THE STATE OF THE NATION A WEEKLY UPDATE

# Tax experts: Budget 2025 to see expanded tax scope, new taxes unlikely

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KPMG

**Soh: Malaysia's tax revenue is relatively low compared with that of Asean counterparts**

PWC

**Chia: The sugar tax will not be aimed at increasing government revenue but to address unhealthy lifestyles**

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DELOITTE MALAYSIA

**Sim: Should the GST be introduced, there will be room for the government to cut personal and corporate income tax rates**

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**Farah: Through whichever manner the government undertakes to shore up its revenue, such as the implementation of e-invoicing, the shadow economy is more likely to be targeted instead of burdening the rakyat**

As Putrajaya seeks to shore up the national coffers and reduce its fiscal deficit while balancing the needs of businesses and the public in an environment of high inflation, most tax experts are expecting the Ministry of Finance (MoF) to expand the scope of several taxes that were introduced earlier, as well as provide clarity on newer initiatives like e-invoicing in the upcoming Budget 2025. They don't expect new taxes to be implemented in the national budget that will be tabled on Oct 18.

Note that in the MoF's pre-Budget 2025 statement in July, the government had made clear its intentions to broaden the tax base, "continuously ensure a progressive tax system, reduce tax leakages and enhance tax compliance, with the budget also initiating measures to better manage public expenditure in order to effectively and efficiently support Ekonomi Madani aspirations".

"Currently, Malaysia's tax revenue stands at 12.6% of the national gross domestic product (GDP) for 2023, which is relatively low compared with that of Asean counterparts.

"To address this, the government aims to reduce the deficit target to 4.3% of GDP in 2024, down from 5% last year. This reduction is essential for meeting fiscal goals and financing future needs," Soh Lian Seng, head of tax at KPMG in Malaysia, tells *The Edge*.

He points out that to achieve these goals, the OECD Economic Surveys: Malaysia 2024 report published on Aug 27 emphasised the need to mobilise additional tax revenues, which is crucial for reaching the short-term 3% deficit target and funding future spending.

Like his peers in the tax fraternity, Soh expects the government to commit to broadening the tax base through a progressive tax system that reduces leakages and enhances compliance, building on the initiatives introduced in Budget 2024.

In fact, the reintroduction of the broad-based Goods and Services Tax (GST) would be welcome and inevitable, say about half a dozen tax experts whom *The Edge* spoke to last week.

Until then, the current administration will continue to look at incremental expansion within the existing system such as expanding the scope of the Sales and Service Tax (SST) to cover more taxable services.

One such example is the increase in sugar-sweetened beverage tax, with excise duty rising to 50 sen per litre in January and a new duty on pre-mixed products introduced in March.

As the sugar tax is meant to support the "war on sugar" campaign led by the Ministry of Health, the understanding is that further taxes on sugary drinks may be imposed.

"This, however, will not be aimed at increasing government revenue," explains PwC Malaysia tax leader Steve Chia, who surmises that the funds raised from the sugar levies could be allocated to public and early education initiatives, addressing unhealthy lifestyles from a young age and potentially reducing public healthcare costs in the long term.

Separately, further rate increases as seen in service tax increase from 6% to 8% (excluding businesses in the food and beverage and telecoms sectors) in Budget 2024 are also broadly expected in Budget 2025. It is noteworthy that when this levy was increased this year, tax experts noted that the main challenges stemmed from the expansion of the scope of taxable services rather than the rate increase.

"The recent increase in the service tax from 6% to 8% across most industries has presented significant challenges. Many service providers, particularly in the logistics sector, are experiencing pushback from consumers. This is especially true for companies that outsource or provide in-house transport to deliver goods at no extra charge but are now required to apply the service tax. Inevitably, this will lead to higher prices, as the tax is passed on indirectly to consumers, who often don't see the breakdown of costs, only that prices are rising every year," says Grant Thornton Malaysia national tax practice leader Datin Seah Siew Yun.

Such issues have prompted the Royal Malaysian Customs Department (RMCD) to issue an update on the service tax policy in August, specifically addressing logistics services, recalls KPMG's Soh.

"Based on our observations, this update has demonstrated that the MoF and the RMCD are actively engaging with industry players to enhance the service tax regime. Note that the relaxation of conditions for door-to-door delivery services is a significant improvement. This exemption is not only beneficial for businesses but also advantageous for the rakyat. Affected businesses are encouraged to review their transactions to determine how these updates may impact their operations," he says.

Deloitte Malaysia country tax leader Sim Kwang Gek says due to the cascading effect of the current SST system, the government's consideration of a more holistic review of Malaysia's indirect tax system — or specifically, a more broad-based system that allows for credits on tax paid to mitigate the cascading effect of the present SST system — will be helpful.

"All said, the service tax system has its flaws, and the additional tax collected may not move the needle in terms of revenue generation. As a more efficient and transparent system, the GST remains a more viable and sustainable option for the country to move towards broad-based consumption taxes," Sim advises.

"Should the GST be introduced, there will be room for the government to cut personal and corporate income tax rates, which is a welcome move as it will put us on a par with neighbouring countries in the region," she says.

It is noteworthy that the specifics of a carbon tax continue to be under consideration, reflecting the government's focus on environmental, social and governance (ESG) factors even if the investment, trade and industry minister has said that the tax will not be introduced in Budget 2025.

"A clear roadmap, including measurement methodologies [which require upskilling around calculation and analysis of carbon tax, for instance] and indicative tax rates, would help prepare stakeholders and mitigate economic shocks. Clear government signalling can stimulate investment, particularly in the green economy," PwC's Chia says.

EY Malaysia Tax managing partner Farah Rosley also doesn't think that the government will introduce new taxes in Budget 2025 so as not to burden the people. She is of the view that the authorities may impose levies targeting the shadow economy instead.

"In the past, the shadow economy was [worth about] a fifth of our GDP. Through whichever manner the government undertakes to shore up its revenue, such as the implementation of e-invoicing, the shadow economy is more likely to be targeted instead of burdening the rakyat," she says.

As Malaysia moves toward e-invoicing, the initiative is seen to significantly boost tax reforms, accelerate digital transformation and improve compliance. To this end, Budget 2025 is expected to continue prioritising investments in digital infrastructure and promote technology use, especially among small and medium enterprises (SMEs).

The government might also focus on increasing digital inclusion, encouraging e-commerce and enhancing cybersecurity.

## National growth and MSMEs

KPMG's Soh points out that despite the "vital role that micro SMEs (MSMEs) play in shaping Malaysia's economy — making up 97.4% of businesses and providing 48% of jobs — the pool contributes only 38% to GDP".

He believes that Budget 2025 may see a revisiting of incentives such as the extension of capital allowances for automation or an increase in deductions for environmental, social and governance-related expenses, which could further boost their economic contribution.

"Notable proposals may include double tax deductions for green expenses, financing schemes and digital support for SMEs," Soh predicts.

## Hopes of widened income tax bracket for individuals, lower rate for corporate income tax

Given the rising cost of living, most tax experts believe the government will consider revising the income tax bracket for individuals as it could help to alleviate the public's financial pressures in the economic environment of high inflation.

Note that the Consumer Price Index (CPI) — which measures inflation — rose 1.9% year on year in August, according to the Department of Statistics Malaysia (DOSM). That compares with the 2% y-o-y increase predicted in a Bloomberg survey of economists and July's 2% y-o-y rise.

The food and beverage group, which contributes nearly 30% to the total CPI weight, increased by 1.6% in August 2024, the same rate as recorded in July, while inflation for transport increased by 1.3% in August 2024, marginally higher than 1.2% in July following diesel subsidy re-targetting.

PwC's Chia notes: "The government would consider the cost of living of the rakyat. The M40 often desire an effective reduction of their tax burden as they represent a significant portion of taxpayers. Both approaches have their merits: widening the tax bracket shields taxpayers from a higher tax burden due to salary increases, especially inflationary increments. On the other hand, tweaking the rate will directly reduce tax to be collected by the government.

"Whichever option is chosen, a review will hinge on the government's assessment of the overall impact of Budget measures on the cost of living. A review would be welcome to alleviate living costs for individual taxpayers, potentially boosting spending in the economy which, in turn, will increase revenue from corporate income taxes. Any rate review should ensure that the maximum

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# New taxes must be 'carefully balanced', says Grant Thornton's Seah

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benefit should flow to the B40 and M40 groups while maintaining the tax level for the T20 group."

As for corporate income tax rates, Deloitte's Sim reiterates that a review will be necessary to increase Malaysia's competitive rates, given that they are currently higher than those of other countries in the region.

In Southeast Asia, Malaysia's current corporate income tax rate of 24% is higher than that of Vietnam and Thailand, both of which have a corporate income tax rate of 20%, Sim points out. Malaysia's corporate income tax is also higher than Indonesia's 22% and Singapore's 17%.

"Recently, our observations have revealed that more countries are leaning towards consumption taxes as a more sustainable source of revenue by increasing the GST or value-added tax rate and reducing direct taxes," observes Sim.

Another pertinent issue is the subsidy rationalisation of petrol (RON95), which was initially set to be implemented in the second half.

"It would be surprising if the rationalisation of RON95 takes place soon because the prime minister recently assured that it will not take place for the time being. Unlike the diesel subsidy, RON95 has more systemic implications," says PwC's Chia.

"Therefore, the government would want to iron out certain priorities first and that includes whether the price will be floated to market price immediately or gradually, as well as share the mechanisms to efficiently distribute targeted subsidies. Some lessons can be learnt from the diesel subsidy rationalisation," he says.

Still, Grant Thornton's Seah warns that any new taxes, should they be implemented, must be "carefully balanced".

"Revenue-raising efforts don't solely rely on taxation, as there are alternative methods to achieve fiscal goals. Furthermore, the expansion of the tax base should not disproportionately burden SMEs, which are the backbone of the Malaysian economy. Policies that negatively affect SMEs will have widespread economic repercussions.

"As Malaysia navigates its fiscal challenges, it must acknowledge that there are limits to new tax ideas. Many other countries have already implemented similar measures, making it unlikely that Malaysia can introduce a completely novel tax that will revolutionise its system. Examples like the digital service tax, environmental taxes, excise duties on unhealthy food, and luxury tax expansions are already in place or under consideration," she adds. E