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Malaysia's Budget 2025 Targets Growing Tax Revenue and Investors

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Irene Yong of Shearn Delamore & Co. discusses the most salient features of Malaysia's Budget 2025 proposals that aim to increase tax revenue and attract foreign investors.

As the largest budget ever tabled for Malaysia, Budget 2025 seeks to increase tax revenue and broaden the tax base of both direct and indirect taxes amidst a review of the existing tax incentive framework. Notably, despite the recent implementation of a capital gains tax with effect from January 1, 2024, more new taxes are being proposed for subsequent years of assessment ("YAs"), such as the carbon tax on the iron, steel and energy industries, and a dividend tax. Some of the salient Budget 2025 proposals are discussed below. Unless otherwise stated, the proposed amendments discussed below, when passed by Parliament, would take effect from YA 2025.

Dividend Tax

Dividends (in monetary form or otherwise) paid, credited, or distributed by a tax-resident company to a shareholder who is either a tax-resident or non-resident individual would be subject to a 2% dividend tax on the individual's dividend income above RM100,000. Dividends below that threshold would remain tax-exempt as would be dividends paid to corporate shareholders.

Other dividends that may be tax-exempt include foreign-sourced dividends, dividends distributed from profits of companies with pioneer status or reinvestment allowances or from shipping companies' tax-exempt profits, dividends distributed to contributors or depositors by unit trusts or the Employees' Provident Fund, and dividends distributed by Labuan companies to residents, among others. The exact scope of the exemptions remains unclear and concerns linger over the impact of possible double taxation upon shareholders and investors.

There would be additional compliance requirements for companies as they are required to inform individual shareholders of the gross amount of the dividend. Further, where dividend in specie is

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distributed consisting of property, its market value at the time of distribution would have to be ascertained.

Global Minimum Tax

To mitigate the impact of the Global Minimum Tax ("GMT") on investments into Malaysia, the feasibility of a Strategic Investment Tax Credit is being considered. In the meantime beginning on January 1, 2025, a Marketable Transferable Tax Credit would be incorporated as a tax credit to reduce liability for a covered tax in the jurisdiction that issued the tax credit.

New Investment Incentive Framework

Aimed at attracting foreign investors in high-value activities with a targeted implementation in Q3 of 2025, the new investment incentive framework would encompass tax incentives such as a double tax deduction that would be granted to multinational enterprises ("MNEs") that incur expenses on supply chain resilience initiatives of up to RM2 million annually for three consecutive years.

Aside from that, the amount invested in joint ventures entered into with other local vendors by MNEs or their suppliers would also be tax-deductible while local suppliers participating in this initiative may also qualify for an outcome-based tax incentive package.

In addition, investments made in 21 economic sectors in the states of Perlis, Kedah, Kelantan, Terengganu, Sabah, and Sarawak may also qualify for income tax incentives.

Further, the increased export incentive, which exempts income equivalent to 50% of the value of increased exports, provided it does not exceed 70% of the statutory income for that YA, would be extended to Integrated Circuit design services.

Investments into carbon capture, utilization, and storage activities which are compliant with Environmental, Sustainability, and Governance ("ESG") standards may qualify for investment tax allowances and income tax exemptions.

Forest City Special Financial Zone

The Single Family Office Scheme ("the Scheme") for Forest City Special Financial Zone ("Forest City"), located in the state of Johor, is targeted to be operational by Q1 of 2025. Under the Securities Commission’s purview, the Scheme would be part of the tax incentive package available for Forest City with benefits such as a 0% concessionary tax rate on income generated by eligible investments from the single family office vehicle ("SFOV") for an initial period of 10 years (renewable for another ten years if relevant conditions are met). The requisite conditions would include requiring a new investment holding company to be incorporated in Malaysia that manages at least RM30 million in assets and invests at least 10% of such assets (or RM10 million, whichever is less) in eligible local investments. The SFOV would also be required to have a management company operating in Forest City employing at least one investment professional.

Apart from the Scheme, activities conducted in Forest City relating to financial global business services, financial technology, and foreign payment system operators may qualify for a concessionary 5% tax rate. Special tax deductions on relocation costs and enhanced industrial building allowances would also be available for banks, insurers, capital market intermediaries, and other eligible entities in the financial sector.

Other Tax Incentives, Deductions, and Benefits

From January 1, 2025 to December 31, 2027, investors and/or operators of Smart Logistics Complexes ("SLCs") would be able to apply to the Malaysian Investment Development Authority ("MIDA") for an Investment Tax Allowance if they invest in the construction of smart warehouses and undertake logistics services activities such as regional distribution centres, integrated logistics services, storage of hazardous goods, or cold chain logistics. Alternatively, the SLC operator may qualify for the incentive by leasing a smart warehouse for at least 10 years and undertaking eligible logistics services.

New machinery and equipment donated by companies to the Institut Latihan Kemahiran Awam, polytechnics, and registered vocational colleges from YA 2025 to YA 2027 would qualify for a tax deduction.

A one-off additional 50% tax deduction would be given to employers who incur the following expenditures, provided that their applications are received by Talent Corporation Malaysia Berhad between January 1, 2025 and December 31, 2027:

expenses incurred for capacity building and software acquisition to implement flexible work arrangements, capped at RM500,000;provision of up to 12 months of additional paid leave to employees caring for children or ill or disabled family members; oremployment expenses incurred for a period of 12 months on hiring women who return to work after a career break of least two years.

Effective for YAs 2024 and 2025, expenditures incurred on the purchase of information and communication technology equipment, computer software packages and consultation, licensing and incidental fees relating to customized computer software development, for implementing e-invoicing would be given accelerated capital allowances at the rates of 20% and 40% for the initial and annual allowances respectively.

Sales and Service Tax

Commencing May 1, 2025, the scope of the Sales and Service Tax ("SST") regime would be progressively expanded. Service tax would be imposed upon B2B commercial services while the rate of sales tax imposed upon non-essential items, such as imported premium goods, would be increased.

Stamp Duty

Loan or financing agreements executed by Micro, Small and Medium Enterprises ("MSMEs") and investors from January 1, 2025 to December 31, 2026 to raise capital through the Initial Exchange Offering ("IEO") platforms which are registered with the Securities Commission, are exempt from stamp duty. Further, with effect from January 1, 2025, approved loan or financing agreements executed between MSMEs and financial institutions under the ‘Skim Pembiayaan Mikro’, a micro financing scheme, will be exempt from stamp duty for loans of up to 100,000 (increased from RM50,000).

The self-assessment system for stamp duty would be implemented in stages, commencing:

January 1, 2026 for rental or lease agreements, securities and general stamping;January 1, 2027 for transfers of ownership in properties; andJanuary 1, 2028 for all other instruments.

Correspondingly, numerous new enforcement provisions have been proposed under the Measures for the Collection, Administration and Enforcement of Tax Bill 2024 slated to take effect from January 1, 2026. These provisions will empower the Collector of Stamp Duties to search and inspect any instrument, record, article, or thing. Conversely, taxpayers will be subjected to more onerous record-keeping and reporting obligations in tandem with new offences being created, such as for failing to file the relevant returns or to keep relevant records for the requisite seven years from the date the stamp duty is paid.

Late stamping penalties will also be increased to RM50 or 10% of the amount of deficient stamp duty (whichever is greater) if stamping is done within three months after the time for stamping. Thereafter, a penalty is imposed at RM100 or 20% of the amount of the deficient duty (whichever is greater).

Labuan Business Activity Tax

Starting January 1, 2025, the basis period applicable under the Labuan Business Activity Tax Act 1990 ("LBATA") will be changed from the preceding year to the current year basis, bringing it in line with the Income Tax Act 1967 ("ITA"). The self-assessment system will also be implemented for Labuan entities chargeable to tax under LBATA from YA 2025 (current year basis).

Labuan entities carrying on a Labuan trading activity enjoy a preferential tax rate of 3% under LBATA. Although previously regarded as Labuan trading activity, shipping operations would no longer be regarded as a "Labuan trading activity" with effect from January 1, 2025, and will be taxed under the ITA.

Individual Taxation

Income tax exemption on foreign-sourced income that has already been subjected to income tax in the source country and received in Malaysia by the individual, would be extended from December 31, 2026 to December 31, 2036.

Under the Budget 2025, generally, the various tax reliefs for tax-resident individuals relating to expenses incurred on sports activities, sports equipment, and medical expenses, would be enhanced. Aside from that, the tax relief on premiums paid for education and medical insurance would be increased to RM4,000, while tax relief on payments of deferred annuity premiums would be extended to YA 2030.

Tax deduction of up to RM7,000 would also be granted to first-time homebuyers who are tax-resident citizens on their mortgage interest payments. This would apply to residential properties with purchase price not exceeding RM500,000. A lower tax relief of RM5,000 would be available for residential properties with a purchase price above RM500,000 to RM700,000. This relief would be available for three consecutive YAs for sale and purchase agreements executed between January 1, 2025 and December 31, 2027.

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