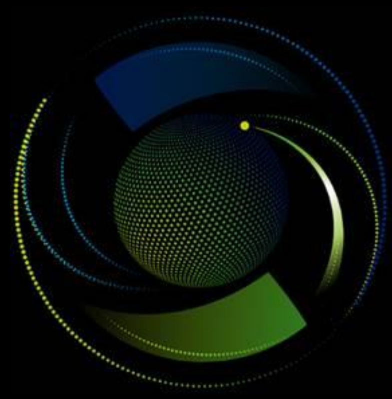
Malaysia | Tax | 1 April 2024



Tax Espresso - Special Alert

Capital Gains Tax in Malaysia (Part 3) – Guidelines for CGT on gains from disposal of foreign capital assets received from outside Malaysia

Introduction

Following the imposition of Capital Gains Tax (CGT) in Malaysia effective from 1 January 2024 via the Finance (No. 2) Act 2023 [*Act 851*] and the Income Tax (Exemption) (No. 3) Order 2024 [*P.U.(A) 75/2024*] (Exemption Order) gazetted on 4 March 2024, the Inland Revenue Board (IRB) has issued the Guidelines: Capital Gains Tax on Gains from the Disposal of Foreign Capital Assets received from Outside Malaysia dated 27 March 2024 (CGT Guidelines for Foreign Capital Assets).

In the previous articles, we provided an overview of CGT in Malaysia with a commentary based on what was known so far about CGT [CGT in Malaysia (Part 1)], followed by an additional commentary based on further details from the CGT Guidelines for unlisted shares and the Exemption Order [CGT in Malaysia (Part 2)]. This article summarises the additional details provided by the IRB in the CGT Guidelines for Foreign Capital Assets.

CGT Guidelines for Foreign Capital Assets

The CGT Guidelines for Foreign Capital Assets explain the CGT treatment on gains or profits from the disposal of capital assets situated outside Malaysia (foreign capital assets, including all types of assets, not limited to shares) received in Malaysia by residents. Such gains or profits from the disposal of foreign capital assets may be eligible for an exemption from CGT if the chargeable person disposing the assets (disposer) complies with the economic substance requirements (ESR), pursuant to the Exemption Order. The Exemption Order does not apply to a resident carrying on the business of banking, insurance, sea transport, or air transport.

Key Points

1. Chargeable person and chargeable gains

Effective from 1 January 2024, gains from the disposal of all types of foreign capital assets (where the disposal occurs on or after 1 January 2024) received in Malaysia (i.e., transferred or brought into Malaysia in the form of cash or through electronic funds transfer; or both) by the following residents are subject to CGT under Section 4(aa) of the Income Tax Act 1967 (ITA) at the prevailing tax rate:

- Company;
- Limited liability partnership (LLP);
- Trust body; and
- Co-operative society.

"Cash" means notes, coins, and cheques.

"Electronic fund transfer" means bank transfer (e.g., credit transfer, debit transfer), payment card (debit card, credit card, and charge card), electronic money (e-money), privately-issued digital assets (e.g. crypto assets, stablecoins) and central bank digital currency (CBDC).

Examples of foreign capital assets situated outside Malaysia are as follows:

(a) Immovable property that are physically situated outside Malaysia such as buildings and land;
(b) Movable property that are physically situated outside Malaysia such as machinery, vehicle, fixtures, fitting, painting, and plant;
(c) Intellectual property rights situated outside Malaysia owned by the owner or licensee of the right who is a resident in Malaysia such as copyright, patent, research and development, computer software and trademark;
(d) Shares issued by a company incorporated outside Malaysia that are not subject to any provisions under the ITA.

In determining the gains from the disposal of foreign capital assets that are chargeable to tax, expenses wholly and exclusively incurred for the acquisition and disposal of capital assets (e.g., legal fees, appraiser fees, advertising, and expenses to increase or maintain capital value) can be allowed under Section 65E(2) of the ITA.

Deloitte's comments: *Based on the existing Section 4(aa) of the ITA, the scope of charge is widely cast as gains or profits from the disposal of any capital assets by any person. On 26 March 2024, the House of Representatives passed the Income Tax (Amendment) Bill 2024. Among the proposed amendments, there is a redefinition of the term "capital asset" for the purpose of CGT [Deloitte Malaysia Tax Espresso – Special Alert: Amendment Bills].* *The term "capital asset" will be redefined as follows:* *"capital asset" means—* *(a) movable or immovable property situated outside Malaysia including any rights or interests thereof; or* *(b) movable property situated in Malaysia which is a share of a company incorporated in Malaysia not listed on the stock exchange (including any rights or interests thereof) owned by a company, limited liability partnership, trust body or co-operative society.* *Unlike Paragraph (b) of the new definition of "capital asset" where the scope of chargeable person was clearly specified, Paragraph (a) of the new definition of "capital asset" is silent on the scope of chargeable person. Pending gazette of the Income Tax (Amendment) Bill 2024, the IRB explained in the CGT Guidelines for Foreign Capital Assets that only the gains from disposal of foreign capital assets by a resident company, limited liability partnership, trust body or co-operative society which are received in Malaysia are subject to CGT. Any gains from disposal of such foreign capital assets received in Malaysia by other resident person (e.g., an individual) does not fall within the scope of charge to CGT under the ITA.*

2. Foreign tax credit

A resident who has been subjected to foreign tax in respect of the gains from the disposal of foreign capital assets received in Malaysia can claim a bilateral or unilateral tax credit under Sections 132 and 133 of the ITA.

Deloitte's comment: *Based on the provisions of Paragraph 9, Schedule 7 of the ITA, any claim for bilateral credit for a year of assessment must be made in writing to the Director General of Inland Revenue not more than two years after the end of the year of assessment. The same timeline shall apply accordingly to a claim for unilateral tax credit.*

3. Tax exemption

Pursuant to the Exemption Order, gains from the disposal of foreign capital assets received in Malaysia by a company, LLP, trust body, and co-operative society resident in Malaysia, which complies with the ESR as prescribed, are exempted from CGT from **1 January 2024 to 31 December 2026**.

The ESR are as follows:

Category of Resident Taxpayer	Economic Substance Requirements (ESR)
• Company; • LLP; • Trust body; and • Co-operative society.	(a) employ adequate number of employees with necessary qualifications to carry out the specified economic activities in Malaysia; and (b) incur adequate amount of operating expenditure for carrying out the specified economic activities in Malaysia.

In light of the different operating methods between industries, the determination of any minimum threshold value for the appropriate ESR is based on the facts of each case. Factors that will be considered include:

(a) the number of employees considering the type of activity involved (e.g., whether it is a capital or labour-intensive industry);
(b) whether the employee works full-time or part-time; and
(c) whether the office premises have been used to carry out related activities and whether the premises are sufficient for those activities.

“Specified economic activities” means:

- Investment holding entity

  (a) Holding and managing its equity participation in other entities; or
  (b) Making necessary strategic decisions in respect of any assets the entity acquires, holds or disposes of, as well as managing and bearing principal risks in respect of such assets.

- Other than Investment holding entity

  In the case of a company, LLP, trust body, and co-operative society carrying out a trade, profession or business in Malaysia, specified economic activities referred to the business operations carried out.

A service director who is employed based on a contract of service and not on a contract for service can be considered as an employee. A non-service director is not considered as an employee.

Outsourcing of specified economic activities by a company, LLP, trust body, and co-operative society to an outsourcing entity is permitted if the following conditions are met:

- Specified economic activities are carried out by the outsourcing entity in Malaysia;
- A company, LLP, trust body, and co-operative society has implemented sufficient monitoring and control over the implementation of specified economic activities by the outsourcing entity;
- The outsourcing entities are generally expected to charge the company, LLP, trust body, and co-operative society for specified economic activities carried out, subject to the application of transfer pricing rules;
- The number of qualified employees employed, and the total operating expenses incurred by the outsourcing entity in Malaysia is equivalent to the level of specified economic activities carried out by the outsourcing entity;
- There is no double counting if the outsourcing entity provides services to more than one company, LLP, trust body, and co-operative society.

4. Tax reporting

Taxpayers must report the gains from the disposal of foreign capital assets received in Malaysia in the basis period for a year of assessment in the Income Tax Return Form (ITRF).

Although the taxpayer is eligible to claim tax exemption, the taxpayer must report the gains from the disposal of the foreign capital asset in the ITRF as follows:

(a) Type and amount of foreign income;
(b) Country where the income arises;
(c) Amount of tax imposed by foreign country; and
(d) Any information to be determined besides Item 4(a) to 4(c).

Deloitte's comments:

Based on the existing Section 77A(1B) of the ITA, every company, limited liability partnership, trust body, or co-operative society who disposes of capital asset shall, within sixty days (or such other period the Director General may allow on a written request being made to him) of the date of disposal of that asset, furnish a CGT return to the Director General. From the existing Section 77A(1B) of the ITA, it appears unclear whether the provision applies to a disposal of foreign capital asset.

From our reading of Paragraph 9.1 of the CGT Guidelines for Foreign Capital Assets, it seems clear that the provision under Section 77A(1B) of the ITA shall not apply to a disposal of foreign capital asset. The disposer is only required to report its gains from the disposal of foreign capital assets received in Malaysia in the basis period for a year of assessment in the ITRF, instead of a CGT return for each disposal of a capital asset.

Please refer to the CGT Guidelines on Foreign Capital Assets dated 27 March 2024 and the Exemption Order [*P.U.(A) 75/2024*] for full details.

Get in touch

For any queries or assistance, please reach out to your usual Deloitte contact.

Dbriefs

Dbriefs

A series of live, on-demand and interactive webcasts focusing on topical tax issues for business executives.

Tax@hand

Latest global and regional tax news, information, and resources.

Recognised as Malaysia Tax Firm of the Year 2023 & Malaysia Transfer Pricing Firm of the Year 2023 by the International Tax Review

Get in touch