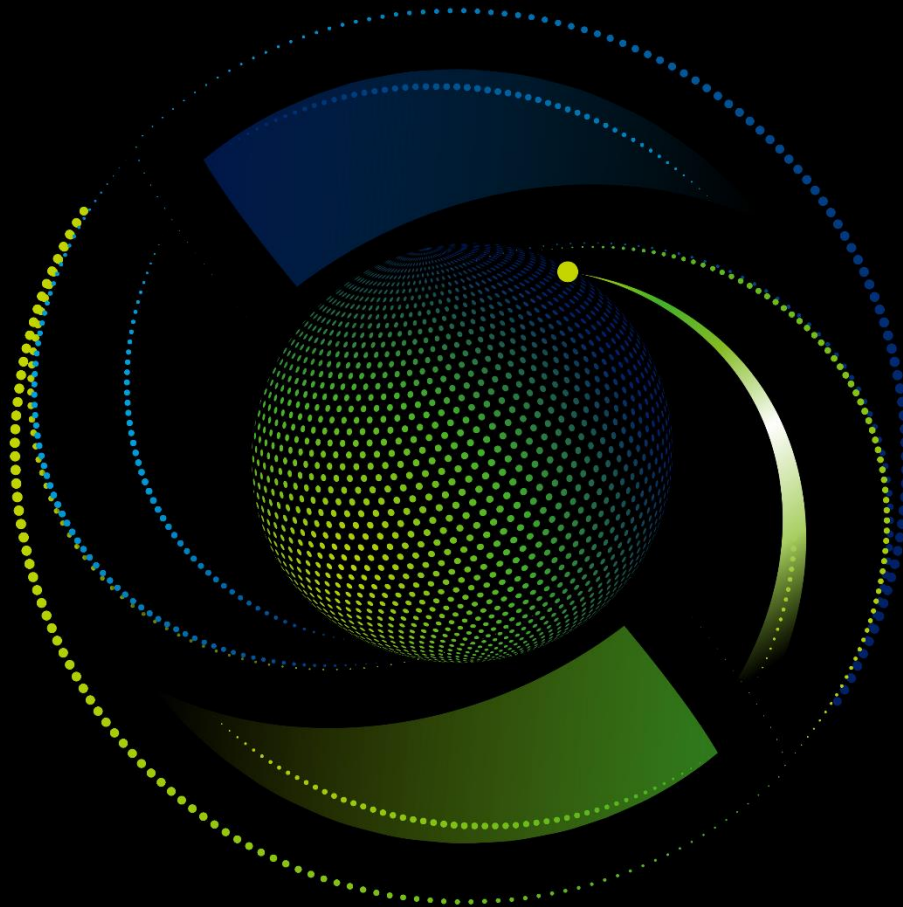


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Indirect Tax Chat

Keeping you updated on the latest news in the Indirect Tax world

April 2022



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Greetings from Deloitte Malaysia's Indirect Tax team

Greetings readers, and welcome to the April 2022 edition of our Indirect Tax Chat. We hope that you are keeping safe and well.

This month, we cover the first sales tax policy issued by the Royal Malaysian Customs Department (“RMCD”). We also explore practical sales tax exemption issues regarding imported goods, and the postponement of the excise duty on pre-mixed preparation products, as well as a high court case on sales tax exemptions for a franchise holder of locally assembled motorcycles.



We are now approaching the final two months of Phase One of the Special Voluntary Disclosure and Amnesty Program (“VA”). While there is a Phase Two, the benefits afforded may be reasonable, but are not as good as what is offered under Phase One. If you are considering to participate, it is important to act quickly. Although the RMCD have said that they would process applications within two weeks, in practice it takes three to four weeks. This period is critical as the benefits under Phase One would only accrue to those taxpayers who settle all claims prior to 30 June 2022, and payment can only occur after the RMCD has approved an application. As a result, anyone who wants to avail themselves of the benefits under Phase One, will need to be in a position to submit an application by the end of May or early June to complete the process in time.

Separately, here are some recent news that may interest you:

- Economist Manokaran Mottain shared his view that the GST is better than the sales tax and service tax (“SST”). For businesses, the GST is an easier process of submission of tax claims, and for consumers, the implementation of the GST has reduced the service tax from 10% to 6%. He explained that the GST was a more transparent and effective regime compared to the SST, sharing that the Finance Minister Tengku Datuk Seri Zafrul Abdul Aziz had noted that many leakages occurred after the SST system was introduced in 2018. For more information, please click [here](#).
- The Malaysian Automotive Association will appeal to the government for a further extension of the automotive sales tax exemption to end-2022 for car manufacturers to fulfil their backlog of orders. Originally scheduled to end on 31 December 2020, the sales tax exemption has been extended thrice — first to 30 June 2021, and then to 31 December 2021, with the latest extension to 30 June 2022. For more information, please click [here](#).

To our readers celebrating, we wish you a *Selamat Hari Raya Aidilfitri!*

Best regards,
Tan Eng Yew
Indirect Tax Leader

1. Sales Tax Exemption on Pallets

Sales Tax Policy 1/2022 (“STP1/2022”) was published by the RMCD on 5 April 2022. The STP1/2022 provides that registered manufacturers or any persons acting on behalf of registered manufacturers are eligible for a sales tax exemption on the importation or purchase of pallets used as packaging materials in manufacturing under Item 1 or Item 3, Schedule C (“C1” or “C3”) of Sales Tax (Persons Exempt from Payment of Tax) Order 2018 (“the Order”).

The sales exempted must meet the following qualifying criteria under paragraph 2 to 4 of STP1/2022:

- Pallets imported or purchased with sales tax exemption under Item C1 or C3 of the Order shall be used as packaging material for finished goods exported or sold and not returned to the registered manufacturer;
- Pallets that are used for the purpose of transporting goods, reusable or returned to the registered manufacturer are not categorised as packing materials, and not eligible for the sales tax exemption under Item C1 or C3 of the Order. In this case, sales tax shall be paid when the pallet is imported or purchased; and
- Pallets used for the purpose of transporting exported goods and then re-imported, are eligible for sales tax exemption under Item 39, Schedule A of the Order when the pallets are re-imported.

Deloitte’s comments

The sales tax policy is to provide clarity on the application to obtain sales tax exemption on pallets for use as packaging materials, subject to conditions. The sales tax exemption will lower the cost for registered manufacturers for the importation or purchase of pallets which are used as packaging materials for its manufacturing activities.

Any registered manufacturers or any persons acting on behalf of registered manufacturers are advised to ensure the above conditions are met before applying for the sales tax exemption on pallets and/or to revisit the existing sales tax exemption application.

The STP1/2022 is currently only available in Bahasa Malaysia and can be accessed [here](#).

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2. Postponement of excise duty on pre-mixed preparations products

Excise duty of RM0.40/litre is currently imposed on 3 categories of ready-to-drink sugar-sweetened beverages:

- a) Fruit and vegetable juices classified under the tariff heading 20.09 which contains sugar exceeding 12 gm per 100 ml (e.g. orange juice)
- b) Drinks classified under the tariff heading 22.02 except 22.02.99.10 00 which contains sugar exceeding 5 gm per 100 ml (e.g. soda, energy drinks, etc.)
- c) Drinks classified under the heading 22.02, based on milk as specified under Chapter 4 of the First Schedule of the Customs Duties Order 2017 which contains sugar exceeding 7gm per 100 ml (e.g. 22.02.99.1000 Flavoured UHT milk based drinks).

As announced by the Minister of Finance in the [Budget 2022](#) speech, to address issues of obesity, diabetes, and other non-communicable diseases associated with nutrition, it was proposed that the scope of excise duty for sugar sweetened beverages be expanded to include pre-mixed preparation products of chocolate or cocoa based, malt, coffee and tea such as 2-in-1 or 3-in-1 pre-mixed beverages.

Excise duty would be imposed on pre-mixed preparations products categorised under the following tariff codes at the rate of **RM0.47 per 100g** and will be based on the threshold of sugar content exceeding 33.3g/100g:

Tariff code	Product description as per Harmonized System (HS) Tariff code by World Customs Organization
18.06	Chocolate and other food preparations containing cocoa
19.01	Malt extract; food preparations of flour, groats, meal, starch or malt extract, not containing cocoa or containing less than 40% by weight of cocoa calculated on a totally defatted basis, not elsewhere specified or included; food preparations of goods of headings 04.01 to 04.04, not containing cocoa or containing less than 5% by weight of cocoa calculated on a totally defatted basis, not elsewhere specified or included.
21.01	Extracts, essences and concentrates, of coffee, tea or maté, and preparations with a basis of these products or with a basis of coffee, tea or maté; roasted chicory and other roasted coffee substitutes, and extracts, essences and concentrates thereof.

The proposed effective date of this excise duty expansion was 1 April 2022. However, the RMCD [announced](#) on 31 March 2022 that the implementation of excise duty on pre-mixed preparation beverages has been **postponed** to a later undetermined date.

Deloitte's comments

The postponement allows more time for businesses to understand the proposed expansion to ensure a smooth implementation. We expect that affected businesses and manufacturers will welcome the postponement, as there were concerns about the lack of details for the implementation especially on product classification (HS codes) as well as the additional cost to the businesses. The postponement allows additional time for stakeholders to discuss, enhance, and finalise details of the implementation of this excise duty.

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3. Sales tax exemption: High Court grants leave for judicial review whether sales tax exemption is available for manufacturers of non-taxable goods for local sale

The High Court (“HC”) granted leave to a manufacturer (HM) to commence judicial review to quash Bills of Demand (“BODs”) issued by the Director General of RMCD (“DG”), to recover sales tax that was exempted in HM’s purchase of taxable goods to manufacture non-taxable goods for local sale. We set out our comments on the case based on the available key background facts and decision of the HC (as published on 4 October 2021 in a newsletter of the law firm which handled the case).

Key background facts

- HM is a franchise holder of locally assembled motorcycles.
- HM imports various components of motorcycle for assembly into motorcycles at its factory in Malaysia.
- HM obtained sales tax exemption on imported components to manufacture “finished goods” (motorcycles), as per a condition under Item 1, Schedule C of the Sales Tax (Persons Exempted from Payment of tax) Order 2018 (Exemption Order) (“C1 sales tax exemption”).
- The DG used the RMCD’s Guide on Sales Tax Exemption as at 24 April 2019 (“RMCD Guide”) to interpret that the condition on “finished goods” in C1 sales tax exemption should be limited to only taxable finished goods.
- Subsequently, the DG issued BODs alleging that HM failed to qualify for C1 sales tax exemption, as the motorcycles assembled by HM (using the imported components) are non-taxable finished goods.
- Aggrieved by the DG’s decision, HM applied to the HC for a judicial review of the DG’s decision to issue the BODs.
- At the leave stage of the judicial review, the DG objected to HM’s judicial review application on a ‘procedural’ ground that HM should not have approached the HC; instead, HM ought to have exhausted the statutory remedy of appealing to the Customs Appeal Tribunal (CAT), based on Section 96 of the Sales Tax Act 2018 (“STA”).

Key factors for the HC to grant leave

The HC granted leave to commence judicial review. No reasons have been indicated, but they have apparently accepted the submissions of HM, summarised as follows: (a) Based on *Government of Malaysia & Anor v Jagdis Singh* [1987] 2 MLJ 185 (“Jagdis Singh”), there are exceptional circumstances which warrant the HC to grant leave, namely error of law by the DG leading to his exceeding jurisdiction to issue the BODs by ignoring fundamental principles of interpretation (the fundamental principles are as follows: (i) strict interpretation of taxing statute based on *National Land Finance Co-operative Society Ltd v Director General of Inland Revenue* [1993] 4 CLJ 339, whereby taxing legislation must be interpreted strictly and “finished goods” in C1 sales tax exemption should include “non-taxable” finished goods, and (ii) DG should have ascertained Minister of Finance’s (“MOF”) purpose of granting C1 sales tax exemption, based on principles in *Syarikat Pendidikan Staffield Bhd v Ketua Pengarah*

Hasil Dalam Negeri [2011] 5 CLJ 916, whereby the MOF's purpose is so that the price of the finished goods is not affected due to sales tax being levied on components used in manufacturing and thus it is not MOF's intention to restrict the definition of "finished goods" to taxable finished goods only), (b) Based on Multi-Purpose Holdings Berhad v Ketua Pengarah Hasil Dalam Negeri [2011] 5 MLJ 447, a guide has no force of law and hence there is no legal basis for DG to interpret "finished goods" in C1 sales tax exemption, as taxable finished goods as per the RMCD Guide, (c) Section 96(1) of the STA 2018 where it has been stated that a taxpayer may appeal to the court (HC) as an alternative (to CAT), unlike the appeal provision in the former sales tax regime in section 68(1) of the STA 1972, where the only appeal avenue was to CAT.

Deloitte's comments

A Judicial review is a two-stage process, where leave of the HC has to be obtained by the applicant at the first stage, to proceed to the second stage 'substantive' hearing of the 'merits' of the application for judicial review. HM was successful in obtaining leave of the High Court at the 1st stage, despite the objection by AG's Chambers representing the DG, and the case will proceed to the 2nd-stage i.e., substantive hearing.

HM's success at the leave stage indicates the HC has found prima facie that HM's application is not frivolous or vexatious and that there is some substance in HM's grounds. In Association of Bank officers, Peninsular Malaysia v Malayan Commercial Banks Association [1990] 3 MLJ 228, the Federal Court held that, at the leave stage of judicial review, "applicants must show prima facie that the application is not frivolous or vexatious, and that there is some substance in the grounds supporting the application". Therefore, it would be open to the HC to examine in detail the grounds of HM's application at the second stage 'substantive hearing', and decide whether to allow HM's application for judicial review – see the decisions of the High Court in Almurisi Holding Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri [2020] 1 LNS 1439, which held that the existence of a statutory remedy only falls to be decided at the 'merits' (i.e. second) stage of judicial review, and not at the leave (first) stage, following the Court of Appeal and Federal Court respectively in QSR Brands Bhd v Suruhanjaya Sekuriti & Anor [2006] 3 MLJ 164 and Chin Mee Keong & Ors v. Pesuruhjaya Sukan [2007] 5 CLJ 363.

Nevertheless, at this stage, we would concur with HM's submission that, section 96(1), STA 2018, expressly provides options of appeal to the CAT or the court (HC). Therefore, in our view, it would not be necessary for HM to show "exceptional circumstances" as per Jagdis Singh to bypass CAT and apply for judicial review to the HC – see Court of Appeal decision in Pengarah Kastam Negeri Johor & Anor v Kedai Makan Kebun Teh Sutera Utama Sdn Bhd & Ors And Another Appeal [2014] 3 CLJ 733 ("Kebun"). HM's submission on exceptional circumstances, i.e., error of law leading to lack of jurisdiction, would seem to be a conservative approach out of extreme caution, due to the law not being settled in this area.

There is certainly controversy in HM's submission that the interpretation of "finished goods" for the purpose of C1 sales tax exemption is not limited to taxable finished goods. We would concur with HM that the RMCD guide (indicating C1 sales tax exemption is for taxable finished goods only) does not have the force of law and hence should not dictate the meaning of "finished goods" under the law, i.e., C1 sales tax exemption. However, the C1 sales tax exemption is expressly for finished goods of the person qualifying for the exemption viz. "any registered manufacturer", where the liability to be a sales tax-registered manufacturer is on any manufacturer of taxable goods only. Therefore, the natural or ordinary (in a sense, "strict") meaning of "finished goods" in its proper context of a registered manufacturer's finished goods, should be taxable finished goods only. See the leading Federal Court case on statutory interpretation of taxing statutes, including the ordinary and natural meaning:

Palm Oil Research and Development Board Malaysia & Anor v Premium Vegetable Oils Sdn Bhd [2004] 2 CLJ 265 (“Palm Oil Research”).

Palm Oil Research also laid down a purposive interpretation of tax statutes to avoid any strict (natural or ordinary) interpretation leading to absurdity. As indicated above, the natural or ordinary meaning of finished goods should be taxable finished goods only, and this is not an absurdity. (On the other hand, it could be said to be an absurdity if finished goods is interpreted to include non-taxable finished goods.) A purposive interpretation would give the same result as the above natural or ordinary meaning. The purpose of registered manufacturers being given sales tax exemption on materials to manufacture taxable finished goods would be to impose sales tax at the ‘single stage’ of the finished goods. Where the finished goods are not taxable, the single stage of sales tax would be imposed at the ‘input’ stage of the materials acquired for manufacturing the non-taxable finished goods, since sales tax would not be imposed on the non-taxable finished goods. (The single stage concept of sales tax has been the well-understood purpose of sales tax, since SST 1.0 under the Sales Tax Act 1972. Note there was and is a separate sales tax exemption, on materials for use to manufacture non-taxable goods for export, to promote exports.)

Despite the success at the leave stage, in our view there are formidable challenges for taxpayer (HM) on the issue of merits of the C1 sales tax exemption being for non-taxable finished goods. If the HC decides in favour of taxpayer on this issue at the second stage, it would create unequal treatment and distortion between non-taxable finished goods manufactured by: (a) registered manufacturers (entitled to C1 sales tax exemption); and (b) non-registered manufacturers (not entitled to C1 sales tax exemption). In such an event, we would expect the C1 sales tax exemption to be amended to remove such distortion and maintain the integrity of the single stage concept of sales tax. The HC decision at the second stage is thus eagerly awaited.

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