

16/09/2003

Govt displays fiscal prudence, focuses on reducing deficit

Khoo Chuan Keat; Sharon Armstrong

CONTRARY to rife pre-Budget speculations that Prime Minister and Finance Minister Datuk Seri Dr Mahathir Mohamad will dish out a bagful of pre-election goodies before his retirement next month, the Government has exercised fiscal prudence in formulating Budget 2004.

While dangling some carrots for businesses and the "rakyat", Budget 2004

is focused on reducing the country's deficit of 5.4 per cent in 2003.

Growth is expected to emanate from the domestic sector as well as riding

the prospects of gradual global economic recovery.

Combining pragmatic macroeconomic management and the pro-growth measures

announced under the Economic Stimulus Package in May this year, Budget 2004 is aimed at enhancing Malaysia's economic resilience against potential external de-stabilisers and strengthening economic growth.

Given our vulnerability in the uncertain global economic landscape, it makes sense that the economic strategy should be domestic-led with the private sector resuming its role in spearheading the engine of economic growth while seeking new export markets in the quest to be a "truly trading nation".

Promoting investments by small- and medium-enterprises (SMEs)

In pursuit of a domestic-led economy, several financial and fiscal measures have been proposed to strengthen the resilience and improve the competitiveness of our local industries particularly SMEs.

The proposal to increase the threshold for chargeable income of SME which is subject to corporate tax at the concessionary rate of 20 per cent

will mean a saving of up to RM40,000 which can be reinvested in expanding

capacity, improving productivity and efficiency, and upgrading quality of

our products.

Encouraging Reinvestment Activities

Carrots are also being dangled in the form of Pioneer Status with tax exemption or Investment Tax Allowance for domestic companies:

- * to reinvest in the production of heavy machinery;
- * to reinvest in the production of machinery and equipment, including specialised machinery and equipment and machine tools;
- * to produce or reinvest in producing value added products using oil palm biomass;
- * engaged in hotels and tourism projects to invest in expansion, modernisation and renovation;
- * to reinvest in providing cold chain facilities and services for perishable agricultural produce.

It should be noted that the tax exemption under Pioneer Status is only given on the increased statutory income arising from reinvestment and Investment Tax Allowance on additional qualifying capital expenditure incurred within a period of five years on reinvestment in the production

of heavy machinery, production of machinery and equipment, and production of value added products using oil palm biomass.

Increasing foreign direct investments by promoting the services sector

The manufacturing sector has been and is still a major contributor to economic growth. However, recent Budgets have seen a shift in the Government's focus to the services sector to attract foreign direct investments.

The proposal to exempt from tax income derived by Operational Headquarters (OHQ) from the provision of qualifying services to its related companies in Malaysia subject to a cap of 20 per cent will hopefully encourage the establishment of more OHQs in the country as the taxability of income from the provision of qualifying services to its related companies locally has been a deterrent for foreign multinational companies to locate their OHQs in Malaysia.

In seeking to attract investors from countries practising Syariah principles to establish offshore companies in Labuan, it has been proposed

that an income tax rebate equivalent to the amount of tithe the paid to the Labuan religious authority be given subject to a maximum of 3 per cent of net profit or RM20,000.

Enhancing cost competitiveness

In order to retain our position as the 17th largest trading nation in the world, we need to remain cost competitive particularly in the wake of globalisation and emerging economies with lower cost structures.

While the Government can only encourage and provide incentives to companies to improve productivity and efficiency, it should not itself implement policies that directly or indirectly add to the cost of doing business.

One of the major issues in contention in the past is the disallowance of legitimate business entertainment expenses and the extended definition of hospitality adopted by the tax authorities.

By so doing, it fails recognise the realities of business conduct. It is therefore heartening that after prolonged lobbies by relevant bodies that entertainment expenses incurred on sales promotions will be fully deductible and other business entertainment expenses be given 50 per cent deduction, although this category in itself will no doubt be subject to wide interpretation.

Expanding the capital market

A strong financial services industry with ample liquidity is required to support the private sector in driving the nation's economic growth.

Recognising this need, the Government has proposed specific measures to promote the development of private venture capital companies, and the use of asset-backed securities and Islamic financing instruments to augment

the capital markets.

Budget 2004 together with the Economic Stimulus Package have laid down the blueprint for the nation's continued economic recovery in these challenging times.

The success of these strategies now rests squarely on the response by the private sector to heed this call for action.

The writers are PricewaterhouseCoopers Taxation Services executive director Khoo Chuan Keat and managing consultant Sharon Armstrong