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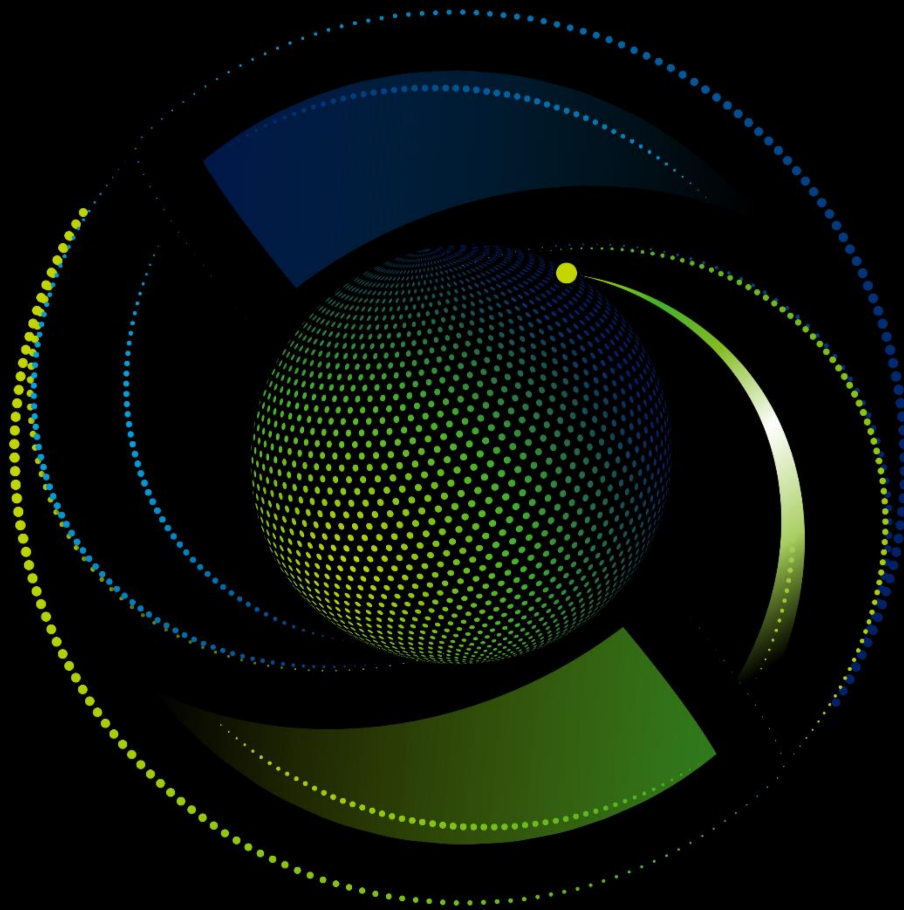

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Indirect Tax Chat

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

May 2023

Issue 05.2023

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Key takeaways:

1. *Legislative updates on SST*
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Greetings from Deloitte Malaysia's Indirect Tax team

Greetings readers, and welcome to the May 2023 edition of our Indirect Tax Chat.

We previously shared the Government's decision to postpone the introduction of the sales tax on low value goods until further notice. The tax was originally slated to commence on 1 April 2023, and to give legislative effect to this postponement, the Minister of Finance has issued a revocation of the earlier appointment date which can be found here.

Moving on to what we will cover in this month's Chat, we look at technical updates including amendments to Sales Tax Orders and Service Tax Regulations. We also cover some interesting insights in relation to the High Court case on the entitlement to Goods Service Tax ("GST") input tax credit by a trader acting as a purchasing agent.

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

- Deputy Finance Minister Steven Sim said that Malaysians are not ready to take on the burden of the Goods and Services Tax (GST) yet as it could cripple the household financial stability of younger families, which is why the tax would not be implemented anytime soon. He said greater fiscal discipline and a focus on ensuring the growth of businesses would be the government's fiscal strategy going forward. Sim added that Malaysia's economic growth hit 5.6% in the first quarter of 2023, surpassing the economic growth of Indonesia (5%), Vietnam (3.2%), China (4.5%) and Singapore (0.1%), click here to read more.

- A circular on the Malaysian Palm Oil Board website showed on Thursday that Malaysia has maintained its June export tax for crude palm oil at 8% and raised its reference price, click here to read more.

- The Royal Malaysian Customs Department will facilitate the transhipment activities for rice and sugar consignments on the duty-free island of Labuan and Sabah. Megah Port Management Sdn Bhd chief operating officer Datuk Seri Patrick Tiong said its constant efforts to highlight transhipment issues to the higher authorities have brought about this new directive. He said the new procedures would benefit players in the transhipment industry in Sabah and Labuan, click here to read more.

For those of you in Southeast Asia, we hope you continue to stay cool and hydrated during this extreme weather. We look forward to chatting with you next month.

Best regards,
Tan Eng Yew
Indirect Tax Leader

1. Legislative updates on SST

Sales Tax (Exemption from Registration) Order 2023, Sales Tax (Goods Exempted from Tax) (Amendment) Order 2023 and Service Tax (Compounding of Offences) (Amendment) Regulations 2023 have been gazetted in April 2023.

Sales Tax (Exemption from Registration) Order 2023

The Sales Tax (Exemption from Registration) Order 2023 ("Exemption Order") was gazetted on 28 April 2023. The Exemption Order extends the exemption as below:

- "Any person who carries on the activity of manufacturing finished goods of the Royal Pahang Weave is exempted from registration under subsection 13(1) of the Sales Tax Act 2018 irrespective of the total sale value of the taxable goods for the period of two years."

Sales Tax (Goods Exempted from Tax) (Amendment) Order 2023

The Sales Tax (Goods Exempted from Tax) (Amendment) Order 2023 ("Amendment Order") was gazetted on 3 April 2023. The amendments were made to Schedule A of the Principal Order, Sales Tax (Goods Exempted from Tax) Order 2022 ("STGEO").

Amendments to Schedule A

The goods under subheadings as follow have been removed from the STGEO as non-taxable goods:

- In relation to heading 12.07, the subheadings 1208.10.0000 and 1208.90.0000 and the particulars relating to it;
- In relation to heading 30.06, in subheading 3006.93.0000, where the item is "solely for medicaments";
- In relation to heading 84.38, the subheading 8438.90.1900 and the particulars relating to it.

Service Tax (Compounding of Offences) (Amendment) Regulations 2023

The Service Tax (Compounding of Offences) (Amendment) Regulations were gazetted on 10 April 2023. The amendment was made to the First Schedule of the Principal Regulations, Service Tax (Compounding of Offences) Regulations 2018.

Amendment of First Schedule

- The "item (xiA) section 73A" was inserted after item (xi) in paragraph (a).

The amendment above includes the following offence under Section 73A of the Service Tax Act 2018 to be one of the offences which may be compounded:

"Any person who causes or attempts to cause the deduction of service tax under subsection 23(1), 34A(1) or 39(2) for himself or for any other person of any amount in excess of the amount properly so deductible for him or for that other person commits an offence and shall, on conviction, be liable:

- to a fine not exceeding fifty thousand ringgit or to imprisonment for a term not exceeding three years or to both.
- to a penalty of two times the amount deducted in excess of the amount properly so deductible."

Deloitte's comments

The Exemption Order and Amendment Order will affect some businesses which were previously exempted from registration for sales tax to register. Meanwhile, some businesses which were previously registered for sales tax may potentially be required to de-register as they may qualify for the sales tax exemption.

The removal of the relevant non-taxable goods under the Amendment Order will also increase the cost of doing business as sales tax will be applicable to the relevant goods purchased from the registered manufacturer or imported into Malaysia.

However, the lack of an indication in the Exemption Order and Amendment Order as to when the Exemption Order and Amendment Order come into effect may cause difficulty for businesses in gauging the extent of the implications to their businesses.

For affected businesses, it would be important to re-evaluate the eligibility of the sales tax exemption to ensure compliance to relevant legislations.

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2. Legal update: High Court decision on GST

On 21 December 2022, the High Court of Malaya ("HC") in Rora Trading Sdn Bhd v Ketua Pengarah Jabatan Kastam Dan Eksais Diraja Malaysia [2022] MLJU 3330, quashed the Royal Malaysian Customs Department's Bill of Demand ("BOD") to RORA Trading Sdn Bhd ("RORA") for RM6.2 million in relation to Goods and Services Tax ("GST").

The BOD related to RORA's acquisition of goods (solar panels) for or on behalf of its overseas customer (principal), Lemoove Investments Sp Z.o.o. ("Lemoove"), that was paid for directly by Lemoove to RORA's supplier.

Deloitte provided litigation support to RORA in connection with the judicial review action at the HC which had a successful outcome for RORA. (Before that, Deloitte had assisted RORA in the Royal Malaysian Customs Department ["RMCD"] audit which had led to the BOD.)

The case is a rare one as it concerns both 'actual supply', and 'deemed supply' under section 65(3) of the GST Act 2014 ("GST Act"), of goods to a trader, RORA, who was an agent acting in own name for Lemoove. The GST law and accounting treatment were thus not straightforward, which led to RMCD failing to appreciate the correctness of RORA's Input Tax Credit ("ITC") claim, as will be discussed in this article.

Summary of key background facts

In summary, the key background facts in RORA's case are as follows:

- RORA entered into an agreement with Lemoove, whereby RORA would effectively purchase goods (i.e., solar panels) for Lemoove. The goods would be purchased by RORA from First Solar Singapore Pte Ltd ("First Solar Singapore") and RORA would sell the goods to Lemoove.

- First Solar Singapore, in turn, purchased the goods from its related company, which manufactured the goods in Malaysia i.e. First Solar Malaysia Sdn Bhd ("First Solar Malaysia").

- RORA, First Solar Singapore and First Solar Malaysia were all GST-registered in Malaysia.

- Therefore, 6% GST was charged in the supply of the goods from First Solar Malaysia to First Solar Singapore and then to RORA.

- As RORA had exported the goods to Lemoove outside Malaysia, RORA's export supply was zero-rated for GST.

- This gave rise to RORA's claim for a refund of ITC (totalling RM6.2 million) of the 6% GST on RORA's acquisition of the goods from First Solar Singapore.

  At the request of RORA, Lemoove had paid First Solar Singapore RORA's purchase price including 6% GST. Nevertheless, all tax invoices from First Solar Singapore were issued to RORA and there was a letter from First Solar Singapore to confirm that First Solar Singapore had received from RORA the payment (made directly by Lemoove), including 6% GST.

- Out of the RM6.2 million total ITC claimed, RM4.8 million had been partially refunded by the RMCD to RORA, after more than 9 months after the date of acquisition and claim of the ITC.

- The BOD had attempted to recover the ITC partially refunded (RM4.8 million) plus penalties (RM1.4 million), totalling around RM 6.2 million from RORA.

- The BOD had been issued by the RMCD due to RORA's alleged non-compliance with section 38 of the GST Act. In the RMCD's view, there was apparently 'no evidence of purchase of the goods in RORA's statutory accounts (statement of income)' and, hence, RORA was allegedly liable to "repay" the ITC under section 38(10) of the GST Act, as deemed output tax. In brief, section 38(10) of the GST Act required ITC to be accounted for by a taxable person as deemed output tax, where the taxable person had failed to pay the consideration for the supply to his supplier within 6 months after the date of supply, as required by section 38(9)(a), GST Act, and where the taxable person had deducted the ITC or been refunded the ITC, as required by section 38(9)(b) of the GST Act, within that same 6-month period.

  (Note: The agreement between RORA and Lemoove required RORA to sell the goods to Lemoove at the same price they were to be purchased by RORA from First Solar Singapore, plus a service fee for RORA. RORA accordingly purchased the goods with 6% GST from First Solar Singapore, for RORA's onward export supply of the goods to Lemoove, at a total price that was effectively higher than the purchase price, due to the inclusion of RORA's service fee in RORA's selling price to Lemoove. RORA's accounts had reflected, as its revenue, only this service fee, which equalled RORA's total selling price to Lemoove minus RORA's total purchase price from First Solar Singapore. This is because RORA was regarded as purchasing the goods on behalf of Lemoove.)

- During the course of the HC judicial review proceedings, it was further argued for the Director General ("DG") of the RMCD that:

  - There was "no direct payment" by RORA to First Solar Singapore and thus "no complete purchase" by RORA – As RORA had requested Lemoove to pay RORA's purchase price for the goods, including 6% GST, directly to First Solar Singapore, the 6% GST was reflected in RORA's accounts as a debt owing by RORA to Lemoove that was to be paid pursuant to the ITC refund by the RMCD.

  - 'No direct payment' and 'no complete purchase' also meant that there was "no allowable or reasonable" ITC for RORA to claim under section 39(1) of the GST Act – Section 39(1) of the GST Act essentially stipulates that a taxable person is entitled to ITC that is "allowable and reasonable" to be attributable to the making of inter alia taxable supplies, which include zero-rated supplies.

<u>*Summary of grounds of HC judgement*</u>

The grounds for the HC judgement to quash the BOD are summarised, as below:

- The term "consideration" in section 2(1) of the GST Act allows any person to make payment for a supply. In this case, Lemoove had paid the consideration for RORA in respect of the supply made by First Solar Singapore to RORA, who then would owe a debt to Lemoove as shown in RORA's accounts (RM6.2 million in 6% GST owed to Lemoove).

- It follows that section 38(9)(a) of the GST Act does not require "consideration" for the supply to be made directly by the taxable person (RORA) to the supplier (First Solar Singapore). The DG cannot ignore the tax invoices from First Solar Singapore to RORA and the letter from First Solar Singapore that payment including 6% GST was received from RORA. Since the payment, including 6% GST was made directly by Lemoove to First Solar Singapore, it created a debt owed by RORA to Lemoove, as evidenced in RORA's accounts where the 6% GST of RM6.2 million is owed by RORA to Lemoove pursuant to the ITC refund by the DG.

- The obligation to "repay" ITC as deemed output tax under section 38(10) of the GST Act is subject to the fulfilment of section 38(9) of the GST Act. Section 38(9)(b) of the GST Act must be read with section 38(10) of the GST Act, which requires the ITC to be deducted or refunded to RORA within the same period of 6 months after the date of supply. There was no deduction of the ITC by RORA since RORA's supplies to Lemoove were zero-rated. And the DG does not dispute that the ITC partially refunded to RORA (RM4.8 million) was refunded more than 9 months after the date of supply. Therefore, the basis of the DG to require RORA to account for the ITC as deemed output tax under section 38(10) of the GST Act, is inconsistent with section 38(10) of the GST Act read with section 38(9)(b) of the GST Act.

- The DG's assertion that "no direct payment" meant "no allowable or reasonable" ITC claimable by RORA under section 39(1) of the GST Act is out of context of section 39(1) of the GST Act. This is because section 39(1) of the GST Act stipulates "allowable and reasonable" ITC claimable in the context of attribution of the ITC to taxable supplies, including zero-rated supplies, like RORA's zero-rated export supply to Lemoove. The DG did not dispute that RORA's supplies to Lemoove were zero-rated export supplies. Hence, RORA's ITC on the acquisition of the goods from First Solar Singapore was allowable and reasonable to be attributed to RORA's zero-rated export supply, and thus claimable by RORA as ITC.

- The agreement between RORA and Lemoove showed that RORA purchased the goods (for) and on behalf of Lemoove though the tax invoices from First Solar Singapore to RORA issued in RORA's own name. The DG does not dispute that RORA purchased the goods on behalf of Lemoove. Under section 65(3) of the GST Act, the GST treatment of an agent acting in their own name deems a supply to the agent and by the agent. Therefore, besides the 'actual supply' of the goods by First Solar Singapore to RORA as evidenced by tax invoices in RORA's name, section 65(3) creates a 'deemed supply' by First Solar Singapore to RORA and by RORA to Lemoove. Paras 13 and 14 of the DG's own GST Guide on Agents, support RORA's position on section 65(3) of the GST Act - paras 13 and 14 indicate the DG's view that, it is only "sometimes" that the commercial reality of a transaction entered into by an agent acting in own name, is between the principal and the third party. This fits RORA's case that the transaction to purchase the goods is between RORA and the third party (First Solar Singapore).

- It is the duty on the part of the DG as a public authority to give reasons at the time decision is conveyed and not at the time an application for judicial review was filed (Uniqlo v Ketua Pengarah Kastam dan Eksais [2020] 9 CLJ 521 ["Uniqlo"] and Kesatuan Pekerja-Pekerja Bukan Eksekutif Maybank v Kesatuan Kebangsaan Pekerja-Pekerja Bank [2017] 4 CLJ 265 were cited).

- The written basis of the DG before the BOD was issued was that there was no purchase recorded in the accounts (statement of income) of RORA. This is a substantially different reason from the reasons given by the DG during the judicial review proceedings i.e. no direct payment, incomplete supply/purchase, unreasonableness under section 39(1). These latter reasons are indeed afterthoughts by the DG, which are not to be taken into account by the HC.

- As a conclusion, RORA has demonstrated that the DG had acted ultra vires the GST Act and therefore the BOD is quashed. Accordingly, the DG was directed by the HC to refund the balance ITC of around RM1.4 million (i.e. RM6.2 million - RM4.8 million partially refunded), with interest, to RORA by virtue of section 38(3) of the GST Act.

Deloitte's comments

The HC decision is a formidable one from a GST technical aspect.

Deloitte had worked closely with external legal counsel appointed by RORA to provide strong GST technical grounds as input into legal counsel's submissions for RORA to the HC, from GST law including GST case law, all of which were accepted by the HC in its reasoning.

These included that, under GST law the obligation to "repay" ITC is premised on the existence of a supply/acquisition (purchase) by RORA for which RORA had received the benefit of ITC refund but did not pay the supplier, within a period of 6 months after the date of supply. Hence, the RMCD was contradicting itself in alleging there was no evidence of purchase by RORA. Deloitte had also developed the arguments based on "deemed supply" under section 65(3) of the GST Act.

More importantly, based on GST case law ("Uniqlo"), Deloitte advanced 'natural justice' grounds for legal counsel to argue that public decision-makers like the DG are bound to written reasons given at the time of decision-making (i.e. no evidence of purchase as alleged by the RMCD in its written decision to RORA) and that the RMCD was prohibited from advancing substantially different reasons in court (i.e. no direct payment, unreasonableness etc). This HC case solidifies the precedent that the RMCD would be bound by natural justice to written reasons at the time of decision-making that cannot be altered during court proceedings. It should be noted that the DG is appealing to the Court of Appeal. It is hoped that the HC decision would be affirmed by the Court of Appeal in order to further strengthen this precedent.

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