More exemptions needed for widened SST scope, say tax consultants, businesses

BY **ESTHER LEE**

The widened scope of the sales and service tax (SST) signifies one of the moves the government is making to broaden the tax base shore up the country's fiscal position.

Under the wider scope of the sales tax, it is estimated that over 3,000 categories of goods, based on tariff codes that were previously exempted from sales tax, will be subject to a tax of 5% from July 1. Meanwhile, the widened scope of service tax means that several previously exempted sectors have been added to the fold.

A comparison of the list of taxable goods and services under the previous goods and services tax (GST) regime against the expanded list of taxable goods and services under the widened scope of the SST, shows that the gap between the two has narrowed, says Deloitte Malaysia indirect tax leader Tan Eng Yew.

Nevertheless, tax experts point out that the two tax regimes are structurally very different, so a direct comparison is not entirely straightforward. While the GST was a comprehensive multi-stage tax that encompassed a wide range of goods and services across the supply chain, the SST presents a more limited tax base, with a tax on certain manufactured and imported goods and prescribed services.

"The recent SST expansion reflects the government's aim to broaden the tax base in a more targeted and progressive manner, without placing undue burden on the rakyat," says KPMG Malaysia head of indirect tax Ng Sue Lynn.

However, the inherent weakness of the SST remains — this being the cascading effect of the tax system because of the absence of credit for tax paid in previous stages of the supply chain — which means costs could trickle down to the consumer.

The government has tried to remedy the situation and provided business-to-business (B2B) exemptions for the service tax on certain services, upon certain criteria being met.

Does this help to mitigate the cascading effect of the tax?

Yes, to a certain extent, say tax consultants. But the present exemptions for businesses do not entirely eliminate the cascading effect because its scope of exemption is not as broad as in the GST environment. The cascading effect tends to result in rising costs of doing business.

EY Asean tax leader Amarjeet Singh says the current scope of exemptions provided to businesses have inherent limitations and certain businesses may not be able to utilise these exemptions due to their business arrangements.

"It is good that the government has initiated exemptions, but it's not broad enough to mitigate the cascading effects. There is a need to review the current B2B exemptions and where gaps are identified, the government should consider further enhancements to the exemptions. Businesses need to be competitive. If the SST creates a significant increase in cost to businesses [because of the cascading effect], it will affect the cost of doing business. But of course, competitiveness isn't just caused by taxes," he explains.

While the SST primarily targets manufacturers and prescribed services, says PwC Malaysia indirect tax director Annie Thomas, taxable goods and services that are not exempted may still encounter some cascading effect if involved in multiple transactions.

"For businesses to fully capitalise on the mitigating provisions of the SST, understanding industry-specific exemptions is crucial, and consulting with tax authorities or advisors is often necessary to effectively navigate the complexities of the tax regime," she says.

Steel industry facing challenges on several fronts

The Malaysian Iron and Steel Industry Federation (Misif) is one of many industries that are feeling the heat of the expanded SST scope. In a June 13 press statement, it said the industry was already struggling with low utilisation rate at around 39% amid overcapacity in the region. The upcoming SST expansion will subject previously exempted items to tax, including coking coal and coke (5%), steel components (5% to 10%), steel scrap (5%) and industrial machinery (10%), on top of the 8% on services like rental or leasing services, it added.

"For instance, with the 5% sales tax on scrap, the entire supply chain bears the cost. When a scrap dealer purchases scrap with 5% sales tax, that additional burden is not absorbed — it is passed on to steel mills. As the industry faces rising input costs, their margins tighten and they are either forced to raise prices or absorb losses, undermining their competitiveness," it explained, adding that the industry was already facing various challenges such as the upcoming carbon tax on iron and steel in 2026 and the US tariff on steel.

"A key concern is the inconsistent treatment of goods under Chapters 72 and 73 of the Customs Tariff, which respectively cover upstream and downstream steel products. For example, previously exempted essential steel materials, steel wire mesh are now suddenly subject to a 10% sales tax, while stainless steel and even perforated cable trays have been unexpectedly slapped with a 5% sales tax — all without a clear rationale. This sudden shift raises input costs unpredictably and adds needless complexity to manufacturing operations, exactly when the industry needs stability and transparency most," Misif's statement reads.

Deloitte's Tan suggests that perhaps in the coming days, the government can consider broadening the B2B relief to better cushion the impact of the expansion.

Notably, Minister of Finance II Datuk Seri Amir Hamzah Azizan tells *The Edge* in an interview that the door to potentially introduce more exemptions in the future is still open. He says the government is practical.

"If we find that over time, there are still challenges, we are open to explore. But for the moment, the threshold that we set is reasonable enough to manage the impact for where we have parked things," he adds.

"So similar to the e-invoicing [where we delayed the implementation for businesses with below RM500,000 in annual sales], we will look at it [more B2B exemptions]. But it must be backed by substance and data."

Businesses have also been voicing their concerns about the lack of clarity and guidance when it comes to the widened SST scope.

"Businesses often feel the need for more detailed information and clearer communication regarding SST policies and exemptions. A related concern involves uncertainty about which goods and services are subject to SST and whether they fall within exemptions or taxable categories," says PwC's Thomas.

KPMG's Ng also hopes for greater clarity and guidance from the authorities, including practical examples that would help to support better compliance. She says that, ultimately, certainty and ease of application will help provide greater confidence to taxpayers.

There have been calls from various industries subjected to the wider service tax for the government to defer or lower the tax rate, given its wider scope now. Businesses say they feel the cost pressures which have intensified in recent times, with the rising minimum wage, electricity tariff and now the expanded SST.

Can the government lower the tax rate?

If the aim is to reduce the deficit and improve the country's fiscal position, some think that it would be difficult to do so.

Amarjeet highlights that the SST collected-to-GDP (gross domestic product) ratio in 2024, before the current expanded scope, stood at 2%. Whereas, under the GST regime that was implemented from 2015 to 2018, the GST collected-to-GDP ratio stood at 3% in the year with the highest GST collection.

"This is an indication that — without taking into account the SST expansion —we're not there yet in terms of matching the GST potential. This is because certain categories are not captrured under SST, for example, IP rights and licensing fees, commercial property sales and others. This just means the government cannot afford to tax at a lower rate of tax at this juncture if the objective is to achieve a better fiscal position," he says.

Others have highlighted the issue of the limited time frame for implementation and compliance. While many are willing and ready to comply, the compressed timeline poses practical challenges in updating systems, training staff and understanding the revised scope, says KPMG's Ng.

Nonetheless, she commends the government for having engaged with the relevant associations and affected industries before the announcement to gather feedback, and hopes that the open and candid consultations will continue to address any implementation issues.

Amir Hamzah disagrees that the time given is insufficient, saying that SST is not a new system to businesses, that it is a mechanism already in place.

"The sales and service tax is already in place. If you are in the system, you're already paying, maybe only a new category will be added. It doesn't take anything to change. We are giving businesses the next couple of months to register if they are above the threshold. We have also said in the press statement that in the first six months of the rollout, enforcement is not going to be with penalties," he says.

"We'll be practical about it. But we want to see you try and start doing something about it." E