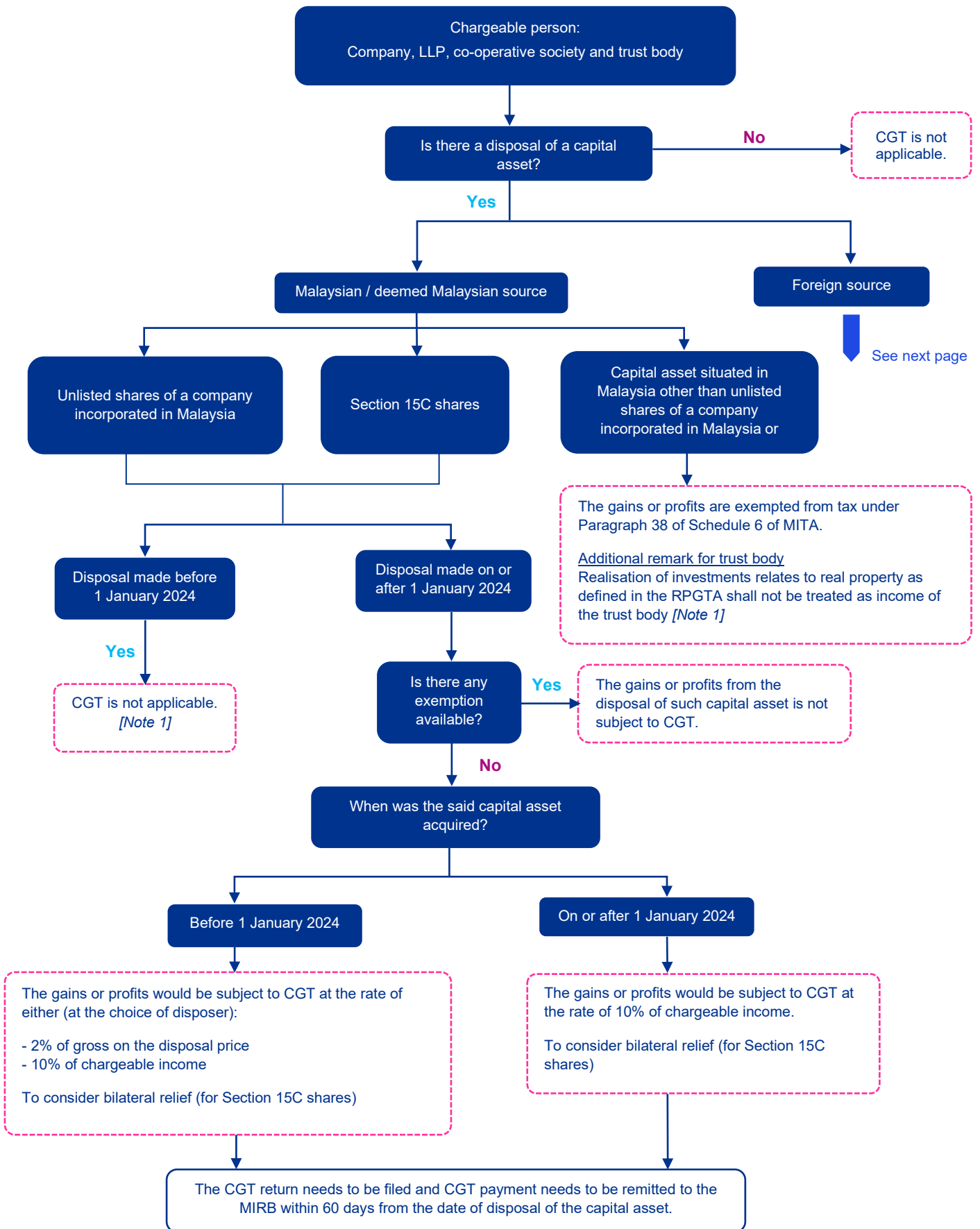
Generally, losses arising from the disposal of capital assets are allowable to be offset against the adjusted income of the **subsequent disposal** of capital assets in the same basis period for a YA. Any unutilised losses can be carried forward for **10 consecutive YAs**.

However, the MIRB has expressed its view that losses from the disposal of capital assets situated in Malaysia / deemed derived from Malaysia are not able to be set off against gains from the disposal of capital assets situated outside Malaysia.

Observation:

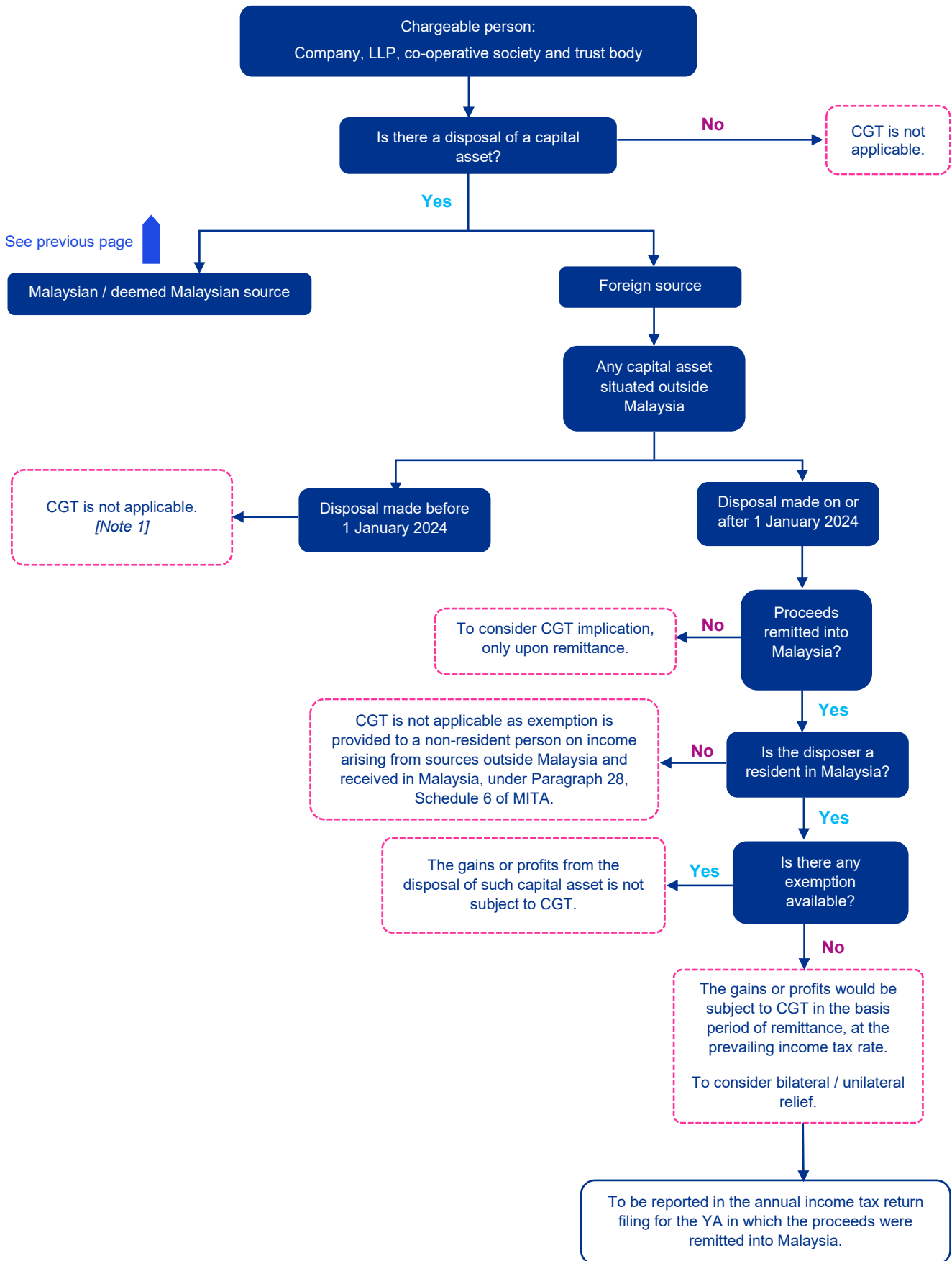
- The losses from the disposal of capital assets are ring-fenced, i.e. not allowed to be offset against aggregate income from business or non-business source, and not allowed to be carried back. In this respect, taxpayers need to take extra care when contemplating a series of disposals of capital assets. Capital assets which will result in an allowable loss should be first disposed of prior to the disposal of any capital asset that will result in a gain in order for an offsetting to occur. **In the MIRB's explanatory note to the CGT return form, it is expressly mentioned that where there is more than one disposal made within the same day, taxpayers are allowed to notify the disposal of capital asset which resulted in an allowable loss as the first asset to be disposed of.**
- **Example 7 of the CGT Guidelines implies that the current year adjusted losses shall be fully utilised before utilising any unabsorbed losses brought forward from the prior YA.**

CGT implication flowchart



Note 1: To consider RPGT implications.

CGT implication flowchart (continued)



Note 1: To consider RPGT implications.

Interaction with real property gains tax (“RPGT”)

With a shift from RPGT to CGT, affected taxpayers may wonder if they are now in a better off position when disposing of shares which were previously caught under the RPC provision in the RPGTA. We have summarised the distinct differences or similarities below:

	RPGT	CGT
Definition of disposal	Sell, convey, transfer, assign, settle or alienate whether by agreement or by force of law	The same definition under RPGT is adopted with a broadened scope, which covers reduction of share capital and purchase by a company of its own shares
Cost base (for shares in a Malaysian company)	Based on the consideration paid, or deemed transacted at market value under certain circumstances, if it is RPC shares at the date of acquisition If it only turns into RPC shares after the date of acquisition, the acquisition price shall be computed based on defined value	Based on the consideration paid, or deemed transacted at market value under certain circumstances
Cost base (for shares in a foreign company – Section 15C shares)	Based on the consideration paid, or deemed transacted at market value under certain circumstances, if it is RPC shares at the date of acquisition If it only turns into RPC shares after the date of acquisition, the acquisition price shall be computed based on defined value	Based on the consideration paid, or deemed transacted at market value under certain circumstances, if it is Section 15C shares at the date of acquisition If it only turns into Section 15C shares after the date of acquisition, the acquisition price shall be computed based on defined value
Disposal price	No deductions are allowed for: <ul style="list-style-type: none"> • Enhancement expenditure • Cost of establishing, preserving or defending the owner’s title; and • Incidental expenses on disposal 	Deductions are allowed for these expenses, although these expenses are unlikely to be significant for a disposal of shares
Losses arising from the disposal	Not an allowable loss to offset against other chargeable gains or to be carried forward (i.e. permanently lost)	Allowable loss can be offset against the adjusted income of the subsequent disposal of capital assets in the same YA. Any unutilised losses can be carried forward for 10 consecutive YAs.

	RPGT	CGT
Interest expense attributable to the acquisition of shares	Not an allowable expense in RPGT computation	Not an allowable expense in CGT computation
Tax rate	Ranging from 10% to 30% on chargeable income, depending on the holding period before disposal	<p><u>Asset acquired before 1 January 2024</u></p> <p>10% on chargeable income / 2% of gross on disposal price (at the option of the disposer)</p> <p><u>Asset acquired on or after 1 January 2024</u></p> <p>10% on chargeable income</p>
Exemptions available for restructuring scheme	<p>With the prior approval from the MIRB, the transfer of assets between companies in the same group receives no gain and suffers no loss, if the transferee company is a resident in Malaysia and, amongst others:</p> <ul style="list-style-type: none"> The transfer will bring about greater efficiency in operation for both transferor and transferee; or The transfer is pursuant to any scheme of reorganisation, reconstruction or amalgamation. 	<p>It is proposed in the 2024 Budget that the following are exempted from CGT:</p> <ul style="list-style-type: none"> Internal restructuring Initial public offering Venture capital company <p>This is pending the issuance of the relevant gazette orders to legislate this exemption. It remains to be seen whether prior application is required and whether similar conditions imposed under RPGT will be adopted.</p>
Double taxation relief	Not applicable, as RPGT is not a covered tax under the DTA	Applicable, if the relief conditions are met
Filing requirement	<ul style="list-style-type: none"> Both the disposer and acquirer are required to file RPGT return within 60 days from the date of disposal. Where the disposal consideration consists wholly or partly of money, the acquirer is required to withhold a certain amount of money (as defined) and remit the amount to the MIRB within 60 days from the date of such disposal. Upon assessment by the MIRB, if the final RPGT due is higher than the amount withheld, the difference should be paid by the disposer to the MIRB within 30 days from the date of Notice of Assessment. Otherwise, the disposer may request for a refund. 	<ul style="list-style-type: none"> Only the disposer is required to file CGT return within 60 days from the date of disposal. There is no requirement for the acquirer to withhold any amount when making payment to the disposer. Under the self-assessment system, the submission of the CGT return is deemed a Notice of Assessment being served to the disposer. Any CGT payable is due on the same day of submission due date, i.e. within 60 days from the date of disposal.

Way forward

As part of good tax planning, it is pertinent for the affected taxpayers to plan early in ascertaining the applicability of CGT and its exemptions. Nevertheless, as CGT has just been introduced and there are still areas of uncertainty awaiting further clarification from the MOF / MIRB, affected taxpayers should continue to keep abreast of evolving developments.

The table below sets out the various abbreviations and references used in this publication.

Abbreviation	Reference
CGT	Capital Gains Tax
COR	Certificate of Residence
DTA	Double Taxation Agreement
LBATA	Labuan Business Activity Tax Act, 1990
LLP	Limited Liability Partnership
MITA	Malaysian Income Tax Act, 1967
MIRB	Malaysian Inland Revenue Board
MOF	Ministry of Finance
NTS	National Tax Seminar
RPC	Real Property Company
RPGT	Real Property Gains Tax
RPGTA	Real Property Gains Tax Act, 1976
YA	Year of Assessment

Contact Us

Petaling Jaya Office

Soh Lian Seng

Partner – Head of Tax and Tax Dispute Resolution
lsoh@kpmg.com.my
+603 7721 7019

Tai Lai Kok

Partner – Head of Corporate Tax
ltai1@kpmg.com.my
+603 7721 7020

Bob Kee

Partner – Head of Transfer Pricing
bkee@kpmg.com.my
+603 7721 7029

Long Yen Ping

Partner – Head of Global Mobility Services
yenpinglong@kpmg.com.my
+603 7721 7018

Ng Sue Lynn

Partner – Head of Indirect Tax
suelynnng@kpmg.com.my
+603 7721 7271

Outstation Offices

Penang Office

Evelyn Lee

Partner – Penang Tax
evewflee@kpmg.com.my
+603 7721 2399

Kota Kinabalu Office

Titus Tseu

Executive Director – Kota Kinabalu Tax
titustseu@kpmg.com.my
+603 7721 2822

Ipoh Office

Crystal Chuah Yoke Chin

Associate Director – Ipoh Tax
ycchuah@kpmg.com.my
+603 7721 2714

Kuching & Miri Offices

Regina Lau

Partner – Kuching Tax
reglau@kpmg.com.my
+603 7721 2188

Johor Office

Ng Fie Lih

Partner – Johor Tax
flng@kpmg.com.my
+603 7721 2514

KPMG Offices

Petaling Jaya

Level 10, KPMG Tower,
8, First Avenue, Bandar Utama,
47800 Petaling Jaya, Selangor
Tel: +603 7721 3388
Fax: +603 7721 3399
Email: info@kpmg.com.my

Penang

Level 18, Hunza Tower,
163E, Jalan Kelawei,
10250 Penang
Tel: +603 7721 3388
Fax: +604 238 2299
Email: info@kpmg.com.my

Kuching

Level 2, Lee Onn Building,
Jalan Lapangan Terbang,
93250 Kuching, Sarawak
Tel: +603 7721 3388
Fax: +6082 530 669
Email: info@kpmg.com.my

Miri

1st Floor, Lot 2045,
Jalan MS 1/2,
Marina Square, Marina Parkcity,
98000 Miri, Sarawak
Tel: +603 7721 3388
Fax: +6085 321 962
Email: info@kpmg.com.my

Kota Kinabalu

Lot 3A.01 Level 3A,
Plaza Shell,
29, Jalan Tunku Abdul Rahman,
88000 Kota Kinabalu, Sabah
Tel: +603 7721 3388
Fax: +6088 363 022
Email: info@kpmg.com.my

Johor

Level 3, CIMB Leadership Academy,
No. 3, Jalan Medini Utara 1,
Medini Iskandar,
79200 Iskandar Puteri, Johor
Tel: +603 7721 3388
Fax: +607 266 2214
Email: info@kpmg.com.my

Ipoh

Level 17, Ipoh Tower,
Jalan Dato' Seri Ahmad Said,
30450 Ipoh, Perak
Tel: +603 7721 3388
Email: info@kpmg.com.my

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