Taking stock of indirect taxes

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Comment

THIS year has seen significant developments in indirect tax, with key changes such as the sales tax on low-value goods (LVG), the increase in the service tax rate from 6% to 8%, an expanded scope of taxable services and a new excise duty on pre-mixed preparations.

Businesses have been kept busy and focused on ensuring compliance with these regulatory changes.

As Budget 2025 looms, the key update, if any, would be the likelihood of a reform to a more broad-based consumption tax system in Malaysia – a move that has been widely advocated both locally and internationally to broaden Malaysia's tax base.

While the potential reintroduction of the goods and services tax (GST) or value-added tax (VAT) has been widely debated, what other alternatives could be proposed to improve Malaysia's indirect tax regime in the upcoming budget?

The delayed high-value goods tax could see a revival.

In January this year, the excise duty for sugar-sweetened beverages rose to 50 sen per liter, and an excise duty of 47 sen per 100g was introduced on pre-mixed preparation products on March 1, 2024.

As the "War on Sugar" continues to curb non-communicable diseases, an additional tax on sugary drinks may be imposed.

The Prime Minister has stated that Budget 2025 will focus on strategies to mitigate inflation and address the rising cost of living.

Balancing the financial welfare of the rakyat with the need for additional revenue may perhaps favour a holistic adjustment over drastic changes to the current indirect tax system.

If an overhaul of the indirect tax is not on the cards, then housekeeping the existing indirect tax framework may serve as a temporary solution.

Sales tax: Time for a strategic review?

The sales tax has been a key contributor to Malaysia's indirect tax revenue, with RM18.3bil projected for 2024.

Currently, it is levied at the rate of 5% or 10% unless exempted (0%), based on tariff classification of the goods.

These rates have remained unchanged since the sales tax was reintroduced in 2018.

A review of the rates or reclassification of goods under the respective rates to better reflect the current global economic environment and supply chain may yield additional revenue to the country.

In tandem with this, it is crucial to prevent the sales tax from further cascading and increasing the cost of doing business.

While exemptions are available, they come with varying conditions and reporting requirements that businesses must comply with, or risk clawback of the tax exempted.

For example, a manufacturer of taxable goods (5% or 10%) can claim an exemption on inputs, which can be in perpetuity.

In contrast, a manufacturer of exempted goods (0%) may also qualify but must renew the exemption annually.

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Reporting can differ too; taxable goods require reports to be prepared, kept and submitted only upon request, whereas exempted goods require a separate report prepared, kept, and in some cases, submitted quarterly.

As our tax system moves to a self-assessment basis, standardising these conditions and simplifying reporting would help promote compliance, enable proper monitoring, reduce unintentional errors and more importantly, improve the ease of doing business in Malaysia.

Streamlining service tax intricacies

The second major tax revenue contributor is the service tax, imposed on prescribed taxable services.

In 2024, numerous changes have been implemented, with ongoing updates that businesses sometimes find challenging to navigate.

While the authorities have made commendable efforts to align the service tax legislation with business practices, the continuous changes and updates may require renegotiation of business and commercial terms, which adds to the challenges for businesses to manage.

A significant development in 2024 was the introduction of the service tax on logistics services – a critical component of the supply chain.

Although policies and guidelines have been issued for clarity, some uncertainty still exists around the rules for special areas and designated areas, as well as the conditions for the door-to-door exemption.

Given that the service tax represents an additional cost for businesses, it may be prudent for the government to simplify the conditions, applicability and consider offering leniency in the first year of new legislation or policies to avoid penalties for unintentional non-compliance due to uncertainty.

Is a shift to stricter compliance due?

If the government's aim is to distinguish between compliant and errant taxpayers, audits and stricter penalties could be enhanced.

Over the past few years, the government has commendably introduced several "carrots" such as the voluntary disclosure programmes to promote awareness, education and facilitation.

These include the Voluntary Disclosure and Amnesty Programme in 2022, the Voluntary Disclosure Programme in 2023, and the Customs Compliance Verification Audit Programme in 2024, all paired with penalty waivers.

However, it may now be time to shift towards the "stick" approach for defiant and delinquent taxpayers, as sufficient leniency has been granted.

Ride the wave of advanced technology

As governments worldwide invest in artificial intelligence (AI) and technology to enhance revenue collection systems, Malaysia should not overlook this opportunity.

With indirect tax being a transaction-based tax that generates large volumes of data, the use of AI is crucial.

The implementation of e-invoicing, although a direct tax initiative, represents a step towards broader automation.

It would be wise to assess how the information collected from e-invoicing can be leveraged to improve the efficiency of the indirect tax regime.

Businesses must be cognizant that information provided for e-invoicing purposes can and will be utilised for both direct and indirect tax assessments.

Reforming a tax system is not an overnight affair as it requires consideration of both legislation and the socio-economic impacts of the policies to the country.

In-depth studies and consultations are essential, which is why a long-term roadmap should be in place.

Pending an overhaul of the indirect tax regime, a practical interim measure would be to conduct a stock-take and enhance the existing system, including the Customs Act, Excise Act, Sales Tax Act and Service Tax Act, among others.

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