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# Service Tax on Digital Services in Malaysia

17 April 2019

# Breaking News:

## *Malaysia has introduced a new Service Tax on digital services*

**“ The digital tax is to provide a level playing field among local and foreign companies, as well as between online and offline service providers ”**

*Datuk Amiruddin Hamzah, Deputy Finance Minister of Malaysia  
9 April 2019, The Edge*

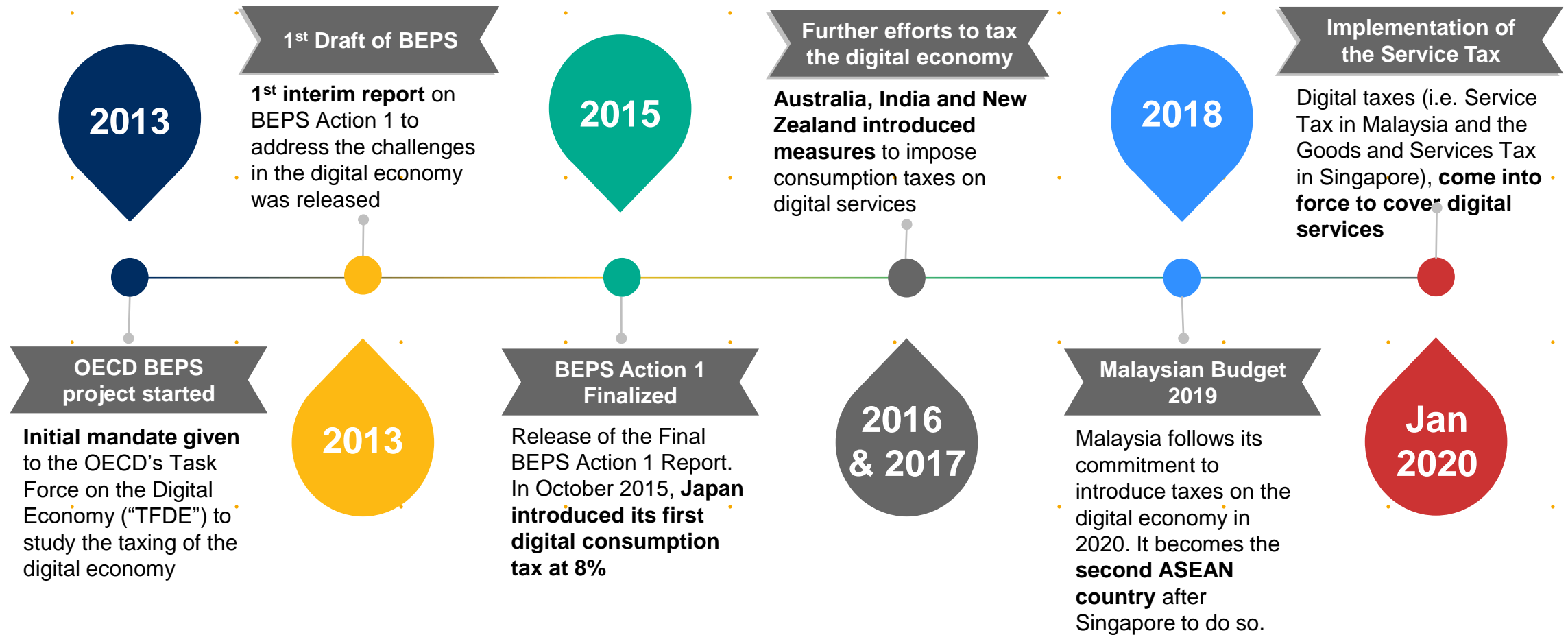
### **Salient Points of the new Service Tax**

- Effective 1 January 2020
- Imposition of a 6% Service Tax on digital services provided by Foreign Service Providers (“FSPs”) by an amendment to the Service Tax Act 2018
- FSPs are required to register from 1 October 2019

# Why has Malaysia taken this step towards implementing a Service Tax on digital services?

-  The number of digital based services offered by businesses to consumers has significantly increased in past years. At present, around **95% of businesses worldwide benefit from high speed internet** connection (OECD, 2018).
-  Reduction of the tax base of countries around the world due to **Base Erosion Profit Shifting (“BEPS”)** has **worsened due to digitalization trends**. These trends have also resulted in an **unlevel playing** field between offline and online businesses.
-  To counter this BEPS, initiatives by the Organization for Economic Cooperation and Development (“OECD”) (e.g. BEPS Action Plans) have been introduced to redevelop global tax systems as **current tax rules are no longer “fit-for-purpose” to tax the digital economy**.
-  The **BEPS Action 1: Addressing the Tax Challenges of the Digital Economy** was issued in 2015, to propose recommendations for global tax administrators to tax digital businesses (e.g. through consumption tax systems). Since then, many developments have taken place that have led to Malaysia’s implementation of the Service Tax on digital services in 2020.

# Timeline on development of Digital Taxes in Malaysia and the World



# Implementation of Service Tax on Digital Services in Malaysia

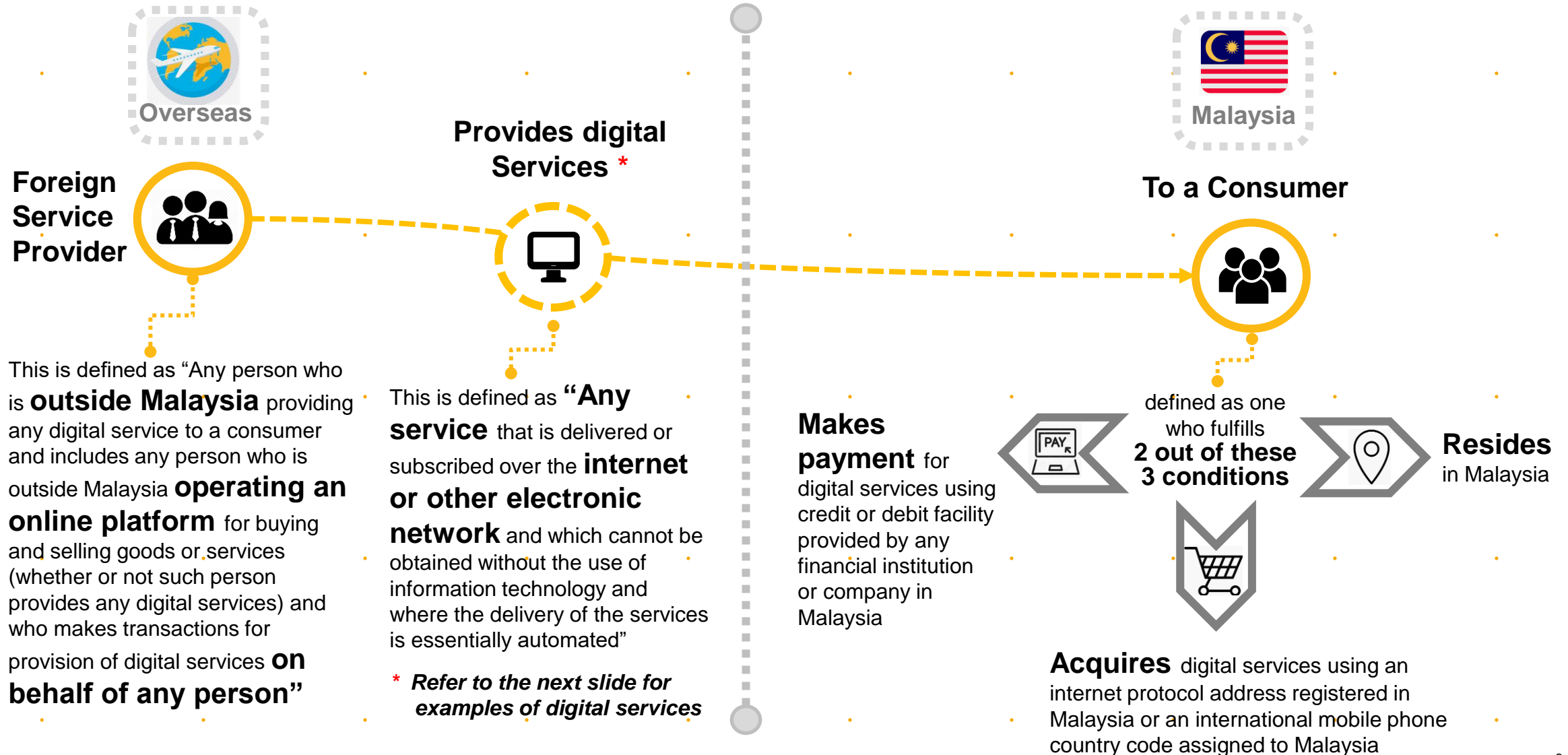


From 1 January 2020 onwards, a Foreign Service Provider (“FSP”) providing “digital services” to a **consumer** is required to register for Service Tax if the taxable turnover of the FSP is more than the registration threshold of RM500,000.

In general, a “consumer” means a person who purchases goods or services for personal use and not for resale purposes. The definition of “consumer” for digital service tax purposes is separately defined to include any person who fulfils any two out of three conditions (i.e. makes payment, acquires digital services, or resides in Malaysia). In this regard, a person who purchases on behalf of another person may also be defined as a “consumer” for digital service tax purposes.

Sometimes, the digital service may be provided by another party. In such circumstances, the indirect service provider may also be covered under the Service Tax Act due to the words “**on behalf of any person**”. In other words, the FSP who does not directly provide the digital services to a consumer may also be liable to register for Service Tax.

# Mechanism of the Service Tax on Digital Services



# Examples of Digital Services

## Online movie / streaming sites



**Netflix**  
**Spotify**

## Cloud computing



**Amazon**  
**Google**  
**Microsoft**

## Online games



**Tencent**  
**Sega**  
**King**

## E-commerce



**Lazada**  
**Alibaba**  
**11street**

## Apps Store



**Google Play**  
**Apple Apps Store**

## Online Ads



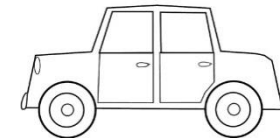
**Facebook**  
**YouTube**  
**LinkedIn**

## Online Payment Gateway



**PayPal**  
**iPay88**

## E-Hailing



**Grab**

# Digital Service Tax Framework



It is important for the FSPs to understand the Service Tax framework on digital services to be implemented in Malaysia to ensure compliance with the Service Tax legislation in Malaysia.

The Service Tax compliance framework includes but is not limited to the following aspects; effective date, the time when Service Tax is due and the taxable periods for reporting purposes.



# Compliance requirements

**6%  
on**

The “value of supply” should be the value charged by the foreign registered person

**Due** at the time  
**when  
payment is  
received** by  
the foreign  
registered person

#### **Transitional period:**

- If the digital service is provided before the effective date and spans after the effective date, the digital services provided after effective date shall be subject to Service Tax (“SET”);
- If payment is received before the effective date and the digital service is provided on or after the effective date, such digital service shall not be subject to SET.

Taxable period:  
**Every 3  
months**

Filing and Payment :  
Not later than the  
**last day of the  
month**  
**following** the  
end of the taxable  
period

Effective date:  
**1 January  
2020**

Registration  
threshold:  
**RM500k**

# Registration and Furnishing of Service Tax Return



The Foreign Service Provider that provides digital services exceeding the registration threshold should register three (3) months before the effective date. Since the effective date is 1 January 2020, the FSP should register by 1 October 2019.

We provide in the next slide a timeline of the compliance procedures and penalties for non-compliance.

# Timeline for Service Tax (SET) Registration and Filing

1 October 2019



1 January 2020



31 March 2020



30 April 2020



## Application for registration

Foreign service provider who is liable to be registered shall apply for registration **3 months** before the effective date by using the prescribed form

- If he has reasonable grounds for believing that the total value of digital services from 1 Jan 2020 to 31 Dec 2020 will exceed RM500k

### ➤ Failure to register before effective date:

On conviction, he is liable to a fine not exceeding RM30,000 or imprisonment not exceeding 2 years or to both

**Effective date**

## First taxable period

The taxable period for a foreign registered person shall be **3 months** ending on the last day of any month of any calendar year (instead of 2 months for other types of taxable services.)

### ➤ Failure to charge the SET:

On conviction, he is liable to a fine not exceeding RM50,000 or imprisonment not exceeding 3 years or to both

## Submission of first return and payment

Foreign registered person shall furnish the SET return by using the prescribed form and pay SET to the Director General of Customs

### ➤ Failure to make payment:

No prosecution is instituted:

- First 30 days overdue: 10% of unpaid SET;
- Second 30 days overdue: additional 15% of unpaid SET; and
- Third 30 days overdue: additional 15% of unpaid SET.

On conviction, FSP is liable to a fine not exceeding RM50,000 or imprisonment not exceeding 3 years or to both

### ➤ Failure to furnish return:

On conviction, the FSP is liable to a fine not exceeding RM50,000 or imprisonment not exceeding 3 years or to both

# Challenges of Implementing the Digital Service Tax



With this introduction of the new Digital Service Tax in Malaysia, there will likely be uncertainties and ambiguities faced by Foreign Service Providers (“FSPs”) and consumers. To enhance the compliance requirements, it is hoped that the RMCD will provide more information and guidelines to address such uncertainties.

We present in the next slide the possible challenges faced by Foreign Service Providers, Consumers and the Royal Malaysian Customs Department in the implementation of this tax.

# Possible clarifications required on the Digital Service Tax

## From the perspective of the FSPs

### Liability to be Registered

- How is the FSP to identify whether the services are provided to the consumer “in Malaysia” and not to another country?
- Will FSPs who have unique business models be liable to be registered for the Digital Service Tax (e.g. foreign domiciled company with or without an establishment in Malaysia, local agent who acquires the digital services from overseas and provides to the consumer in Malaysia, etc.)?
- Is there any exemption from registration in Malaysia?
- Will there be double taxation of the digital services provided by the FSPs if the FSP is taxed in both countries?

### Application for Registration

- How does the FSP register?
- Is there any prescribed form provided by the RMCD?
- Can it be done online?

### Format of Invoice

- Is it compulsory for the FSP to issue an invoice with all prescribed particulars?

### Filing / Furnish of Return

- How does the FSP furnish the return?
- Is the return to be submitted by the FSP similar to the existing SET-02 return?

### Payment of SET

- How should the FSP make payment to the RMCD?

## From the perspective of the Consumers

- ❖ Under what circumstances will a consumer be exempted from payment of SET on the digital services acquired from the FSP?
- ❖ Is there any cost saving to subscribe for the digital services from the FSP through a local agent in Malaysia?
- ❖ How will the consumer know that the tax imposed on them by the FSP is eventually remitted to the RMCD?

## Enforcement by the RMCD

- How can the RMCD compel the FSPs who provide digital services to register for SET and comply with all the requirements stipulated in the Service Tax Act?
- How will the RMCD trace the turnover of the FSPs and know whether they exceed the registration threshold of RM500,000?

# Comments by Crowe Malaysia in The Edge Malaysia (15 April – 21 April Edition)

8 | CORPORATE | THE STATE OF THE NATION A WEEKLY UPDATE | THE EDGE MALAYSIA APRIL 15, 2019

## The digital tax conundrum

BY JOYCE GOH

The 6% digital service tax, announced by the government last week and coming into force on Jan 1 next year, may face hurdles in its execution given that the foreign service providers caught under this tax may not have a physical presence in the country.

The digital tax conundrum is not unique to Malaysia, says Amarjeet Singh, Malaysia tax leader at Ernst & Young Tax Consultants Sdn Bhd. "Governments around the world are considering various options in implementation and enforcement," he says.

He points out that a key issue in enforcing the tax is how to encourage or ensure compliance among foreign entities with no physical presence here.

"We would expect the large players to take steps to comply with the obligations for reputational reasons. However, foreign service providers can be from any part of the world and the speed of trends these days means it will be difficult to accurately identify or anticipate the actual size and scope of digital services that will be covered under the digital tax scope," says Amarjeet.

"Potential sources of information could be through financial models and how income is earned evolves. Income earned may not be territorial anymore for tax purposes. It could be borderless and taxed in many countries," he points out.

Indeed, countries are aware of leakages in taxes when it comes to digital income.

Last month, German Finance Minister Olaf Scholz raised concerns about tech giants paying tax "nowhere" and stressed the need for the world to find a solution.

Google, Amazon, Facebook and Apple have faced intense criticism in various countries for not paying enough tax.

Scholz told CNBC that coming to an agreement on tax reforms to match the digital age remains a "global" problem.

Interestingly, France has introduced a 3% levy on the revenue of tech companies that earn more than €750 million worldwide each year with €25 million from within France. The UK has also proposed a 2% digital services tax on tech firms that make at least €500 million a year in global revenue.

annual turnover to register with the Customs Department and charge 6% service tax on these services to certain consumers.

Tax experts *The Edge* spoke to do not have any estimates as yet on how much the Malaysian authorities can collect from the digital tax.

Sunway University Business School economics professor Dr Yeah Kim Leng told *The Edge Financial Daily* that a tax rate of 6% could potentially yield about RM2.4 billion in digital tax revenue, based on the Statistics Department's survey that estimated Malaysia's e-commerce income at RM398 billion in 2015.

However, Deloitte's Senthuran



**Poon:** Income earned may not be territorial anymore for tax purposes. It could be borderless and taxed in many countries.



**Kishenjeet:** The potential impact for leakage of government revenues could increase exponentially over the next few years.

**Social media tax next?**  
Another rising digital trend likely to be on the radar screen of tax authorities is the use of social media as an income platform.

Kishenjeet Dhillon, manager of tax transfer pricing at Crowe

**“There continues to be this question of whether a digital tax should be an indirect tax or direct tax. Income earned may not be territorial anymore for tax purposes. It could be borderless and taxed in many countries.”**

*Poon Yew Hoe, Managing Partner, Crowe Malaysia*

**“Persons operating their businesses through online platforms, like Instagram, would hardly have a business presence in any particular country. Hence, greater questions need to be asked about how administrators can start to tackle the untaxed economy.”**

*Kishenjeet Dhillon, Tax Manager, Crowe Malaysia*



# Thank You

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