M40, B40 to feel the pinch from low value goods tax

BY **INTAN FARHANA ZAINUL**

In April, Malaysia could impose a new 10% sales tax on goods priced RM500 and below that are sold online and shipped via land, sea or air. The move has earned high praise from local producers as they believe it will help level the playing field. A sales tax of 5% to 10% is currently imposed on Malaysian manufacturers.

For perspective, under the new tax regime, a consumer who buys an item priced RM490 will be required to pay an additional RM49, bringing the total to RM539 (excluding delivery charges). Low value goods (LVG) purchased before April 1, as well as items such as cigarettes, tobacco and liquor, will not be subject to the new tax.

The 10% LVG tax was announced during the initial tabling of Budget 2023 in October last year. Its implementation, originally slated for Jan 1, has been tentatively postponed to April.

It is worth noting that the LVG tax is not unique to Malaysia. Other countries have already imposed such a regime under their Goods and Services Tax (GST), including Australia, New Zealand and Singapore.

Singapore currently imposes 7% GST on items priced S$400 (RM1,300) and below that is brought into the country via air or post. The country plans to increase the tax rate to 9% by 2025.

In Thailand, its government is mulling the removal of the exemption on import duty and Value Added Tax (VAT) for goods priced THB1,500 (RM194) and below.

Experts say the implementation of the LVG tax in Malaysia comes at the right time in view of the growing number of online shoppers. Currently, items priced RM500 and below that are sold online are not subject to tax under the de minimis facility. This has been seen as unfair treatment of locally produced goods.

However, there are concerns about the proposed LVG tax's impact on consumers in the low- and middle-income groups amid the rising cost of living.

"LVG are currently excluded from sales tax when they are brought into Malaysia. The rationale behind the imposition of the LVG sales tax by the government is to promote equitable and fairer treatment between LVG purchased from overseas and locally, as local manufacturers are currently charged a sales tax of 5% to 10% on taxable goods," Baker Tilly Malaysia indirect tax leader Sandra Saw tells *The Edge*.

Having said that, she foresees that the low- and middle-income groups are likely to feel the impact of the new tax regime. "The issue at hand is whether the proposed treatment will in fact achieve its aims as it is still unclear in Malaysia how price sensitive or demand impactful such a move will be on consumers, and whether import substitution will take place — it is too early to tell.

"With e-commerce trends and patterns, it remains to be seen which consumer segment will be most impacted by the imposition of the new sales tax. If it impacts the M40 or B40 considerably, then it may not be the most popular move right now."

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Federal government revenue (2021 to 2023)

COMPONENT	RM BIL			CHANGE (%)			SHARE (%)		
	2021	2022[1]	2023[2]	2021	2022[1]	2023[2]	2021	2022[1]	2023[2]
Tax revenue	**173.704**	**198.227**	**205.583**	**12.5**	**14.1**	**3.7**	**74.3**	**69.5**	**75.4**
Direct tax	**130.116**	**147.206**	**152.392**	**15.6**	**13.1**	**3.5**	**55.7**	**51.6**	**55.9**
Income tax									
Companies	79.829	84.760	88.870	59.5	6.2	4.8	34.2	29.7	32.6
Individuals	27.051	30.640	33.630	-30.6	13.3	9.8	11.6	10.7	12.3
Petroleum	11.570	19.302	16.189	-9.4	66.8	-16.1	4.9	6.8	5.9
Indirect tax	**43.588**	**51.021**	**53.191**	**4.1**	**17.1**	**4.3**	**18.6**	**17.9**	**19.5**
of which:									
Sales & service tax	25.616	29.710	32.060	-4.3	16.0	7.9	11.0	10.4	11.8
Excise duties	10.241	10.720	11.970	3.9	4.7	11.7	4.4	3.7	4.3
Import duty	2.645	3.020	3.220	12.7	14.2	6.6	1.1	1.1	1.2
Export duty	2.057	2.200	1.450	175.7	7.0	-34.1	0.9	0.8	0.5
Non-tax revenue	**60.048**	**86.990**	**66.987**	**-15.0**	**44.9**	**-23.0**	**25.7**	**30.5**	**24.6**
of which:									
Licences and permits	10.578	13.330	13.788	-3.2	26.0	3.4	4.5	4.7	5.1
Investment income	35.018	63.442	42.710	-24.0	81.2	-32.7	15.0	22.2	15.7
Total revenue	**233.752**	**285.217**	**272.570**	**3.9**	**22.0**	**-4.4**	**100.0**	**100.0**	**100.0**
Share of GDP (%)	**15.1**	**16.7**	**15.0**						

[1] Revised estimate [2] Budget estimate excluding Budget 2023 measures

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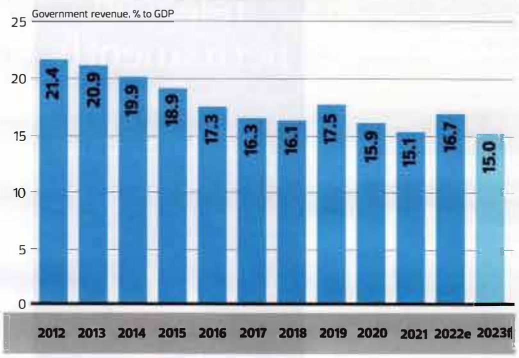
Government revenue has been on a downward trend since 2012



Broadening the government's revenue base

Collection from the proposed LVG tax is estimated to bring in an additional RM200 million to RM300 million for the government's coffers, which is a mere 1% increase from the government's annual Sales and Service Tax (SST) revenue. In 2021, the government collected RM25.6 billion in SST and is expected to generate RM29.71 billion in 2022 and RM32.06 billion in 2023.

UOB Malaysia senior economist Julia Goh says the main goal of the proposed LVG tax is to create a level playing field between local and foreign sellers, and the government is expected to collect RM200 million from the LVG tax in the first year. Nevertheless, the government would need to continue looking at other ways to enhance its annual revenue.

"I think the government will look at medium-term revenue enhancements, including GST or widening the current SST. The purpose of this is to widen the revenue base, reduce dependence on oil revenue and increase share of revenue to gross domestic product (GDP). However, timing-wise, we think it is unlikely to be implemented this year," she adds.

Since 2012, the government's revenue has been on a steady downward trend amid increasing debt levels. This shows the government has been raising debt to fund its growing expenditures.

The decline in revenue will make it a challenge for the government to achieve fiscal consolidation amid elevated debt levels after the Covid-induced spending drive to shore up the economy. In addition, the government has seen its annual budget strained due to subsidies, which is expected to reach RM80 billion in 2022, with fuels and cooking oil alone accounting for half of the value.

According to a report by the Organisation for Economic Co-operation and Development (OECD), Malaysia's tax-to-GDP ratio stood at 11.4% in 2020, below the Asia-Pacific average of 19.1%.

"The tax-to-GDP ratio in Malaysia decreased by 1.0 percentage point from 12.4% in 2019 to 11.4% in 2020. From 2007 to 2020, the tax-to-GDP ratio in Malaysia decreased by 3.4 percentage points, from 14.8% to 11.4%. The highest tax-to-GDP ratio during this period was 16.1% in 2012, and the lowest was 11.4% in 2020," it said.

Meanwhile, Malaysia faces rising debt servicing charges. These charges, which made up 8% of federal government revenue in 2008, surged past the 18% mark in 2021.

In short, revenue needs to grow a lot faster than expenses for the country to tackle future challenges, including an ageing population and any economic shocks.

Last week, Prime Minister Datuk Seri Anwar Ibrahim, who is also finance minister, said he is currently not considering reinstating GST and will instead focus on increasing the income of Malaysians and gradually lowering the nation's debt. He acknowledged that GST remains the most transparent and efficient taxation system.

Anwar is slated to retable Budget 2023 on Feb 24. All eyes will be on the federal budget to see if the government will pursue or delay the implementation of the LVG tax.

Digital economy

Although the LVG tax may not be able to address the shortfall in government revenue, it could help local manufacturers to remain competitive, say experts. It could also be the beginning for the government to tap the growing digital economy.

Malaysia is not the only country facing decreasing tax revenue amid a booming digital economy. While technology is great, it has allowed businesses to operate and generate profit with limited or no physical presence, and in turn avoid certain taxes incurred by companies in the traditional economy.

In an interview with *The Edge* last September, Malaysia Digital Economy Corporation (MDEC) CEO Mahadhir Aziz predicted an explosive growth in e-commerce and rising rates of digital adoption. He pointed out that the digital economy already contributed 22.6% to the country's GDP and the number is set to rise to 25.5% by 2025.

It is estimated that more than 31 million parcels were sent to Malaysia in 2021, according to data provided by the Malaysian Communications and Multimedia Commission (MCMC).

Sunway University economics professor Dr Yeah Kim Leng sees the implementation of the LVG tax as an interim measure by the government to collect tax from products sold online, as well as to tap the growing popularity of e-commerce platforms and online shopping. "If GST is implemented, the LVG tax can be scrapped to avoid double taxation," he says.

It is worth noting that local producers are subject to a sales tax of 5% to 10% on top of corporate income tax. As such, the proposed LVG tax can be viewed as "equalising" the tax treatment between products purchased online and those bought from local physical stores and retailers, says Yeah.

"The LVG tax will create a level playing field for online traders and local retail stores, but its implementation will likely dent the price competitiveness of online retailers. However, there are other advantages for online shoppers such as convenience, price discounts and special offers that are expected to sustain the strong growth of the online retail industry," he adds.

Still, the key to the LVG tax will be the execution. To prepare merchants who will be affected by the implementation of the new tax, the Royal Malaysian Customs Department (RMCD) has come out with a draft tax guide.

The new sales tax of 10% will only be imposed on goods that are priced RM500 and below that are bought online from April 1 this year. The tax will not be imposed on delivery charges or insurance costs for bringing in the item from overseas.

According to a statement on the RMCD's website, sellers of LVG are responsible for acquiring "Registered Seller" (RS) status from the department. Registration will be required for both Malaysian citizens and foreigners who deal in LVG brought into the country via land, sea or air, and exceed RM500,000 in total sales value over 12 months.

KPMG Malaysia head of tax Soh Lian Seng says some processes under the new LVG tax are not very clear at the moment, especially how the RMCD wants to ensure all players, especially those overseas, register for this new tax regime.

"Also, what if there are returns to the supplier, will there be a refund of the sales tax paid? And if yes, what is the process like? The rate is fixed at 10% regardless of the tariff code. But if it is not LVG and the tariff code rate is 0% or 5%, there may be inequality in treatment," he points out.

Soh says the new LVG tax will help the local producers of such goods to be more competitive, and that the government is giving merchants enough time to understand the tax structure. E