



Budget 2023: Special Legal Insights

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On 24.2.2023, the Unity Government re-tabled the long-awaited Budget 2023 (“**Budget**”). Beneficiaries include the EV and agriculture industries, MSMEs,¹ and M40s, who stand to receive various tax reductions and incentives. Apart from changes in tax rates for individuals and MSMEs, the newly proposed luxury tax and capital gains tax is also noteworthy.

In this article, we summarise the key tax measures and share our thoughts on the potential legal implications.

A. New Tax 1- Luxury Tax

The Government plans to tax luxury goods which exceeds a certain value, a concept introduced by the French more than a century ago in 1918. Being widely regarded as the birthplace of luxury, the French adopted a 3-fold classification of “luxury”:²

- (i) Articles of obvious luxury such as jewellery, antiques, perfumes, sculptures, watches and yachts;
- (ii) General articles which are considered luxury only when they exceed a certain price such as \$20 for suits, \$2 on imitation jewellery, \$50 on women’s costumes, \$100 on horses, \$500 on safes and motorcycles, \$8 on pleasure dogs, etc; and
- (iii) Spending in luxury establishments such as hotels and restaurants.³

Naturally, what was considered luxurious a century ago may not necessarily be perceived as such now. However, the test is largely similar: non-essential, luxurious or extravagant items.

Introducing Luxury Tax rather than GST may be seen as politically prudent, a tax on luxury goods consumed only by the wealthy would certainly be more acceptable to the public compared to a broad-based consumption tax like GST. The following are some of the possible methods for the implementation of Luxury Tax:

- (a) Increasing the existing sales tax rates for luxury goods (“**Option 1**”);
- (b) Imposing excise duty on luxury goods (as seen with the sugar tax implemented in July 2019) (“**Option 2**”); or

¹ Micro, Small and Medium Enterprise.

² E.L.Bogart, “Luxury Taxes”, The Bulletin of National Tax Association, June 1919, Vol. 4 No.9 pp.237-239; see also UK Parliament Hansard on Luxury Tax Vol.105 <<https://hansard.parliament.uk/Commons/1918-04-22/debates/93d93192-adbf-4164-b327-ee71d5a296fc/LuxuryTax>>.

³ Ibid.

(c) Enacting new legislation specifically targeting luxury goods ("**Option 3**"). See Select Luxury Items Tax Act in Canada which imposes luxury tax on aircraft, yachts, and certain motor vehicles that meet specific criteria with effect from 1st September 2022.⁴

Imposing Luxury Tax on goods through the existing Sales Tax Act 2018 or Excise Act 1976 (**Options 1 and 2**) present several challenges:

(a) Importantly, the HS (Harmonised System) Codes used under both Acts do not differentiate between luxury or non-luxury goods. For example, a women's handbag which falls under HS Code 4202 does not differentiate between a RM 500 handbag with a RM 50,000 one. Without a clear criterion to define luxury goods and their value, imposing luxury tax through these existing legislations would be difficult. Establishing clear and specific criteria to determine what qualifies as luxury goods would be imperative.

(b) Further, the Government should also consider imposing Luxury Tax at the retail level rather than the import / manufacturing level. This would improve transparency for consumers regarding the taxes imposed & prices increase. The latter by contrast may attract criticism for being opaque and resulting in cascading taxes along the supply chain.



Currently, sales tax and excise duty are only applied at the import/ manufacturing level, where the costs of these taxes/ duty are embedded in the price of the goods. Modifying the current sales tax structure to levy Luxury Tax at the retail level, similar to the implementation of sales tax on low-value goods (effective from 1st April 2023), could be a viable option.

Alternatively, the creation of a new piece of legislation for the imposition of Luxury Tax (**Option 3**) would be a better though less likely option. This would establish Luxury Tax as a distinct category of tax and allow for the definition of clear criterion on what qualifies as luxury goods. This would offer greater flexibility for future adjustments and expansion for the Luxury Tax to include luxury services, when required, such as fine dining experiences at Michelin-starred restaurants and exclusive club memberships.

Regardless, any modification to the existing tax structure could have long-term impacts and require further study. Ultimately, the effectiveness of Luxury Tax will depend on the Government's criteria for classifying goods as luxurious, and their implementation.

⁴ Select Luxury Items Tax Act (SC 2022, c 10, s 135)' (Justice Laws Website, 2022) <<https://laws-lois.justice.gc.ca/eng/acts/S-8.35/FullText.htm>> accessed 28 February 2023.



B. New Tax 2- Capital Gains Tax ("CGT")

Traditionally, gains on share disposals are non-taxable in Malaysia, unless it involves shares in a real property company (**RPC**) under the RPGT Act or if the disposer is engaged in the business of trading in shares. However, the Government has proposed to introduce a limited Capital Gains Tax (**CGT**) in 2024 on the disposal of unlisted shares by companies.

Neighbouring countries have CGT rates ranging from 0% (Singapore) to 22% (Indonesia):

i. Singapore - 0%

ii. Thailand - As Thailand has no separate capital gains tax law, Thailand's corporate tax law treats capital gains income derived by entities as normal assessable income subject to corporate income tax of 20%.

iii. Vietnam - Capital gains generally are taxed as ordinary income at the corporate income tax rate of 20%.

iv. Indonesia - Capital gains earned by a resident company generally are taxed as ordinary income at the corporate income tax rate of 22%. Gains on the sale of shares listed on the Indonesia Stock Exchange are subject to 0.1% of the transaction value. An additional final tax of 0.5% applies to founder shares on the share value at the time of an initial public offering (**IPO**), regardless of whether the shares are held or sold following the IPO.

Key considerations relating to the proposed imposition of CGT include:

(a) Determining a suitable CGT rate is crucial. A higher CGT rate than our neighbours could potentially affect the competitiveness of the Malaysian commercial market, particularly for foreign investors who have traditionally favoured Malaysia for not having a CGT regime.

(b) The decision to tax capital gains on listed shares only is curious, but not necessarily unwelcome. Corporate investors (individuals have already been excluded) may become more conservative with investments in unlisted companies. This may also dampen M&A activities. Companies intending to divest investments in unlisted companies may consider asset sales instead as an alternative to heighten tax efficiency. Companies intending to restructure or divest their interest in unlisted shares should consider accelerating their plans and keep abreast of updates regarding the proposed CGT regime.

Ultimately, the question remains whether the proposed CGT on unlisted shares is a precursor to introducing taxes on other types of capital goods in Malaysia.

C. Special Voluntary Disclosure Program ("SVDP") 2.0

The Special Voluntary Disclosure Program (SVDP) was previously introduced in 2019 (by the Inland Revenue Board) and in 2022 (by Customs) to offer remission of penalties at various rates. Budget 2023 proposes the reintroduction of SVDP with an extension that allows taxpayers a full 100% waiver on tax penalties for the period between 1st June 2023 to 31st May 2024, provided that the disclosure and payment of taxes/duties are made within the same period.

Past results have demonstrated that SVDP may increase tax compliance and awareness, and lead to better revenue collection. However, taxpayers should remain cautious with regards to the following issues:

(i) Can IRB/ Customs still audit taxpayers after a voluntary disclosure has been made on a particular issue/ for a relevant year of assessment? Will IRB/Customs issue a public ruling (not mere guidelines or press releases) to confirm that audits will not be conducted after voluntary disclosure?

(ii) Should taxpayers disclose issues based on differing legal interpretations, since IRB/Customs' interpretation may not be correct in law?

(iii) Should taxpayers disclose potential issues for time- barred years since these may not be subject to assessment?

To make an informed decision about whether to proceed with a voluntary disclosure, taxpayers should seek legal advice on the merits of their case, as such disclosure often entails signing an admission that the taxpayers have breached the relevant laws by filing incorrect tax returns. Even if taxpayers believe that they have a legitimate expectation that no further audits will be conducted, without written clarification or rulings, there is no guarantee that the IRB/Customs will not use the disclosed information to conduct additional audits.



D. Reduction of Individual Tax Rates for B40 & M40 & Increase for T20⁵

Chargeable Income (RM)	Current		Proposed			
	Tax Rate	Tax Payable	Tax Rate	Tax Payable	(Tax Savings)/ Additional	
	(%)	(RM)	(%)	(RM)	(RM)	(%)
35,001 - 50,000	8	1,200	6	900		
		1,800		1,500	(300)	-16.7
50,001 - 70,000	13	2,600	11	2,200		
		4,400		3,700	(700)	-15.9
70,001 - 100,000	21	6,300	19	5,700		
		10,700		9,400	(1,300)	-12.1
100,001 - 250,000	24	36,000	25	37,500		
		46,700		46,900	200	0.4
250,001 - 400,000	24.5	36,750	25	37,500		
		83,450		84,400	950	1.1
400,001 - 600,000	25	50,000	26	52,000		
		133,450		136,400	2,950	2.2
600,001 - 1,000,000	26	104,000	28	112,000		
		237,450		248,400	10,950	4.6
1,000,001 - 2,000,000	28	280,000	28	280,000		
		517,450		528,400	10,950	2.1
Over 2,000,000	30		30			

A tax resident with chargeable annual income of up to RM100,000 could enjoy tax savings of up to RM1,300 annually. On the other hand, a tax resident with chargeable income of up to RM1,000,000 is expected to pay RM10,950 in additional taxes.

However, the hike for higher income earners would widen the gap of rates with our neighbours. For instance, the highest rate in Singapore is 22% for income exceeding \$320,000 (equivalent to RM 1,051,299)⁶, whereas the rate in Malaysia for the same income bracket is 28%.

Over the past few decades, there has been a noticeable increase in the migration of our high-skilled workers to neighbours like Singapore. It is difficult to see how the increased tax rates will stem the flow. Unless measures are taken to provide incentives to retain these high-skilled workers, Malaysia will be likely to continue experiencing an outflow of talent.

Additionally, Malaysia may also find it challenging to compete with other countries to attract highly-skilled (and paid) expatriates.

⁵ Appendix for Budget 2023, p.2 & 3.

⁶ At the exchange rate of 3.28 SGD/ MYR.

E. Stamp Duty Exemption for Intergeneration Transfer

The Government has also announced a 100% stamp duty exemption with effect from 1 April 2023 on properties below RM 1,000,000 in value for transfers made between parents and children or between grandparents and grandchildren. For properties in excess of RM 1,000,000 in value, a 50% exemption/ remission will be given. It should be noted that this exemption is only applicable if the transferee is a Malaysian Citizen and is subject to any further conditions which may be imposed in the gazette order.

This is a significant development from the existing stamp duty rate of 1-4% (scaled rate based on sale price or market value of the property) that is applicable to transfer between grandparents and grandchildren with only 50% remission being applicable for transfer from parents to children. The proposal resolves a long-standing issue regarding transfers within the family. In fact, there are similar treatments for RPGT, where property transferred between parents and children or between grandparents and grandchildren would be deemed to result in a "no gain & no loss" position for the donor.⁷



Consideration should further be given to amending s.16 of the Stamp Act 1949 which effectively impose ad valorem duty on inter vivos gifts, unless it is transferred between parents and children (with 50% exemption)⁸ or between a husband and a wife (with 100% exemption).⁹

SECTOR FOCUS – WHO ARE THE WINNERS?

F. Electric Vehicles ("EV") Industry

The domestic EV industry stands to benefit from:

(a) Extending the full import duty exemption on components for locally assembled EV until 31.12.2027 (existing exemption ends on 31.12.2025);

(b) Extending the full excise duty and sales tax exemptions on locally assemble CKD EV until 31.12.2027 (existing exemption ends on 31.12.2025); and

(c) Existing full import duty and excise duty exemptions on imported CBU EV until 31.12.2025 (existing exemption ends on 31.12.2023).

In addition, tax incentives for manufacturers of EV charging equipment are available between now and 31 December 2025:

⁸ Stamp Duty (Remission)(No.2) Order 2019, Para 2.

⁹ Stamp Duty (Exemption) (No.10) Order 2007, Para 2.



Companies renting non-commercial EVs are given tax deduction under s.39(1)(k) of the Income Tax Act 1967 ("ITA") up to RM300,000 from YA 2023 to 2025 on the rental.

G. E- Cigarettes & Vapes

In a recent study, the Government reportedly missed the opportunity to collect approximately RM866 million in taxes last year from liquids containing nicotine used for vaping or electronic cigarettes.¹⁰

To address this, it is proposed that the imposition of excise duty be extended to liquids or gel containing nicotine used in e-cigarette and vape, with 50% of the collection to be earmarked for the Ministry of Health to improve the quality of healthcare services, in line with the Government's Generation End Game (GEG) policy.

The proposed move would also restore parity in tax treatment for the conventional tobacco industry. It is foreseeable that the Excise Duty Order 2022 would be amended to reflect this change. However, this move may drive the illegal smuggling of vaping and e-cigarette products. To avoid repeating the issues that plagued the tobacco industry, the Government should be cautious about setting the excise rate too high, as this could lead to increased smuggling through land, sea and duty-free zones.

To promote smoking cessation, the Government further declares 3 years of import duty and sales tax exemption for nicotine replacement therapy products.

H. MSMEs

Effective YA 2023, MSMEs are given a 2% reduction in their corporate tax rate from 17% to 15% for the first RM150,000 of the chargeable income, equivalent to RM3,000 tax savings.

MSMEs are company/LLP resident with paid-up capital of not more than RM2.5 million at the beginning of the basis period for a YA and gross income not exceeding RM50 million.

I. Agriculture & Food Industry

Public outcry of food shortages and steep prices over the past few years has driven the Government to introduce tax incentives for the agriculture and food industry:

(a) Accelerated Capital Allowance of 100% on automation equipment is expanded to now include the agriculture sector, with the aim of improving productivity and efficiency. The capital expenditure threshold is also increased up to RM10million. The condition is that the scope of automation must include adaptation of Industry 4.0.

(b) 10-year 100% income tax exemption for new food production project is extended until 31 Dec 2025, similarly for 5-year exemption for an expansion project. The scope is also extended to include agriculture- based project on Controlled Environment Agriculture ("CEA").¹¹

(a) 100% exemption on statutory income from YA 2023 to YA 2032; and

(b) 100% Investment Tax Allowance for a period of 5 years and can be set off against up to 100% of the statutory income for each year of assessment.

¹⁰ Ben Tan, 'Budget 2023: Vape liquids with nicotine to be taxed, receipts to help fund (Malaymail, 24th February 2023) <<https://www.malaymail.com/news/malaysia/2023/02/24/budget-2023-vape-liquids-with-nicotine-to-be-taxed-receipts-to-help-fund-health-ministry/56583>> accessed 28 February 2023.

¹¹ CEA, "vertical farming" or "indoor farming" is a method of creating fully controlled environments for growing plants. Everything plants need at their various growing stages is provided artificially, including water, temperature, humidity levels, ventilation, light and CO₂.

(c) ACA 100% on qualifying CA and income tax exemption of 100% equivalent to qualifying CA for closed house breeding systems for the poultry industry.

The tax incentives seek to encourage automation which has the potential to increase productivity and yield, promoting food security and reducing the country's dependence¹² on imported food. However, from a legal perspective, industry players should carefully scrutinise the conditions imposed by the various investment and tax agencies for such incentives. This is to prevent potential allegations of non-compliance which could result in retrospective clawback of taxes by the IRB.

Conclusion

The core message sent by the Government is that they are taxing the rich and reducing the burden of the poor through tax policy. Tax incentives have also been given to key industries in an effort to either mitigate or address current day concerns of the Rakyat. Yet, these tax policies will remain mere talking points if they are not accurately reflected in the Finance Bill. It is therefore imperative for the Finance Bill to capture the spirit and essence of these tax policies. A comprehensive analysis of the Finance Bill will be conducted once it is available. **LH-AG**

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¹² According to the Department of Statistics Malaysia, the country's self-sufficiency ratios are low for agricultural items such as beef (22.2%), for which we spent RM2.2 billion on imports, mutton (9.6%) with RM879.4 million spent on imports, chilli (30.9%), and rice (63%).

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