Capital Gains Tax Comes To Malaysia

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Overview and Commentary

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Key Message

As has been widely anticipated, in the 2024 Budget, Prime Minister and Finance Minister YAB Dato' Seri Anwar Bin Ibrahim announced the introduction of a new capital gains tax at the rate of 10% that will apply to disposals of non-listed shares by Malaysian companies starting from 1 March 2024. Though there will be some exemptions, such as for new IPOs and group restructurings, the introduction of this tax is a sea change in the Malaysian tax system. A great number of questions are yet to be answered from the announcement, not least of all is for the Government to clarify precisely who this tax applies to. Perhaps most shocking of all is the transitional provision in the Appendix that the tax will apply not just to shares acquired from 1 March 2024, but also to those acquired before this date at an optional tax rate of 2% of gross sales value or 10% of net gains.

At present, Malaysia does not have a Capital Gains Tax (CGT) regime, with the exception of Real Property Gains Tax (RPGT), which only applies to gains arising from the disposal of real property located in Malaysia or shares in a Real Property Company (RPC).

As announced by the Prime Minister and Finance Minister, YAB Dato' Seri Anwar Bin Ibrahim in the 2024 Budget, Malaysia now intends to implement a new CGT at the rate of 10%, which would apply to companies that dispose of local company shares that are not listed on the Malaysian Stock Exchange (Bursa Malaysia). This tax will apply to shares acquired from 1 March 2024 onwards, although a transitional rule will also apply for shares acquired before 1 March 2024.

Specifically, as set out in the Appendix to the Budget Announcement, the new CGT is set to be implemented with the following rates and effective dates:

Shares Acquisition Date	CGT Rate
Before 1 March 2024	The taxpayers may choose between: i. 10% on the net gain on disposal of shares; or ii. 2% on the gross sales value.
From 1 March 2024	10% on the net gain on disposal of shares

Notwithstanding the above, in addition to disposals of listed shares being exempt from this new CGT, additional exemptions will be granted to gains derived from:

- Disposals of shares related to Initial Public Offerings approved by Bursa Malaysia;
- Disposals of shares that are undertaken as part of an internal group restructuring; and
- Disposals of shares that are derived by Venture Capital Companies.

Beyond the above outline given by the Prime Minister and Finance Minister in his budget speech, there are not yet any further details regarding the application of this new tax or the abovementioned exemptions. It is expected that further explanation and clarifications will be given when the Finance Bill and further guidelines are released. While this announcement was not unexpected, a number of questions and challenging issues immediately arise from this tax.

Which taxpayers precisely is this tax intended to apply to

In the Prime Minister and Finance Minister's Announcement, he referenced that this tax is to apply to disposals of shares in unlisted local companies **by** Malaysian companies. This suggests that this tax will only apply to the gains of Malaysia incorporated companies. However, the English translation of the Announcement does not specify at all which taxpayers this applies to while the Appendix to the Announcement refers to gains 'for companies'. From this ambiguity stems a number of questions:

- Is the tax intended to apply to Malaysian companies only, or both Malaysian and foreign companies?;
- If foreign companies, how would the tax be collected and would it even be extended to include the taxation of indirect transfers of Malaysian companies (in a similar manner to rules introduced in China, India, Indonesia and Vietnam);
- Is this tax only intended to apply to companies or would individuals also be included. Based on the previous Budget Announcement and the wording of the Appendix suggest that this tax is only intended to apply to companies, but it is not completely clear at this stage.

Further clarifications will be eagerly awaited in the hope that some of the above ambiguity will be removed by making clear precisely which taxpayers are intended to be caught by this tax. To the extent that it is intended to apply only to Malaysian taxpayers, we may see a rebalancing of investment structures take place to remove Malaysian holding companies from structures where they are no longer essential. In this regard, the ability to quickly restructure ahead of 1 March 2024 is somewhat thwarted by the suggested that this tax is also meant to apply to investments made before 1 March 2024.

The transitional rules for existing investments

While it was anticipated that a CGT was coming and that it would apply to new investments, a more unexpected development appeared in the Appendix to the Budget Announcement which stated that in respect of shares acquired before 1 March 2024, taxpayers could opt to be taxed at either 10% of net gains or 2% of gross sale value. This means that sales of any existing investments in non-listed companies would also be subject to this tax (though with an option of 2% on gross sales value as an alternative). It is not clear, however, if this measure would only apply to investments disposed of in 2024 or earlier. If the former, then we may see a move to rapidly transfer local company shares to taxpayers that are outside of the scope of this tax (individuals or foreign companies, to the extent it is confirmed that they are not subject to this tax.

Exemptions on internal group restructuring

As stated in the Announcement and further referred to in the Appendix, there will be certain exemptions from this tax, most notably of all being any gains derived from internal group restructuring. The details of how this exemption will apply are not yet known and it will be very important to note, for instance:

- What the definition of ‘group’ will be in this context including minimum shareholding percentages;
- Whether or not this exemption will apply to international groups. If so, you may expect to see international groups moving their subsidiaries out from under Malaysian holding companies under group restructuring exercises so that they may be disposed of later by jurisdictions that do have capital gains exemptions
- Whether, to thwart the type of action mentioned in the preceding point, Malaysia introduces rules that any gains derived from internal group restructuring are only deferred at the time of restructuring, with the gains then triggered when the subsidiary is sold outside of the group.

The calculation of the gains and rules for set off

It is unsurprising that the Budget Announcement and its Appendix do not yet contain much detail as to how the gains are to be calculated. However, it will be important for taxpayers to study the Finance Bill and any guidance or implementing regulations that follow to see the precise calculation and set off mechanisms. A few key considerations on this include:

- Whether the tax is intended to apply to only realized gains or whether unrealized accounting gains in the books of companies would also be caught;
- Whether taxpayers may carry forward and deduct their capital losses against other future capital gains;
- Which expenses will be allowed for deduction against such gain

How the new CGT will interact with the existing RPGT Act

While Malaysia does not have an existing CGT regime, it does already tax gains derived from sales of real properties and real property companies at rates of 10% to 30%. There is no explanation as yet as to how the Government intends for these two rules to interact. For instance, will those transactions that are subject to RPGT be excluded from the new CGT rule, as they are already taxed, or will the RPGT Act be replaced entirely? As yet, there is no indication and it is hoped that further details will be released to make this clearer.

In conclusion, in many ways the introduction of this new CGT, that has far broader application than the already existing RPGT regime, represents a sea change in the Malaysian tax system. Malaysia appears to now be at a point where it seeks to re-balance the desire to be seen as an attractive low tax jurisdiction from an investment holding perspective with the need to derive greater tax revenues and increase the progressiveness of its tax system. There will be a great number of questions and debates that follow from the introduction of this tax as many taxpayers seek to determine the applicability of this tax to their own investments and structures and whether they need to undertake any new tax planning to mitigate any potential negative impacts to their future returns. Such taxpayers will be keenly awaiting the release of the Finance Bill as well as further guidelines and we will provide further updates as soon as they are released.

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