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Tax companies, not individuals on foreign-sourced income

Affected taxpayers may be eligible for relief against the Malaysian tax payable for foreign taxes suffered at source on the foreign income

by **NUR HANANI AZMAN**

THE government should consider directing the proposal to tax foreign source income (FSI) to corporates and not individuals as the cost of doing business will increase where FSI is remitted to Malaysia.

Effective Jan 1, 2022, a proposal to remove the tax exemption on income derived from foreign sources and received in Malaysia by Malaysian residents under Paragraph 28, Schedule 6 of the Income Tax Act 1967 was announced in the recent Budget 2022.

KPMG Malaysia ED Corporate Tax Nicholas Crist said Malaysia appears to be adopting a stance similar to that of Singapore's where FSI will be taxed only if it is received in Malaysia.

He said affected taxpayers may be eligible for relief against the Malaysian tax payable for foreign taxes suffered at source on the foreign income.

"What should be highlighted here is that this only applies to income. Capital gains that are not taxable in Malaysia will not be subject to tax. A transitional tax rate of 3% is accorded on the gross amount received in Malaysia from Jan 1, 2022, to June 30, 2022, and this is likely to encourage early remittance.

"Moving forward, where a taxpayer's foreign-sourced remittances consists of income that is both revenue and capital in nature, it would be crucial to identify and segregate the income in order for the appropriate tax treatment to be taken," he told *The Malaysian Reserve (TMR)*.

He said tax deductions should be available for expenses incurred in the production of FSI that is revenue in nature. Of particular significance is the interest expense on loans taken out to finance overseas investments which would now prima facie qualify for a tax deduction.

Malaysian Association of Tax Accountants deputy secretary general Dr Mohd Fairuz A Razak said if the FSI paid tax overseas, the Malaysian taxpayer should claim tax relief through the Double Tax Agreement (DTA) or unilateral tax credits. However, there are many complicated issues in this matter.

He said an example would be that although Malaysian dividends are not taxed, foreign dividends received in Malaysia will be subject to tax from 2022, therefore, there could be more than one level of taxation on foreign dividends.

"Similar complications could exist for interest income, rental income, business

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income and other income. The first hurdle to cross is determining whether the monies remitted into Malaysia are income or capital: Income is taxed while capital is not.

"Taxpayers will have difficulties dealing with this issue since the monies would have been accumulated over a long period. Unless you have good records, you may have a problem in arguing that the amount remitted is capital in nature," he told *TMR*.

Another example would be dividend income paid by Malaysian companies will not be taxable.

He said if income accumulated over many years is remitted into Malaysia, determining the amount of the tax paid overseas over the period can be tricky unless you have good records.

"There are special provisions in some DTA when you receive dividends that allow you an underlying tax credit. It is another area of complexity that needs to be understood by the taxpayer before a claim is made under Section 132.

"The removal of the exemption on FSI should create hitherto additional revenue to the government. It remains to be seen whether the benefits will outweigh the costs," he explained.

Mohd Fairuz said taxpayers with funds overseas may become understandably reluctant to repatriate funds back to Malaysia during a pandemic considering the various uncertainties, but whatever it is, let's wait for the Inland Revenue Board to give a guideline on the FSI.

"Our tax reforms must be in line with the country's overall economic and financial goals, especially in a time when the pandemic grievously hits international economies.

"Therefore, the Malaysian tax system should remain simple, easy to comply with and competitive to maintain its attractiveness for foreign investments and taxpayers' confidence," he said.

Ernst & Young Tax Consultants Sdn Bhd Malaysia tax markets leader Farah Rosley said the removal of tax exemption for FSI in the recently announced Budget 2022 might give a wrong signal to investors and will make the country less competitive.

She expressed worries that in the next six to seven weeks, there might be a lot of remittance happening from Malaysia because people don't want to be taxed.

"From what I am seeing, listening and reading, the removal of tax exemption for FSI will bring additional revenue of RM3 billion.

"However, is this extra billion worth the behaviour of making Malaysia a less attractive investment destination," she said during post-Budget 2022: Towards Recovery? organised by the Malaysian Institute of Economic Research recently.

Mohd Fairuz noted the number of Malaysians with digital nomads lifestyles is on the rise thanks to the pandemic. While digital nomads have freed themselves of commutes and water-cooler talk, their tax obligations remain — this is where the FSI comes in.

"We are moving leagues beyond the industrial revolution now. We have the privilege of restoring dignity to our co-workers. Our task is to restore choice and flexibility, accountability and trust.

"For different reasons, the pandemic had a good reason for Malaysians wanting to escape the current system they are in. However, digital hubs and work from home are here to stay for good with the new landscape of working culture in Malaysia."