Goods and Services Tax (GST) – Counting Down

by Wong Chow Yang

After years of indecision and speculation revolving around the introduction of a GST framework in Malaysia, the Government finally announced an implementation date for GST during the 2014 Budget proposals that were presented back in October 2013. A proposed implementation date of 1st April, 2015 was set, meaning that businesses had less than 18 months from date of that announcement to prepare for the introduction of GST. Three months have passed since the announcement back in October 2013 and as we are now well into 2014, it is perhaps time to take stock of where we are with the GST legislation and assess if things are moving according to plan.

The GST Framework

Let us start by taking a look at the legislation that will give effect to the GST framework. Until today, the updated GST bill has yet to be tabled in parliament. If GST is to come into effect on 1st April, 2015, the relevant laws would need to be in place now so that businesses can proceed with certainty to deal with GST issues and to prepare their systems to be GST ready.

Legislation aside, the Customs authorities would also have to resolve issues that are faced by specific industries, hold numerous dialogues with representatives from those industry groups and eventually finalise practice notes or guidelines on transactions where the GST treatment is either uncertain or contentious in nature. To put this into perspective, consider that as of today, in draft form, there is one general guide, over thirty industry guides and fourteen specific guides dealing with numerous GST issues which are available in the public domain. The Customs authorities have indicated that there will ultimately be more than sixty industry guides which means that there is still much to be done, particularly as new representations from different industries continue to be made to the authorities to lobby for special treatment and to seek clarity on issues.

Without this entire framework properly in place, it is difficult to see how businesses can be fully ready to transition to a GST system by the intended implementation date. It is clear that the Government is committed to introducing the GST regime in 2015 and that remains a certainty. However, if the GST legislation were to be delayed much further, it would certainly be within the realms of possibility that the GST implementation date may be delayed by a few months to allow smoother transition to the new tax regime. There are rumblings that this is increasingly likely.

Are Businesses Preparing Themselves for GST?

Under the proposed GST regime, a person who makes annual taxable supplies of goods or services exceeding RM500,000 will be required to register for GST. Given this relatively low threshold, many small and medium sized businesses in Malaysia will be required to register for GST. What is clear is that many large businesses are currently devoting significant time and resources in preparing for the imminent new tax regime, while others are now only beginning to seek help from tax experts in preparing for GST. On the other hand, it would appear that many of the small and medium sized businesses will continue to adopt a wait and see approach and that can only result in rush and panic when it is time to register for GST.

Why then is there a lack of urgency shown by so many businesses when it comes to GST? One of the primary reasons is due to a lack of understanding of the amount of time and resources needed to prepare a GST compliant system within an organisation. The expectations are often out of sync with reality.

Let us take a closer look at the GST framework and related laws to understand why this is the case.

The GST system, which is similar to other VAT systems around the world, is, at its very foundation, a system designed to tax the value added components within a supply chain, with the tax ultimately borne by the final customer at the end of that supply chain. This is essentially achieved by requiring a business entity to charge GST on the supply of goods and services ("taxable supplies"). GST charged on the making of taxable supplies is known as "output GST". The business entity is then entitled to claim back GST that it pays on its expenses and acquisitions of assets, known as "input GST", used to make taxable supplies. The excess of any output GST over input GST would be required to be paid over to the Customs authorities. Conversely, any excess of input GST over output GST would mean that the Customs authorities would need to refund the excess to the business entity. This summarises the basic tenets of a GST or VAT system.

In the Malaysian GST framework, there is a distinction to be drawn between taxable supplies and exempt supplies. Taxable supplies are those which are subject to GST, and depending on the types of goods or services in question, the rate of GST can be either at the proposed standard rate of 6% or zero rate (0%). Exempt supplies on the other hand are not subject to GST. As an example,

the supply of residential properties will be an exempt supply while the supply of commercial properties will be standard rated. Exports, on the other hand, are zero rated supplies.

The distinction between a taxable supply that is zero rated and an exempt supply that is not subject to GST is important because input GST on expenditure incurred by a business can only be claimed if the expenditure is directly attributable to taxable supplies. If the expenditure relates specifically to exempt supplies made by the business, no input GST will be allowed, meaning that GST incurred on that expenditure cannot be recovered.

If a business provides mixed supplies, comprising both taxable and exempt supplies, then GST incurred on expenditure that relates to both types of supplies will have to be apportioned such that only that portion of GST incurred relating to taxable supplies will be allowable as input GST. The rules (known as the Capital Goods Scheme) with regard to the apportionment of input GST in relation to capital goods used for making mixed supplies are somewhat complex. The portion of input GST that is attributed to exempt supplies will not be recoverable.

In addition, there are also specific types of expenditure where no input GST is allowed to be claimed. These are generally referred to as blocked inputs. There are also conditions under which a business is deemed to make taxable supplies and would therefore have to account for output GST under those circumstances, although no consideration is received. The above is just a brief overview of some of the key issues for consideration in the Malaysian GST scenario.

Steps Needed to Prepare a Business for GST

A GST implementation exercise will necessarily involve an analysis of all expenditure and revenue streams arising from various business processes within the supply chain of the business. The

incidence of GST will have to be identified for each stage of those processes. Contracts and trading terms will also have to be reviewed for GST implications. Intercompany transactions will need to be reviewed to determine the exposure to GST. If intercompany arrangements are exposed to GST, there may be a need to reassess the structure and terms of those arrangements to make them more efficient.

Enterprise information systems will have to be reconfigured to incorporate GST modules into the systems. Crucially, accounting and billing systems will have to be ready to produce accurate GST reports, tax invoices and to ensure GST compliance in an accurate and timely manner, especially in view of the penalty provisions for non-compliance under the GST framework. Employees will also need to be trained on the application of GST on business processes.

Impact of GST on the Pricing of Goods and Services

For businesses that produce goods or services that are exempt supplies, as outlined above, input GST incurred on expenditure relating to the making of those exempt supplies will not be recoverable. Consequently, the cost of producing such products or services may rise, depending on whether those costs would previously have been subject to sales tax and/or service tax. In this context, it should be noted that sales tax (10%) and service tax (6%) will be replaced by GST at 6%. However, sales tax and service tax currently only apply to certain goods and services, whereas, the GST net will be much wider, hence the anticipated increase in costs. For exempt suppliers, the input GST cost which cannot be recovered will inevitably lead to embedding the cost of input GST into the pricing of their products or services. It is therefore necessary to understand the incidence of input GST to undertake a pricing review exercise.

Still a Work in Progress

It is clear that there is still much to be done both by regulators and businesses to prepare for the introduction of GST and both sides would need to do their part in ensuring a smooth transition to a GST system. For business organisations, as alluded to above, preparing for GST clearly involves much time and resources across different functions within the organisation. The authorities in turn must enact the law and provide the relevant guidelines to enable businesses to move forward with GST implementation with certainty and clarity. Everyone needs more time to prepare for GST, it appears. Time is, however, not a luxury anyone can afford.

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