Withholding tax rate to be reduced to 10%

QUESTION 1
What are the changes proposed in the budget affecting withholding tax payments to non-resident contractors who carry on business in Malaysia?

ANSWER:
In 1983, tax laws were introduced to ensure that non-resident contractors who carry on business in Malaysia pay income tax on profits earned in

This is the final part of the Q & A series which The Star and leading accounting firm PricewaterhouseCoopers are running in relation to tax and other issues in conjunction with Budget 2003.
Malaysia to ensure that they file tax returns to the Malaysian tax authorities while carrying on a business here.

It was realised by the Malaysian tax authorities then that there were many non-resident contractors who did not register a file with the Inland Revenue Department and submit tax return while carrying on a business in Malaysia.

By the time the authorities were aware of the presence of these non-resident contractors, these contractors had already completed their projects and left Malaysia.

To overcome this problem, the tax laws require payments to a non-resident contractor for services rendered under a contract be subject to a withholding tax of 15% for purposes of income tax of the non-resident contractor and 8% for the non-resident contractor’s employees.

This 15% withholding tax is merely an advance payment by the non-resident contractor who is then required to submit a tax return to determine its actual tax liabilities. The 15% withholding tax suffered is then compared with the non-resident contractor’s actual tax liabilities to determine whether additional tax payment is due or if there is excess payment, the amount is to be refunded to the non-resident contractor.

The 8% withholding tax will also be refunded to the non-resident contractor once it can be proven that the non-resident contractor’s foreign employees have submitted tax returns in Malaysia and paid taxes on their employment income.

Since 1983, while the income tax rate for companies has been reduced from 40% to the current rate of 28%, the withholding rate for non-resident contractors has remained the same.

The Finance Minister has now proposed to reduce the withholding tax to 10% for purposes of income tax of the non-resident contractor and 3% for the non-resident contractor’s employees.

The proposed reduction will improve the cash flow of the non-resident contractors.

**QUESTION 2:**

The company may be offering a voluntary separation scheme (VSS) to its employees. What are the implications of the proposed amendment to the tax-exempt amount for payments made to the employees under this scheme?

**ANSWER:**

Under current legislation, compensation paid to employees who are retrenched or who participate in VSS are exempt to the extent of RM4,000 for each completed year of service. To recognise the increased cost of living, it was proposed that the exemption amount of compensation paid be increased to RM6,000 for each completed year of service.

The proposed amendment will be effective beginning in Year of Assessment 2003.

**QUESTION 3:**

I have been told that Singapore is moving towards a one-tier tax system soon where the dividends received from a Singapore company would not be taxable.

Please explain the difference between Singapore’s one-tier system and our Malaysian tax system in respect of dividend income.

Besides, would the exempt dividend income received from Singapore under the one-tier system be taxable in Malaysia?

**ANSWER:**

Malaysia adopts a tax system known as “imputation system” for dividends paid by companies resident in Malaysia.

Under the imputation system, in simple terms, tax paid by a company on its income will be deemed to be an advance tax paid on behalf of its shareholders and it will be credited to an account called Section 108 account.

When the company subsequently pays dividend to its shareholders, the tax paid in advance by the company will be imputed to the shareholder at the prevailing corporate tax rate as tax deducted at source. The gross dividend (including the tax deemed deducted at source) received by the shareholder will be taxable in his hands but he will be able to claim the tax at source as tax credit against the tax payable on his total income.

In cases where the tax credit exceeds the tax payable, he will be entitled for a refund.

Singapore adopts a similar system currently but has announced in its recent budget that it will be introducing a one-tier tax system where tax paid by a Singapore company will be a final tax and no credit will be attributed to its shareholders.

Further, dividends paid by a Singapore company will be exempt from tax in the hands of the shareholders.

Singapore’s one-tier system was aimed at reducing massive paper work and record keeping which need to be maintained in respect of taxes paid by companies.

On your last question, exempt dividends declared by a Singapore company and received by a Malaysian tax resident will be taxable in Malaysia.

**QUESTION 4:**

The Finance Minister has in his budget speech proposed 10 measures to reduce the cost of doing business to enhance the country’s competitiveness.

Under the third measure he proposed that the valuation method for sales tax on imported goods, which is based on the actual transaction value, be adopted for locally manufactured goods.

1. Could you elaborate on what is meant by actual transaction value?

2. Does this mean the sales tax levied on locally manufactured goods will be at parity with imported goods?

**ANSWER:**

Budget 2003 proposed that the valuation method for locally manufactured goods be standardised with that of imported goods.

The value of imported goods is determined in accordance with the Customs (Rules of Valuation) Regulations, 1999, which is adopted from the WTO customs valuation system.

1. Under the WTO customs valuation system, the transaction value is the actual price paid or payable for the goods.

2. The intention of the proposal is that the valuation method for locally manufactured goods should be the same as that adopted for imported goods.

**QUESTION 5:**

If you were to import goods worth RM450 into Malaysia via air express cargo other than KLIA, would I be eligible for any exemption from import duty and sales tax?

**ANSWER:**

Budget 2003 has proposed to exempt import duty/sales tax on goods, excluding liquor and cigarettes, worth RM500 (the limit on the value of the goods is increased from RM200 as at present) imported via air express cargo through all international airports (and not only KLIA as at present).

However, Budget 2003 did not announce when the proposal would be effective from. Therefore, it would be better if you could wait for the gazette to be published before importing the goods, to ascertain when the exemption is effective from.