

Malaysia: Introduction of capital gains tax on profits from disposal of capital assets

In brief

Since the publication of our client alert on tax highlights of the Malaysian Budget 2024, the Finance (No. 2) Act 2023 ("**Finance Act 2023**") has been passed by Malaysia's Parliament and gazetted into law on 29 December 2023. The Finance Act 2023 sets out the provisions, via amendments to the Income Tax Act 1967 ("**ITA**"), for implementing capital gains tax ("**CGT**") on gains or profits from the disposal of capital assets. These provisions are effective from 1 January 2024, but are subject to the Income Tax (Exemption) (No. 7) Order 2023 ("**Exemption Order**") which exempts a company, limited liability partnership, trust body or co-operative society ("**Chargeable Person**") from the payment of income tax in respect of any gains or profits received from the disposal of shares of a company incorporated in Malaysia not listed on the stock exchange made on or after 1 January 2024 to 29 February 2024.

In this alert, we examine the key provisions on CGT in the Finance Act 2023 and their implications for taxpayers.

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Key CGT provisions

Gains or profits from the disposal of a capital asset

The Finance Act 2023 amends the ITA by introducing a new Chapter 9, which subjects a Chargeable Person that receives gains or profits from the disposal of capital assets to CGT.

1. Definition of key terms

Term	Definition (as reproduced from the Finance Act 2023)
Capital asset	Means movable or immovable property, including any rights or interest thereof
Consideration	Means consideration of money or money's worth
Disposal	Means to sell, convey, transfer, assign, settle, or alienate whether by agreement or by force of law, and includes a reduction of share capital and purchase by a company of its own shares
Shares	Means all or any of the following: <ul style="list-style-type: none"> a. Stock and shares in a company. b. Loan stock and debentures issued by a company or any other corporate body incorporated in Malaysia. c. A member's interest in a company not limited by shares whether or not it has a share capital. d. Any option or other right in, over, or relating to shares as defined in paragraphs (a) to (c).

2. Types of gains or profits currently liable to CGT

The Finance Act 2023 amends Schedule 6 of the ITA to exempt all gains or profits from the "disposal of a capital asset situated in Malaysia" from CGT, except for gains or profits from:

- a. The disposal of unlisted shares of a company incorporated in Malaysia.

- b. The disposal of shares of a controlled company¹ incorporated outside Malaysia, which is deemed derived in Malaysia if the controlled company owns substantial² real property situated in Malaysia and/or shares in another controlled company owning substantial real property situated in Malaysia.

Pursuant to the Exemption Order, gains or profits from the disposal of unlisted shares of a company incorporated in Malaysia made on or after 1 January 2024 to 29 February 2024 are exempted from CGT. The Exemption Order does not apply where such gains or profits are considered as business income under Subsection 4(a) of the ITA.

Generally, gains or profits from the disposal of capital assets situated outside of Malaysia are **not** exempted under the ITA or the Exemption Order. Such gains or profits will be liable to CGT if the gains or profits are received in Malaysia. However, please note that gains or profits received from the disposal of shares of a controlled company incorporated outside Malaysia which owns substantial real property situated in Malaysia and/or shares in another controlled company owning substantial real property situated in Malaysia are **deemed to be derived in Malaysia** and therefore liable to CGT.

3. Calculation of adjusted income or loss

The adjusted income or loss of a Chargeable Person from a "source consisting of gains or profits from the disposal of a capital asset" is to be determined by:

- a. Taking the consideration for the disposal of the capital asset, reduced by:
 - i. Any "expenditure wholly and exclusively incurred on the capital asset at any time after its acquisition" by or on behalf of the Chargeable Person making the disposal for the "purpose of enhancing or preserving the value of the capital asset, being expenditure reflected in the state or nature of the capital asset at the time of the disposal".
 - ii. Any "expenditure wholly and exclusively incurred at any time after the acquisition of the capital asset" by the Chargeable Person to establish, preserve, or defend its title to, or to a right over, the capital asset.
 - iii. Incidental Costs (defined below) to the Chargeable Person of making the disposal.

("Net Disposal Consideration")

- b. Thereafter, by deducting the consideration for the acquisition of the capital asset (together with the Incidental Costs (defined below) to the Chargeable Person of the acquisition), less:
 - i. Any sum received by the Chargeable Person by way of "compensation for any kind of damage or injury to the asset or for the destruction or dissipation of the asset or for any depreciation or risk of depreciation of the asset."
 - ii. Any sum received by the Chargeable Person under a "policy of insurance for any kind of damage or injury to or the loss, destruction or depreciation of the asset."
 - iii. Any sum forfeited to the Chargeable Person as a "deposit made in connection with an intended transfer of the capital asset."

("Net Acquisition Consideration")

Incidental Costs are defined to mean "expenditure wholly and exclusively incurred" for the acquisition or disposal of a capital asset, as the case may be, including:

- a. Any "fees, commission or remuneration paid for the professional services of any valuer, accountant, agent or legal adviser".
- b. The costs of transfer, which include stamp duty.
- c. For an acquisition, advertising costs to find a seller.
- d. For disposal, advertising costs to find a buyer and costs that are reasonably incurred in making a valuation or determining the market value.

An adjusted income arises if the Net Disposal Consideration exceeds the Net Acquisition Consideration. Where the Net Disposal Consideration is less than the Net Acquisition Consideration, the resulting adjusted loss is allowed to be carried

¹ The meaning of a "controlled company" is provided in Section 139 of the ITA.

² For the purposes of this article, "substantial" refers to where the defined value of real property is not less than 75% of the value of a company's total tangible assets.

forward and used as a deduction to reduce the adjusted income of a Chargeable Person for subsequent disposals of capital assets for a period of 10 consecutive years of assessment.

4. Situations where consideration is deemed equal to market value or is to be determined by the Director General of Inland Revenue (DGIR)

a. Consideration deemed equal to market value

The consideration for the acquisition or disposal of a capital asset by the Chargeable Person is "deemed to be equal to the market value of the capital asset at the time of the disposal" in the following circumstances:

- i. An acquisition or disposal made "otherwise than by way of a bargain made at arm's length" and, in particular, one made "by way of gift."
- ii. An acquisition or disposal made "wholly or partly for a consideration that cannot be valued."
- iii. Acquisitions made as "trustee for the creditors of any person in full or part satisfaction of any debt due from that person" or where the Chargeable Person "transfers a capital asset as trustee for the creditors of any person to the creditors in full or part satisfaction of any debt due to the creditors."
- iv. The Chargeable Person "acquires or disposes of a capital asset in a transaction for the transfer of a business for a lump sum consideration."
- v. Where the capital asset disposal is a transaction that takes place between connected persons as defined by Section 65(E)(9) of the ITA.

b. Market value to be determined by the DGIR

The market value of a capital asset will be determined by the DGIR in the following circumstances:

- i. The parties are unable to agree on the market value of the capital asset being disposed.
- ii. Only one party exists to the capital asset disposal.
- iii. The DGIR is of the opinion that the market value as agreed on by the parties to the capital asset disposal is incorrect.

5. Date of disposal of a capital asset

The date of disposal of a capital asset depends on whether (a) there is a written agreement for the disposal and (b) the disposal or acquisition is subject to any regulatory approval.

a. Where a written agreement for the disposal exists

Where there is a written agreement for the disposal, the capital asset is deemed to be disposed on the date of such written agreement. In the absence of a written agreement, the capital asset is deemed to be disposed on the date of completion of the disposal.

The date of completion means either:

- i. The date on which the ownership of the capital asset is transferred by the person disposing of the capital asset ("**Disposer**").
- ii. The date on which the whole of the consideration for the capital asset has been received by the Disposer, whichever is earlier.

b. Where a disposal or acquisition is subject to regulatory approval(s)

Where the acquisition or disposal of a capital asset is subject to regulatory approval(s) by the government or a state government ("**Regulatory Approvals**"), the date of disposal of the capital asset is the date of obtaining such Regulatory Approvals. If the Regulatory Approvals are conditional, the date of disposal will be the date when "the last of all such conditions is satisfied."

6. Duty to provide details of the capital asset disposed and pay applicable CGT within 60 days

A Chargeable Person must provide to the DGIR a return in the prescribed form containing details of the capital asset within 60 days of the date of disposal of the capital asset. CGT on any chargeable income must be paid by the Chargeable Person within 60 days from the date of disposal of the capital asset.

7. Tax rate for disposal of capital asset

The disposal of capital assets situated in Malaysia by a Chargeable Person is subject to the following rates of income tax:

Acquisition date of capital asset	Tax rate
Before 1 January 2024	a. 10% of chargeable income; or b. 2% of gross disposal price.
On or after 1 January 2024	10% of chargeable income

Chargeable income from the disposal of capital assets situated outside of Malaysia are subject to the prevailing rate of tax. The prevailing rate of tax is currently 24%.

Derivation of gains or profits from the disposal of capital assets from real property in Malaysia

The Finance Act 2023 amends the ITA by introducing a new Section 15C of the ITA, which provides that "gains or profits accruing to a person in a year of assessment on the disposal of capital asset," which is a share of a controlled company incorporated outside Malaysia ("**Relevant Company**"), will be deemed to be derived from Malaysia where the Relevant Company owns:

- Substantial real property situated in Malaysia.
- Shares of another controlled company owning substantial real property situated in Malaysia ("**Real Property Company**").

For the purposes of determining the acquisition date of shares in a Relevant Company, Section 15C of the ITA provides that shares in a Relevant Company are deemed to be acquired:

- On such date that the defined value of real property and/or Real Property Company shares owned by the Relevant Company is at least 75% of its total tangible assets.
- On the date of acquisition of the shares of the Relevant Company.

Prior to the Finance Act 2023, Paragraph 34A, Schedule 2 of the Real Property Gains Tax Act 1976 ("**RPGTA**") deems an acquisition or disposal of shares in a real property company to be an acquisition or disposal of a chargeable asset liable to real property gains tax. The Finance Act 2023 amends the RPGTA to provide that, on or after 1 January 2024, Paragraph 34A, Schedule 2 of the RPGTA will no longer apply to an acquisition or disposal of shares in real property companies by a Chargeable Person, other than a Labuan entity as provided under Section 2B of the Labuan Business Activity Tax Act 1990.

Key implications

The implementation of CGT will result in the following implications for taxpayers:

- Effective 1 January 2024, profits or gains from the disposal of capital assets **situated in Malaysia** by a Chargeable Person will, depending on the acquisition date, be subject to tax at 10% of chargeable income or 2% of gross disposal price. Notwithstanding the above, save where profits or gains from the disposal of unlisted shares of a company incorporated in Malaysia are considered as business income under Subsection 4(a) of the ITA, the Exemption Order exempts a Chargeable Person from the payment of CGT in respect of such profits or gains made on or after 1 January 2024 to 29 February 2024.
- Gains or profits from the disposal of capital assets situated outside of Malaysia are not exempted under the ITA or the Exemption Order. Such gains or profits will be liable to CGT if the gains or profits are received in Malaysia. However, please note that gains or profits received from the disposal of shares of a controlled company incorporated outside Malaysia which owns substantial real property situated in Malaysia and/or shares in another controlled company owning substantial real property situated in Malaysia are **deemed to be derived in Malaysia** and therefore liable to CGT.
- Although exemptions to CGT for the disposal of shares for the purposes of internal group restructurings, initial capital offerings on Bursa Malaysia, and venture capital investments had been announced in the Malaysian Budget 2024, such exemptions are not provided for in the Finance Act 2023. It is expected that the exemptions, if any, and further guidance to interpret some of the proposed provisions in the Finance Act 2023 will be separately introduced via subsidiary legislations and guidelines issued by the Inland Revenue Board.

- Generally, the consideration for disposal of a capital asset can be freely agreed between the parties to a disposal. However, in certain circumstances, the consideration for the acquisition or disposal of a capital asset will be deemed to be equal to the market value of the capital asset at the time of the disposal as assessed by a valuer. In any case, the DGIR has the inherent power to determine the market value of a capital asset if the DGIR is of the opinion that the value of a capital asset as agreed upon by the parties to the disposal is incorrect.
- The date of disposal of a capital asset depends on whether or not there is a written agreement for the disposal and if the disposal or acquisition is subject to any regulatory approvals. Where there is a written agreement for the disposal, the capital asset is deemed to be disposed on the date of such written agreement. Where the acquisition or disposal of a capital asset is subject to regulatory approvals by the government or a state government, the date of disposal of the capital asset is the date of obtaining such regulatory approvals (or the date when all conditions are satisfied if the regulatory approvals are conditional).
- A Chargeable Person must furnish to the DGIR a return in the prescribed form containing details of the capital asset within 60 days from the date of disposal of the capital asset. CGT on any chargeable income must also be paid by the Chargeable Person within 60 days from the date of disposal of the capital asset. A failure to furnish a return in the prescribed form and to furnish the correct particulars as required by the DGIR is an offense that will, on conviction, result in a fine and/or imprisonment.
- Gains or profits accruing to a person in a year of assessment on the disposal of a capital asset which is a share of a controlled company incorporated outside Malaysia, will be deemed to be derived from Malaysia and subject to CGT, where the company owns substantial real property situated in Malaysia and/or shares of another controlled company owning substantial real property situated in Malaysia. In line with this, the RPGTA has been amended to clarify that acquisitions or disposals of shares in real property companies by a Chargeable Person will no longer be subject to real property gains tax. When this amendment to the RPGTA and the Exemption Order are considered in parallel, it would appear that gains or profits received from the disposal of unlisted shares of a real property company incorporated in Malaysia in the period beginning 1 January 2024 and ending 29 February 2024 are subject to neither real property gains tax or capital gains tax.

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