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UPDATE OF EXIT TAX

On 1 September 1998, Bank Negara Malaysia ("BNM") imposed new capital controls with a one year freeze on the repatriation of foreign funds and set its currency at a fixed exchange rate. On 3 October 1998, we conducted a seminar on Malaysian New Exchange Control Measures for an overview, accounting and tax impacts of the new capital controls.

The Malaysia government imposed exit levies with effect from 15 February 1999 to replace the one year freeze on repatriating foreign funds. We have introduced the Exit Tax in our ISSUE 8 of Around Us.

On 1 September 1999, exactly one year after Malaysia imposed the new capital controls, a total of US$328 million or 1.2 billion Malaysian ringgit of foreign funds left Malaysia. BNM described the outflow as “small” after releasing the figures on the first day that taxes were removed on principal sums brought into Malaysia prior to capital controls. However, the outflows still wiped out a third of the 3.6 billion Malaysian ringgit inflows since the capital controls were eased and replaced by the exit tax system on 15 February 1999. Since the start of September 1999 to 21 September 1999, it was reported that about US$800 million worth of foreign funds have left Malaysia.

On 21 September 1999, the Malaysia government announced a new policy that a flat 10 per cent rate will replace a two-tier levy (exit tax) system on foreign capital gains on stock investments to further relax the capital controls imposed on 1 September 1998.

BNM’s decision to replace the unpopular two-tier levy system was made in response to appeals from foreign fund managers. According to Bank Negara statement, the new policy will help to ease the administration of the levy system. It will also ease the two external accounts (normal External Account and Special External Account) to be merged into one. To ease the merger of these two accounts, foreign funds that were brought in between 1 September 1998 and 14 February 1999 will be treated as funds that have been brought into Malaysia since 1 September 1998. Therefore, there will not be any levy on the principal amount. Profits from funds brought in on or after 15 February 1999 are subject to a flat 10 per cent levy irrespective of when the profits are repatriated.

According to the Malaysia government officials, relaxation of the capital controls was also prompted by the brighter economic outlook and the low outflow of foreign funds reported at the end of the one year freeze on repatriating foreign funds.

While Malaysia has removed a major pillar (exit tax) of its capital controls, analysts said the other main pillar (the pegging of the ringgit to US dollar at RM3.80) is expected to remain in place for sometime.

Rolling back the controls

From moratorium to 10% tax

September 1998

Foreign fund managers barred from repatriating investments for one year as part of Malaysia's capital controls.

February 1999

Moratorium scrapped and replaced by a two-tier tax.

- Funds brought into the country before February this year are subject to a staggered levy on the principal amount. The levy ranges from 30% to zero in September this year.

- Funds invested in the stock market after February this year are subject to a levy on the profits upon repatriation. 30% is applied if profits are repatriated within one year and 10% thereafter.

September 1999

- Flat levy 10% on profits replaces two-tier tax.

Source: The Business Times, 22 September 1999

References

(1) The Business Times, 2 September 1999 & 22 September 1999.
(2) The Straits Times, 22 September 1999.