LEGAL HERALD

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30TH ANNIVERSARY

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KDN PP 12853/07/2012 (030901

E-Money As A Shariah-Compliant Payment Instrument

By Megat Hizaini Hassan, Nur Liana Azmi and Saiful Akmal Suhaimi

Electronic money, widely known as e-money, is a payment instrument recognised under the Financial Services Act 2013 (**FSA**) and the Islamic Financial Services Act 2013 (**IFSA**). The usage of e-money has evolved significantly, given the increased usage of e-wallets for online retail transactions in Malaysia. In this article, the authors highlight Shariah-compliant e-money, as specifically outlined in the recent Bank Negara Malaysia policy document on e-money.

Shariah-compliant e-money is recognised by the Shariah Advisory Council (**SAC**) of Bank Negara Malaysia (**BNM**) pursuant to a ruling issued in 2020[1] (**SAC E-Money Ruling**) which is applicable to the approved issuers of Shariah-compliant e-money under the IFSA and Section 15(1)(e) of the FSA. The SAC has made a ruling that e-money is a permissible payment instrument under Shariah, provided that such a transaction is structured based on the appropriate Shariah contract(s). One of the applicable Shariah contracts for e-money is the agency contract (wakalah), whereby the approved e-money issuer (**EMI**) acts as an agent of the user to make payments (wakil bi ad-daf'i) to the merchant.

The funds received from the user must be kept in a Shariah-compliant trust account or a dedicated deposit account.[2] Such funds, being construed as a form of loan (qard) from the user to EMI, may be utilised by the EMI for investment purpose and subsequently entitled to any return generated from the investment.

1 SAC's 201st Meeting and 26th Special Meeting on 29 and 30 January 2020.
2 IFSA 2013, *s 137.*

BNM Policy Document on Electronic Money (E-Money)

BNM recently issued a policy document on Electronic Money (E-Money) (**PD**), which supersedes the BNM Guidelines on Electronic Money issued in 2008. The issuance of the PD was preceded by the circulation of an exposure draft for public written feedback in 2021. The PD takes effect on December 30, 2022, except for certain provisions that will become effective on December 30, 2023.[3]

In respect of Islamic e-money,[4] the PD provides that EMI must ensure that such e-money complies with the rulings of the SAC of BNM and relevant Shariah standards.

To ensure compliance with Shariah at all times, the EMI's board and senior management must appoint a qualified individual, company or (if applicable) an existing Shariah committee within their group as a Shariah adviser. The PD includes further requirements for the appointment of the Shariah adviser of such Islamic e-money.

In addition, the PD introduced various requirements for EMI operating in Malaysia, which are outlined below:

a) Categories of E-Money Issuers [5]

EMI can be classified into the following categories:

(i) Eligible EMI: EMI that have a substantial market presence and meet the criteria set out in Appendix 1 of the PD. They are subject to higher regulatory expectations.

(ii) Standard EMI: the default category of EMI that is approved under Section 11 or Section 15(1)(e) of the Financial Services Act 2013 (**FSA**) or Section 11 of the Islamic Financial Services Act 2013 (**IFSA**), but do not meet the criteria for eligible EMI.

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3 Policy Document on Electronic Money (E-Money) 2022, *Para 7.1.*
4 Policy Document on Electronic Money (E-Money) 2022, *Para 12.*
5 Policy Document on Electronic Money (E-Money) 2022, *Appendix 1 and 2, Para 5.*

(iii) Limited Purpose EMI: standard EMI whose business meets the criteria of limited purpose e-money listed in Appendix 2 of the PD.

Non-Bank EMI – though not a separate category, the PD also introduces the concept of "non-bank EMI", which refers to EMIs that are not licensed banks, licensed Islamic banks, or prescribed institutions/ development financial institutions.[6]

b) Board of Directors[7]

An EMI must only appoint as directors such individuals who are not disqualified under Section 59(1) of the FSA or Section 68(1) of the IFSA and have been assessed as meeting the "fit and proper" requirements specified by BNM. In addition, the EMI's director must not be an active politician. The PD includes provisions on the composition of the board, including a requirement that at least two-thirds of board members be non-executive directors, and for eligible EMIs, at least one-third be independent directors.

c) Minimum Capital Funds for Non-Bank EMI[8]

A non-bank EMI is required to maintain a minimum amount of capital funds as prescribed by BNM under the FSA and the IFSA. The required capital funds are to be computed using a formula provided in Appendix 4 of the PD. To take into account the initial investments, particularly technology investments, BNM has excluded intangible assets such as goodwill, licences and intellectual properties from the computation of minimum capital fund.

This treatment is consistent with BNM's approach to capital requirements for other regulated entities.

d) Safeguarding of Funds[9]

A non-bank EMI must deposit the collected funds in a trust account with a banking institution, and these funds can only be used for refunding customers, paying merchants for settled transactions conducted by customers, or paying another e-money account or bank account resulting from a credit transfer transaction conducted by the customer. Furthermore, a non-bank EMI with total outstanding e-money liabilities of less than RM1 million may safeguard the collected funds exchanged for e-money issued using a bank guarantee or other methods, provided that the effectiveness of the method is equivalent to a bank guarantee or trust account and has received BNM's prior written approval.

To further safeguard customers' funds, a non-bank EMI must ensure that the funds in the trust account are always sufficient to cover the total outstanding e-money liabilities. If the total outstanding e-money liabilities exceed the funds in the trust account, a non-bank EMI is encouraged to deposit additional funds into the trust account within one working day.

A non-bank EMI must also have sufficient liquidity for its daily operations, and at a minimum, the PD requires an EMI to maintain a liquidity ratio of one.

e) Outsourcing Arrangement[10]

According to the PD, EMIs must obtain BNM's prior written approval before entering into a new material outsourcing arrangement or making material changes to an existing one. The PD outlines several considerations for EMIs to determine whether an outsourcing arrangement is considered material.

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6 Policy Document on Electronic Money (E-Money) 2022, *Para 5.*
7 Policy Document on Electronic Money (E-Money) 2022, *Para 9.*
8 Policy Document on Electronic Money (E-Money) 2022, *Para 15.*
9 Policy Document on Electronic Money (E-Money) 2022, *Para 16.*
10 Policy Document on Electronic Money (E-Money) 2022, *Para 18.*

f) Account management[11]

EMIs must obtain BNM's prior written approval if there is an increase in wallet limits that results in the limit exceeding RM5,000 or if there are changes to the functionality and product features of the e-money. If such increase in wallet limit is below the RM5,000 threshold and does not involve changes to the functionality and product features of the e-money, EMIs must notify BNM at least 14 days prior to such increase. A similar condition applies to "white labelling" arrangements entered into by EMIs.

E-money balance refunds to customer accounts must be made within 14 days (for normal cases) or 30 days (for complex cases) from the date the claim is made.

g) Cross-selling financial products or services[12]

A non-bank EMI is prohibited from using its e-money platform or system to promote or cross-sell any financial products or services except with BNM's prior approval. Any arrangements to promote or cross-sell any financial products or services must be reviewed and approved by EMI's board before being submitted to BNM for approval. A non-bank EMI must communicate clearly to its customers the demarcation of roles between the non-bank EMI in respect of its e-money business and the provider in respect of any promoted or cross-sold products or services on the non-bank EMI's e-money platform or system.

h) Regulatory process[13]

EMIs must seek BNM's prior written approval for any significant proposed changes to its e-money business model or changes that alter the risk profile of its business model. In addition, the PD requires an EMI to notify BNM before establishing or relocating its offices in or outside Malaysia, and before appointing an auditor, chairman, director, or CEO. This notification must be submitted to BNM 14 days prior in advance of these events.

In addition, an EMI is required to be a member of an approved Financial Ombudsman Scheme, and membership must begin on the date such EMI begins operation.

The gradual substitution of the traditional method of payment with an electronic payment system via e-money signifies the rapid evolution of the digitalisation of financial services in the world today. The issuance of the PD together with the SAC E-Money Ruling have been highly anticipated and are necessary to ensure the ongoing security and reliability of Shariah-compliant e-money in Malaysia, as the position is clear that e-money is ruled as a permissible payment instrument under the Shariah, provided that it employs the appropriate Shariah contract and is in compliance with the requirements of BNM.

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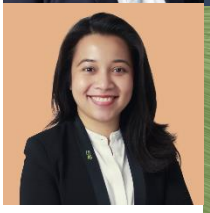
11 Policy Document on Electronic Money (E-Money) 2022, *Paras 20 and 21.*
12 Policy Document on Electronic Money (E-Money) 2022, *Para 22.*
13 Policy Document on Electronic Money (E-Money) 2022, *Paras 32 and 34.*

Handling Flexible Working Arrangement (FWA) Applications



By Shariffullah Majeed and Arissa Ahrom

The recent amendments to the Employment Act 1955 ("**EA**") includes a provision which affords employees the right to apply for a flexible working arrangement ("**FWA**") to vary their hours, days or place of work.[1] This marks a formal parliamentary recognition of such an arrangement which was catalysed by the pandemic that made a widespread adoption of remote work necessary. In fact, it was stated during the Second and Third Reading of the Employment (Amendment) Bill 2021 in Parliament that the FWA provision is aligned with the hybrid working culture shift which resulted from the pandemic.[2]

Pursuant to section **60P** (**1**) of the EA, an application for FWA is subject to the provisions in relation to rest days, hours of work, holidays and other conditions of service or anything contained in the contract of service. Hence, any variation to the hours, days or place of work must be done within the confines of the EA or in the terms of the employment contract.

What shall employers do upon receipt of FWA application?

An application for FWA shall be made by employees in writing and in the form and manner as may be determined by the Director General.[3] At this juncture, there has not been any fixed form or manner in which an application for FWA shall be made.

Therefore, in the absence of any internal policy which sets out the form or manner for FWA applications, employers should readily accept applications in any written form. For example, via e-mail, letter or WhatsApp.

Upon receipt of such written application, an employer shall be brought to either approve or refuse the application within 60 days and inform the employee of its decision in writing.[4] If the employer refuses the application, grounds of the refusal must be stated.[5] It must also be noted that the EA does not specify the grounds in which an employer may refuse an application for FWA. Thus, employers are not obliged in any circumstances to approve such applications.

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1 *Section 60P(1)* of the Employment (Amendment) Act 2022.
2 DR.21.03.2022 at p. 27.
3 *Section 60Q(1)* of the Employment (Amendment) Act 2022.
4 *Section 60Q(2)* of the Employment (Amendment) Act 2022.
5 *Section 60Q(3)* of the Employment (Amendment) Act 2022.

In any event, it is advisable for employers to only refuse an application for FWA on reasonable grounds. For example, where such an arrangement is not practicable or viable in view of the nature of the employee's job. This is particularly where the nature of the job requires the employee to be at a specific location or work during specific hours.

Factors to consider in respect of FWA applications

According to a survey conducted in 2021, 48% of the respondents in Malaysia expressed a preference to flexible working policies post-pandemic[6] as employees increasingly value a healthy work-life balance. It is clear from the implementation of FWAs in organisations worldwide that such an arrangement is made essential in the modern-day workforce.

When implemented effectively, FWAs can boost productivity and reduce issues of tardiness or absenteeism in an organisation as employees spend less time commuting to work and have more scheduling freedom.

While it is obvious that employers must consider the nature of an employee's job in deciding whether to approve or refuse an application for FWA, employers ought to also consider, among others, the following:

(a) Whether the organisation already has a FWA Policy in place to establish the rules and procedures of FWA;

(b) Whether the organisation is equipped with tracking and management tools to monitor and track the employee's performance and productivity;

(c) Whether the organisation has in place sufficient cybersecurity measures to prevent cyber security hazards; and

(d) Whether the employee has sufficient work from home facilities that would enable him / her to perform his / her obligations efficiently.

6 Randstad, '48% of respondents in malaysia wants flexible work arrangements after the pandemic: randstad work monitor' (Randstad, 18 February 2021) <*https://www.randstad.com.my/hr-trends/workforce-trends/1-in-2-respondents-wants-flexible-work-arrangements/*> accessed 9 February 2023.

FWA Policy

Therefore, in order for an effective implementation of FWA, employers should ensure that an FWA Policy is in place to provide clear guidelines to the management and employees in relation to the rules and procedures of the arrangement. Essentially, the policy should contain comprehensive provisions regarding the FWA application process, conditions for approval and / or refusal, the employee's obligations and employer's expectations. It is also imperative that the policy contains specific and structured procedures to address disciplinary and performance issues remotely to avoid any uncertainties and inconsistencies in the organisation's practices.

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Could Artificial Intelligence Replace Lawyers In Malaysian Courts?

By G. Vijay Kumar and Nicole Shieh E-Lyn

'ChatGPT-4 aces the bar with a score around the top 10% of test takers' 'Robot lawyer to use AI in Court for the first time...' 'ChatGPT as a replacement for human lawyers?
'Colombian judge says he used ChatGPT in ruling'

These headlines are dominating the news - and they are not clickbait!

An artificial intelligence ("**AI**") program, ChatGPT-4, has passed a simulated bar exam with a score around the top 10% of test takers.[1]

This development comes on the heels of a law school dean co-authoring a 14-page law article in one hour with the assistance of ChatGPT.[2] Without the assistance of AI, this task could have taken weeks, if not months. Meanwhile, a judge in Colombia used ChatGPT as a tool in his judgment in an insurance case.[3]

For the first time in history, there were plans for an AI legal assistant, dubbed the "*world's first robot lawyer*", to take on a case in a United States court to help a defendant fight a traffic ticket case.[4] Created by DoNotPay, the AI would have run on a smartphone and listened to court arguments in real-time, before telling the defendant what to say via an earpiece.

Any fines imposed would have been covered by DoNotPay.

The AI will not automatically react to everything it hears in court. Instead, it would listen to the arguments and analyse them, before providing instructions on how to respond. The company's ultimate goal is to have AI replace some lawyers altogether, saving litigants money. However, DoNotPay subsequently announced that those plans will be halted for now, due to concerns about the legality of the usage of AI in Court.[5]

Nonetheless, the proposal of utilising AI to represent litigants in court, altogether replacing lawyers, is an interesting prospect and is certainly one worth examining.

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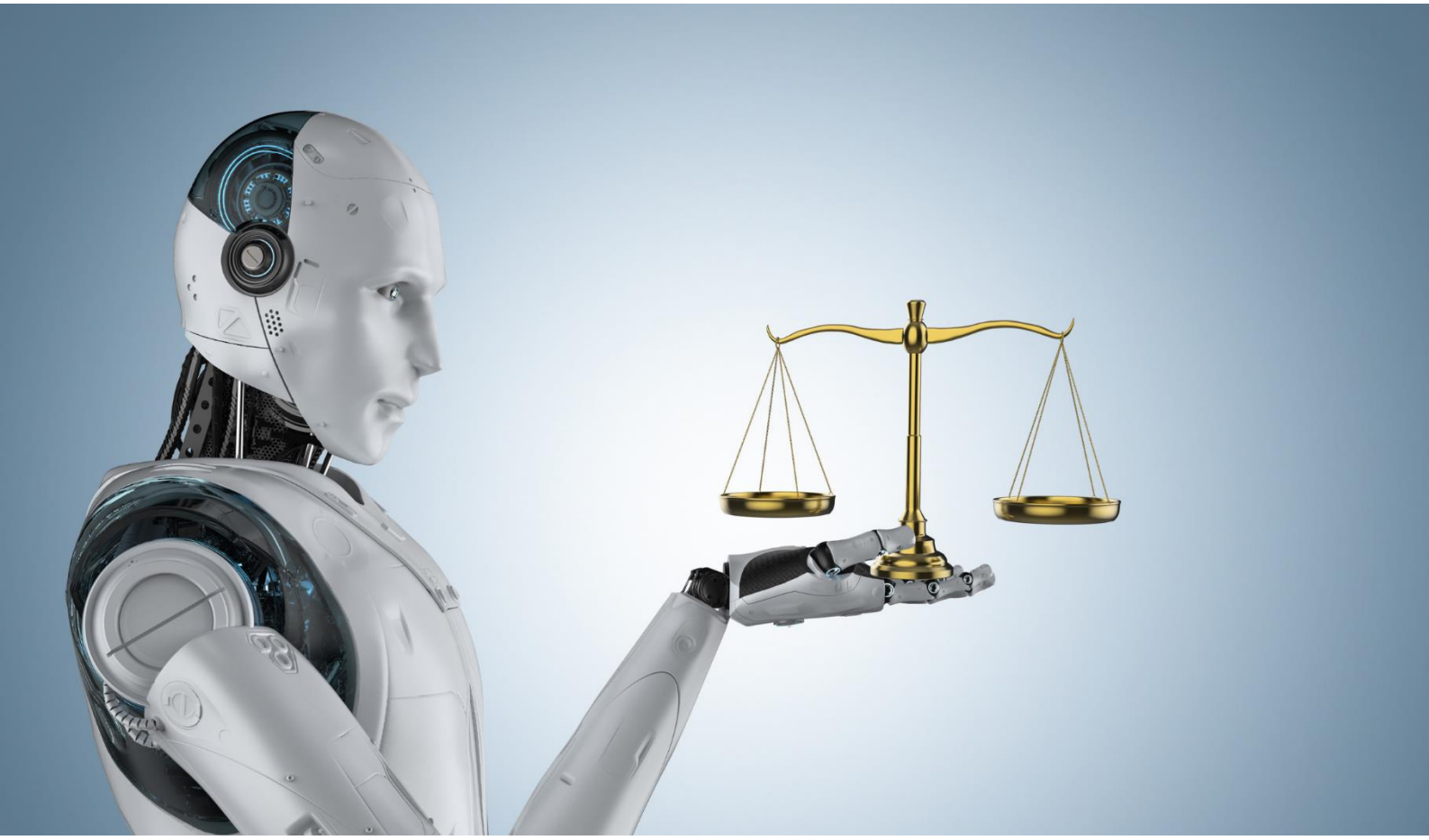
1 OpenAI, 'GPT-4' (OpenAI, 14 March 2023) <*https://openai.com/research/gpt-4*> accessed 25 March 2023 .
2 Open AI's Assistant and Andrew M. Perlman, 'The Implications of OpenAI's Assistant for Legal Services and Society' (Perlman, 5 December 2022) <*https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4294197*> accessed 17 February 2023.
3 The Guardian, 'Colombian judge says he used ChatGPT in ruling' (The Guardian, 3 February 2023) <*https://www.theguardian.com/technology/2023/feb/03/colombia-judge-chatgpt-ruling*> accessed 15 February 2023.
4 New Scientist, 'AI legal assistant will help defendant fight a speeding case in court' (New Scientist, 4 January 2023) https://www.newscientist.com/article/2351893-ai-legal- assistant-will-help-defendant-fight-a-speeding-case-in-court/? accessed 19 February 2023 ; see also: New York Post, "Robot lawyer' powered by AI will help fight speeding ticket as it takes first case in court' (New York Post, 5 January 2023) <*https://nypost.com/2023/01/05/robot- lawyer-powered-by-ai-will-help-fight-speeding-ticket-as-it-takes-first-case-in-court*> accessed 19 February 2023.
5 CBS News, 'AI-powered "robot" lawyer won't argue in court after jail threats' (CBS, 25 January 2023) *https://www.cbsnews.com/news/robot-lawyer-wont- argue-court-jail-threats-do-not-pay/*> accessed 17 February 2023.



Can AI replace lawyers in Malaysian courts?

We know that AI already plays an increased role in the criminal sentencing of defendants in Malaysia. In February 2020, a Sabah court used AI to help mete out a sentence in a drug possession case.[6] This case was a pioneer effort towards plans to provide judges and judicial officers with AI to minimise disparity in criminal sentences.[7]

The million-dollar question is – could AI eventually replace a lawyer in Malaysian courts altogether?

Right of audience

In Malaysia, only an Advocate and Solicitor of the High Court who is a 'qualified person' under the Legal Profession Act 1976 and holds a valid practising certificate has a right of audience in court.[8]

AI systems are not legal persons in law, therefore it is clearly not a 'qualified person' to appear in court. So, how could AI be used to present arguments in Malaysian courts? Could self-representing litigants in Malaysian courts use an earpiece for AI to tell them what to say and do in real-time?

There are several challenges to the implementation of this in Malaysia.

Usage of electronics in court

Firstly, the usage of earpieces (such as Apple AirPods) by litigants in Malaysian courts are unlikely to be allowed. The 'Open Court Etiquette' published by the Office of the Chief Registrar of the Malaysian Federal Court clearly states that mobile phones, pagers and other electronic devices are to be switched off while court is in session,[9] and these rules are strictly enforced by court bailiffs.

The recent implementation of remote court hearing protocols signifies that the Malaysian judiciary has shown their willingness to depart from such etiquette rules to accommodate the use of technology.

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6 PP v. Denis P Modili [2020] 2 SMC 381 (Magistrate Court, Kota Kinabalu); see also Artificial Intelligence (AI), e-Kehakiman Sabah and Sarawak, available online at <*https://ekss-portal.kehakiman.gov.my/portals/web/home/article_view/0/5//1*>.
7 The Right Honourable Chief Justice of Malaysia, Tan Sri Datuk Seri Panglima Richard Malanjum, 'Opening of the Legal Year 2019 Speech' dated 11.1.2019, available online at <*https://www.kehakiman.gov.my/sites/default/files/OLY%202019%20CJ%27s%20Speec h%20-%20Final 0.pdf*> at paragraph 18.
8 *Sections 11* and *29* of the Legal Profession Act 1976.
9 Office of the Chief Registrar, Federal Court of Malaysia, 'FAQ – Open Court Etiquette', available online at <*https://www.kehakiman.gov.my/ms/faq-open-court-etiquette*> at item 10.

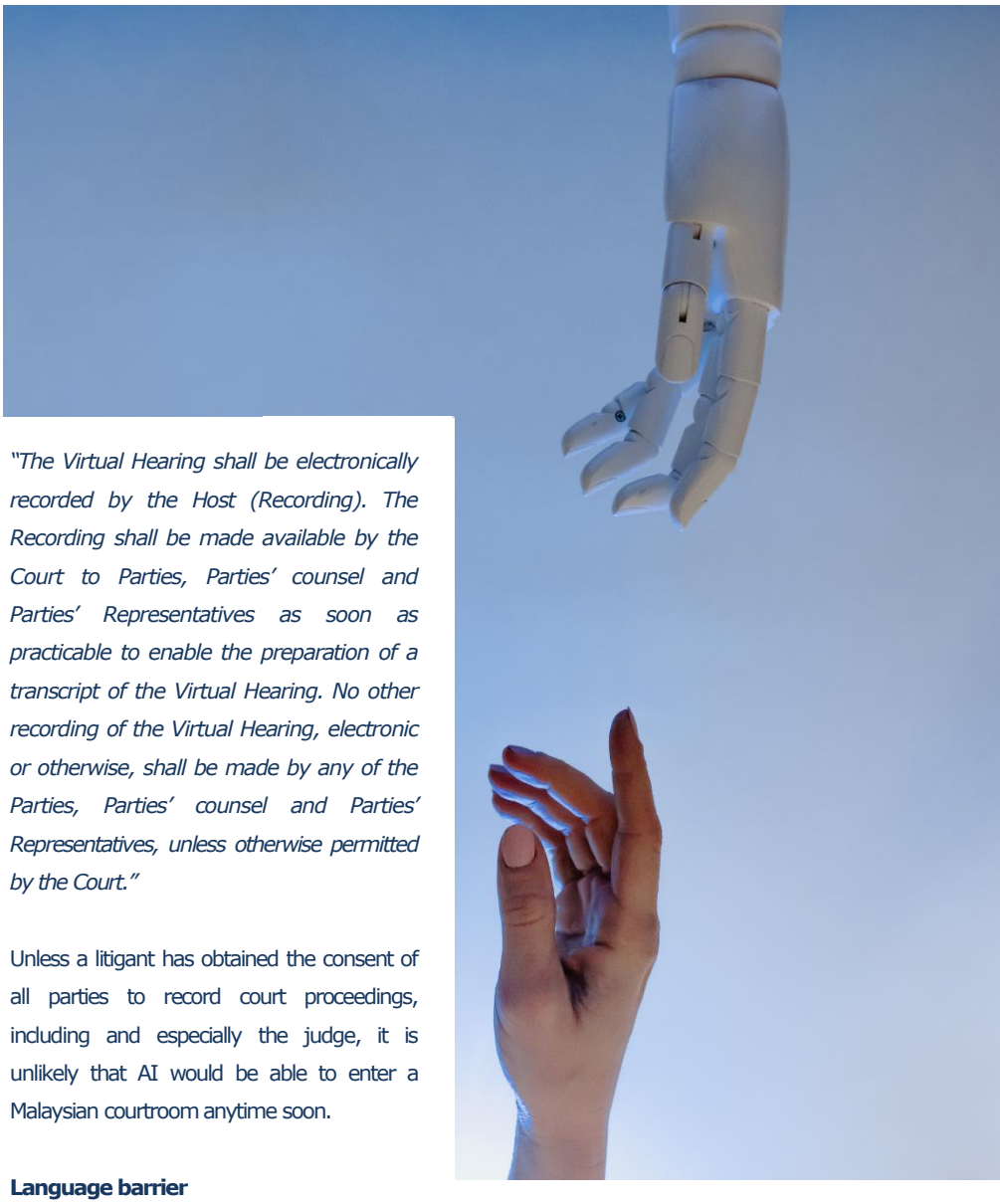
In practice, lawyers use electronic devices such as laptops during hearings. With that said, the usage of laptops by lawyers during court proceedings and the usage of AI earpieces by litigants are two different things.

DoNotPay had proposed to circumvent such practical hurdles in the United States by determining which courts allow defendants to wear hearing aids, some versions of which are Bluetooth-enabled. However, as DoNotPay's plans have been scrapped for now, this method remains untested.

Recording of court proceedings

There is, however, another major issue that would need to be considered for AI to work – court proceedings would technically have to be recorded before AI is able to propose legal arguments in real-time. In order for the AI to provide consistent and coherent legal arguments throughout court proceedings, it would have to retain the information it has been fed. This means that the AI would retain a transcript of the court proceedings it hears through the earpiece worn by the litigant.

The 'Open Court Etiquette' expressly prohibits court recordings in either audio or visual form.[10] The High Court recently reiterated the following court directions applicable to virtual hearings:[11]



"The Virtual Hearing shall be electronically recorded by the Host (Recording). The Recording shall be made available by the Court to Parties, Parties' counsel and Parties' Representatives as soon as practicable to enable the preparation of a transcript of the Virtual Hearing. No other recording of the Virtual Hearing, electronic or otherwise, shall be made by any of the Parties, Parties' counsel and Parties' Representatives, unless otherwise permitted by the Court."

Unless a litigant has obtained the consent of all parties to record court proceedings, including and especially the judge, it is unlikely that AI would be able to enter a Malaysian courtroom anytime soon.

Language barrier

Even if the abovementioned practical issues can be overcome, there lies another major barrier to the usage of AI in Malaysian courtrooms.

'Sorry, I am unable to understand. Please try again.'

Does this sound familiar? Most of the existing AI voice assistants, such as Siri and Alexa, are western-centric and primarily only fully understand western languages and accents.

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10 Office of the Chief Registrar, Federal Court of Malaysia, 'FAQ – Open Court Etiquette', available online at <*https://www.kehakiman.gov.my/ms/faq-open-court-etiquette*> at item 9.
11 Celcom (Malaysia) Bhd & Anor v. Tan Sri Dato' Tajudin bin Ramli & Ors and another case [2022] MLJU 00178, at paragraph 10.

However, there are multiple languages frequently used in Malaysian courts, including Malay, English, Chinese and Tamil. We also have multiple dialects, including Hokkien, Hakka, Cantonese, Kelantanese Malay dialect, Sarawakian Malay dialect, and numerous others. Further, the accents used by Malaysians may not be readily understood by western-programmed AI.

Therefore, until and unless AI is programmed to understand all languages, dialects, and accents of Malaysians, it may not be feasible for AI to be utilised in Malaysian court proceedings.

Attribution of liability for loss or damage caused by AI

It is trite that a lawyer's actions which prejudice their clients can constitute malpractice, and they may be sued for professional negligence. Lawyers are also bound by specific duties and rules pursuant to the Legal Professional (Practice & Etiquette) Rules 1978, which, amongst others, stipulates that a lawyer's paramount duty is to the Court.

How would this apply to AI?

It has been held in England and Wales that an automated system cannot in itself be regarded as an 'agent' because only a person with a 'mind' can be an agent in law.[12] This position is echoed in the US – 'robots cannot be sued'.[13]

Since AI does not have separate legal personality, there is an issue with the determination of liability in relation to the acts and/or omissions of AI. Could the acts and/or omissions of AI acting autonomously be attributed to a party involved in the supply of the AI? This might include: the AI software programmer, the person licensing and distributing the system, the system tester, the operator of the AI system etc.

Our existing laws simply do not have the answers to these questions. As it stands, a litigant using AI in a Malaysian court would have to fully bear the risks of doing so without potentially any recourse if something goes wrong. In fact, the ChatGPT chatbot comes with a legal disclaimer which expressly informs users: "It is important to note that ChatGPT is not a legal expert and cannot provide accurate or reliable legal information or advice."[14]

Final thoughts

Could AI lawyers replace lawyers in Malaysian courts altogether? We conclude that it is unlikely to do so, not in the foreseeable future anyway.

The practical difficulties for the complete substitution of Malaysian lawyers by AI are abundant. At this juncture, an AI is only capable of executing a pre-assigned task based on the data and knowledge input by humans, which still involves a degree of subjectivity. Simply put, what AI knows is somewhat limited to the ambit of knowledge it is fed. In fact, OpenAI has acknowledged that ChatGPT's responses might not always be accurate.[15]

Lawyers are required to think outside the box in performing their duties. This would include coming up with legal strategies and solutions for clients and dealing with cross-examination points during trial.

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12 Software Solutions Partners Ltd, R (on the application of) v. HM Customs & Excise [2007] EWHC 971, at paragraph 67.
13 United States v. Athlone Industries, Inc., 746 F.2d 977, 979 (3d Cir. 1984), U.S. Court of Appeals for the Third Circuit, at paragraph 2 of the Opinion of the Court.
14 s 16 Attorney At Law Magazine, 'ChatGPT and Legal Content Marketing' (Attorney At Law, 9 January 2023) <*https://attorneyatlawmagazine.com/legal-marketing/content/chatgpt- and-legal-content-marketing#chatgpt-itself-recommends-against-using-it-to-create- content*> accessed 16 February 2023.
15 Business Insider, 'ChatGPT 'may make up facts,' OpenAI's chief technology officer says' (Business Insider, 7 February 2023) <*https://www.businessinsider.com/chatgpt-may- make-up-facts-openai-cto-mira-murati-says-2023-2*> accessed 20 February 2023.

Litigators undergo years of practical training to hone their advocacy skills. Even if AI is programmed to do so, it will be limited in capacity. There are many varying factors to be considered in arguing a case in court. There would be immense difficulty for AI, without body language and other subconscious signals, to supersede the capability of a human litigation lawyer.

Perhaps, the more relevant question should be – how AI and Malaysian lawyers can co-exist in legal practice?

The adoption of technology in legal practice has generally benefitted the Malaysian legal industry. Lawyers who take it a step further and embrace the potential of AI to enhance their practice only stand to benefit from it. The potential of AI in performing assistive legal tasks is endless, from generating forms and analysing voluminous documentary evidence, to writing briefs and conducting legal research. Lawyers keen on doing so should watch the AI space for the latest news, or perhaps even start by experimenting with an AI chatbot.

With the plethora of advancements, lawyers should look to adapt to change and incorporate technology, or risk being left behind.

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Budget 2023: Special Legal Insights

By Dato' Nitin Nadkarni, Jason Tan Jia Xin, Ivy Ling Yieng Ping, Chris Toh Pei Roo and Ng Jack Ming

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 motor-cycles, $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

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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.

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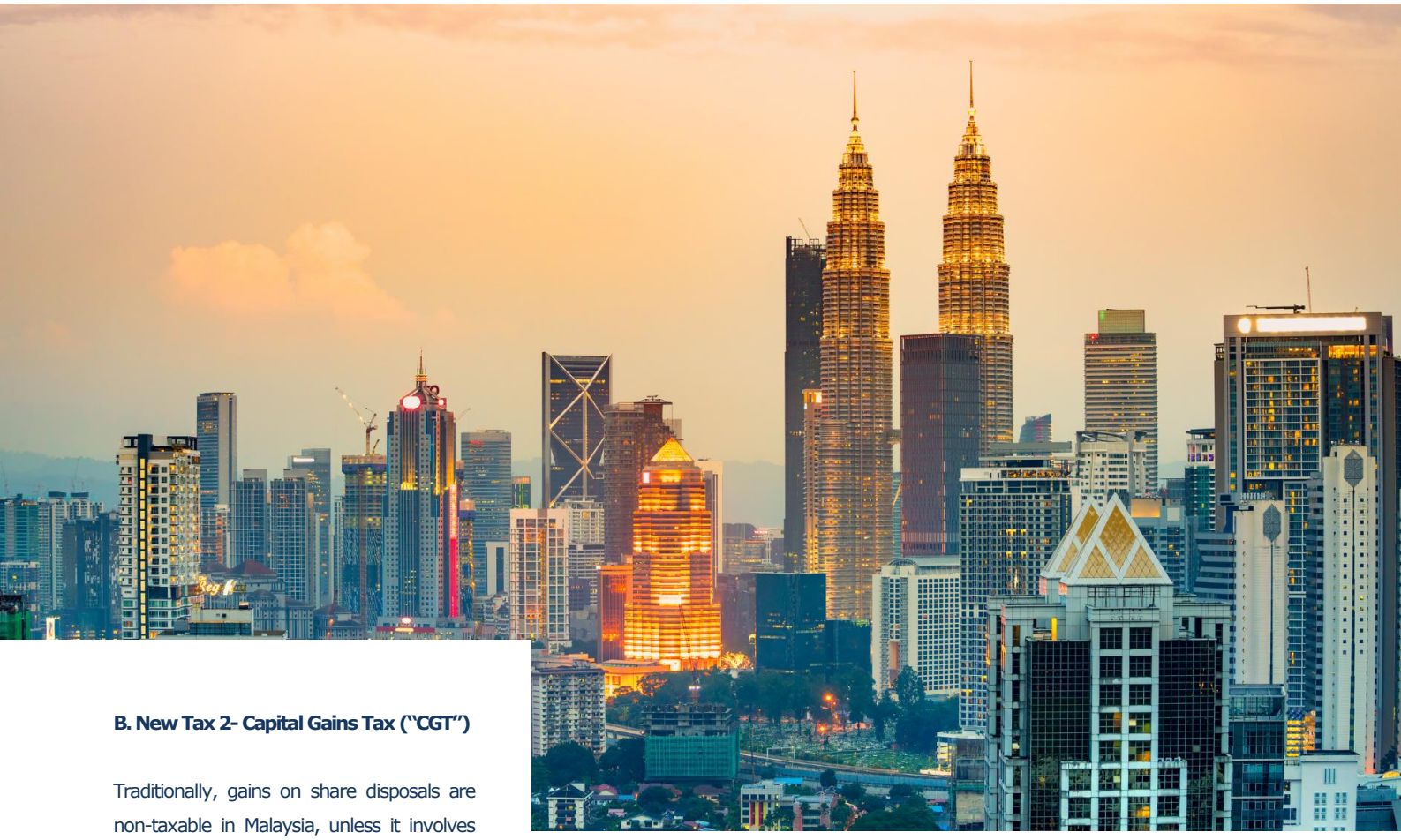
4 Select Luxury Items Tax Act (SC 2022, c 10, s 135)' (Justice Laws Website, 2022) <*https://laws-lois.justice.gc.ca/eng/acts/S-8.35/FullText.htm*l> accessed 28 February 2023.



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

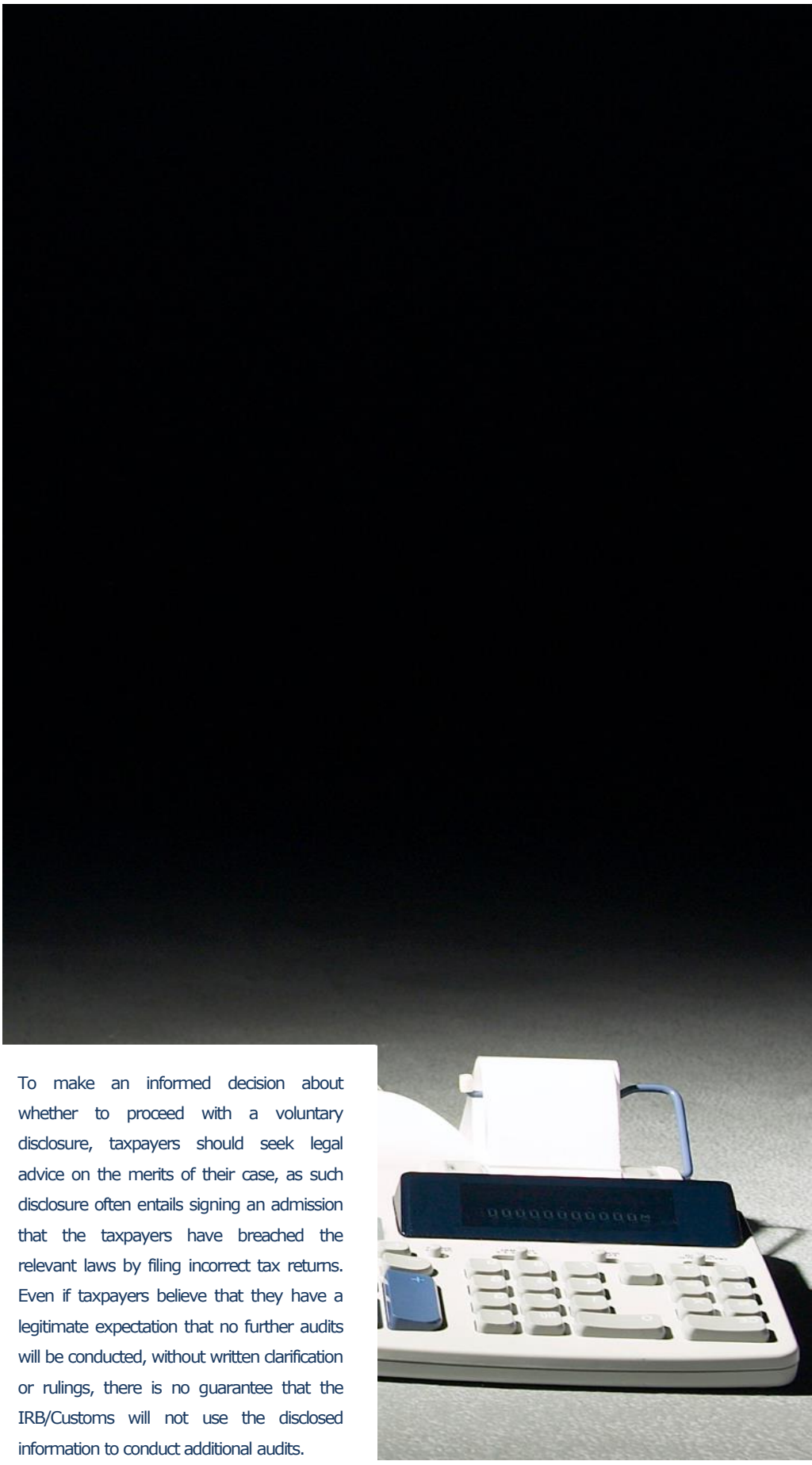
The Special Voluntary Disclosure Program (**SVDP**) was previously introduced in 2019 (by the Inland Revenue Board) and in 2022 (by Customs) to offer remission of penalties at various rates. Budget 2023 proposes the reintroduction of SVDP with an extension that allows taxpayers a full 100% waiver on 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 T20[5]

Chargeable Income (RM)	Current		Proposed			
	Tax Rate (%)	Tax Payable (RM)	Tax Rate (%)	Tax Payable (RM)	(Tax Savings)/ Additional (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.

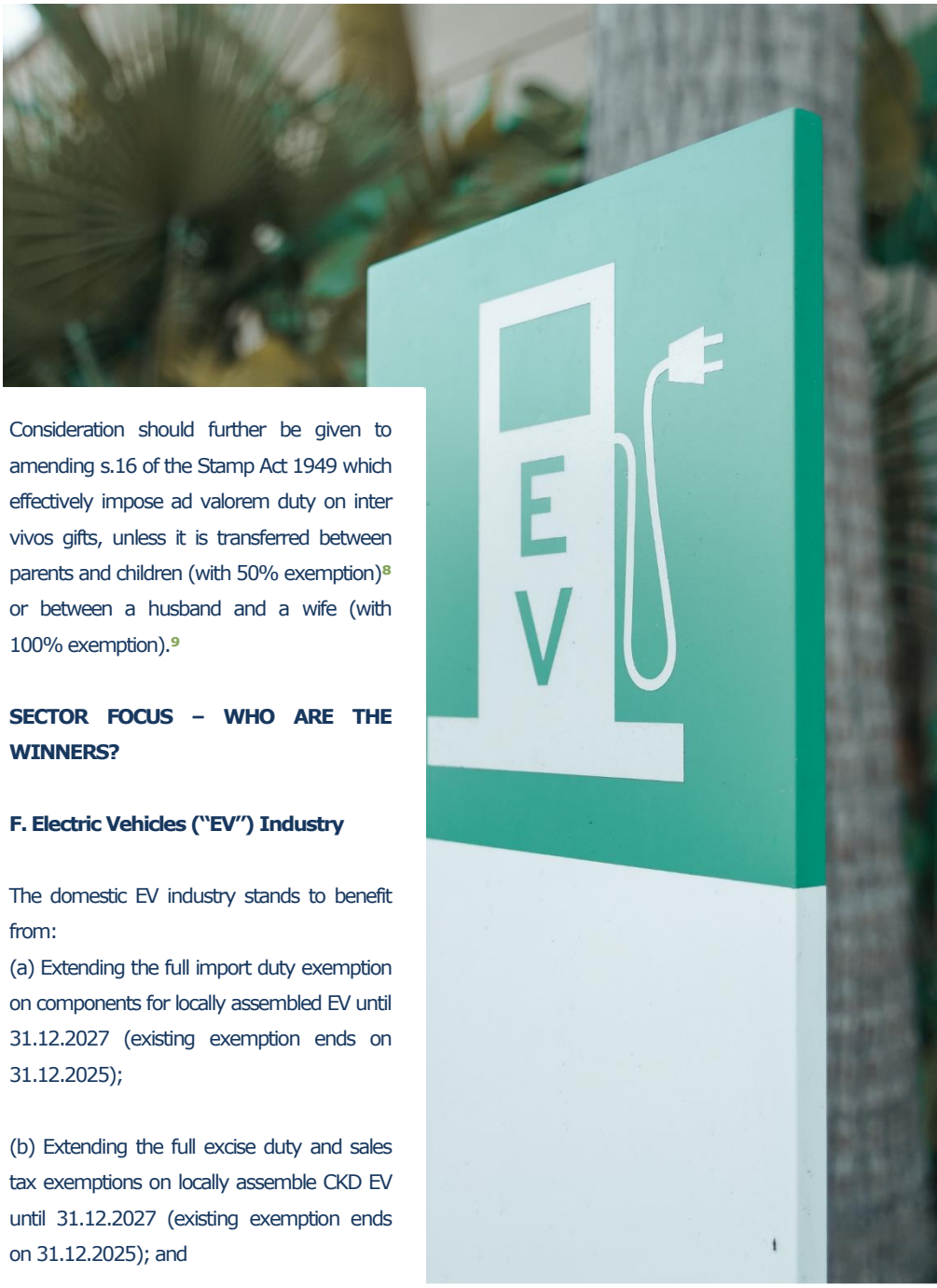
Additionally, Malaysia may also find it challenging to compete with other countries to attract highly-skilled (and paid) expatriates.

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.*

(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.

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]

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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 dependence[12] 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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