



ROYAL MALAYSIAN CUSTOMS

GOODS AND SERVICES TAX

**GUIDE
ON
CONSTRUCTION
INDUSTRY**

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INTRODUCTION

1. This industry guide is prepared to assist businesses in understanding matters with regards to GST treatment on Construction Industry. This Guide covers all contractors including self-employed individuals, partners, companies, local authorities and anyone carrying on a business which includes construction operations.

Overview of Goods and Services Tax (GST)

2. Goods and Services Tax (GST) is a multi-stage tax on domestic consumption. GST is charged on all taxable supplies of goods and services in Malaysia except those specifically exempted. GST is also charged on importation of goods and services into Malaysia.

3. Payment of tax is made in stages by the intermediaries in the production and distribution process. Although the tax would be paid throughout the production and distribution chain, only the value added at each stage is taxed thus avoiding double taxation.

4. In Malaysia, a person who is registered under the Goods and Services Tax Act 2014 is known as a “registered person”. A registered person is required to charge GST (output tax) on his taxable supply of goods and services made to his customers. He is allowed to claim back any GST incurred on his purchases (input tax) which are inputs to his business. Therefore, the tax itself is not a cost to the intermediaries and does not appear as an expense item in their financial statements.

GENERAL OPERATION OF THE INDUSTRY

5. The key players involved in the construction industry are:

(a) Developer

Acquires land and engages contractors to construct building or structure on the land;

(b) Main Contractor



Engaged by the developer to carry out the construction and he takes full responsibility for the completion of the construction project.

(c) Subcontractor

Engaged by the main contractor to perform portions of the main contractor's work. Subcontractors include specialists such as plumbers, electricians, painters and bricklayers.

6. Normally, the construction industry will include activities such as to build new structures, modifications, maintenance, repair, alteration, renovation, dismantling, removal, demolition and improvements on these structures. It includes any works which form an integral part of, or are preparatory for the works mentioned, including site clearance, soil investigation and improvement, earth moving, excavation, laying of foundation, site restoration and landscaping.

7. The construction industry involves main contractors and sub-contractors of the following category:

- (a) Building or general contractors who are involved in the construction of residential, commercial, industrial and other buildings;
- (b) Heavy and civil engineering construction contractors who are involved in constructing roads, highways, tunnels, bridges, sewers and other projects; and
- (c) Special trade contractors who perform other specialized activities related to construction such as carpentry, plumbing, electrical, painting and others.

8. All construction services performed in Malaysia are subject to GST. Hence, a contractor who is the registered person has to charge GST on the supply of construction services, whether in relation to residential and non-residential properties, in Malaysia.

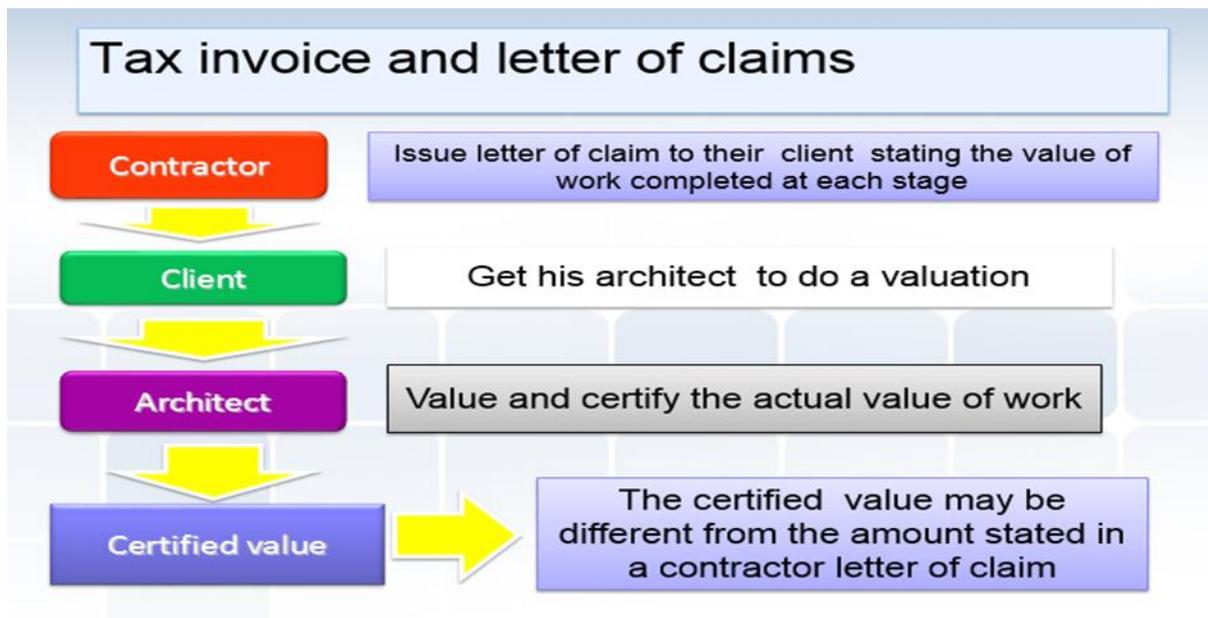
Time of Supply.

9. The time of supply is the time at which supplies made by the provider of the construction services is treated as having taken place. However, the rules under



regulation 11 of GST Regulations 2014 will determine when output tax is to be accounted on any considerations received. The issuance of an invoice will trigger the time of supply of services made by the contractors. The tax invoice issued by the provider of the construction services or any certificate in relation to any work done (in the case where the tax invoice has not be issued within 21 days after such certificate be issued and no payment received) issued by the authorized person, such documents will serve as bill for payment for the services provided if it contains the prescribed particulars as required under section 33 of the ACT. Please refer to the *GST Guide on Tax Invoice and Record Keeping* for further details.

Tax Invoices and Letter of Claim



10. The illustration above shows the relationship between letter of claim and the tax invoice.

11. The contractors issue invoices or letters of claim which will serve as a bill for payment to their developers stating the value of work completed at each stage of the construction. The developer will then have either his architect or engineer as the authorized person to do a valuation and certify the actual value of work done. This certified amount by the authorized person is usually different from the amount stated in the invoices or letter of claim issued by the contractor.

12. Such invoices or letter of claim cannot be treated as a tax invoice as required under section 33 of the GST ACT, as it does not contain the final amount payable by the developer. A contractor who is the registered person should issue a tax invoice to his customer upon certification by the authorized person. He has also to keep the certificate in relation to any work done issued by the architect together with his tax invoices to support the value invoiced to the developer as their client.

Progress payment

13. Progress payments mean amounts billed for work performed on properties sold in respect of property development activities, whether or not they have been paid. They may also be known as progressive payments. This method of payment is a schedule of when (according to project milestones or specified dates) contractors will be paid for the current progress of installed work.

14. It is common for contractors to invoice their customer's progress payments monthly or at regular intervals, for the construction services performed. A contractor who is the registered person shall account for GST according to regulation 11 of GST Regulations 2014. This is only applicable to the work of the main contractors and sub-contractors who are providing construction services (including construction, alteration, demolition, repair or maintenance of a building or any engineering work) which span a period of time and payment is determined or received periodically.

Retention Amount

15. Most construction contracts have a provision for the retention of an amount (known as "retention sum") due to the contractor. Retention amount is the amount of progress payment which is not paid until the conditions specified in the contract for the payment of such amounts have been met or until defects have been rectified.

16. Construction contracts provide for a contractor to render progress payments as work on a contract progresses where the contractor will be paid, usually after the relevant part of the work has been satisfactorily completed, as certified. Such contract allows the developer to withhold a percentage from the payment of each progress payment pending satisfactory completion of the entire contract. This retention amount is a specified amount withheld at each stage of progress payment, and will only be



released to the contractor when the customer is satisfied with the work performed. Usually, retention sums are released only after the construction project has been completed.

17. For retention amount, a supply shall be treated as taking place when a payment in respect of such amount is received or a tax invoice for such retention amount is issued by the contractor, whichever is the earlier.

Liquidated Damages

18. Schedule G and H of Housing Development (Control And Licensing) Regulations 1989 requires a property developer to complete and deliver the property to the house purchaser within 24 calendar months (36 months for condominiums) and if the developer fails to deliver such property within such stipulated time, he is liable to pay to the purchaser a sum (10%) calculated at a rate specified in the sales and purchase agreement as liquidated damages (LAD) until the purchaser takes vacant possession of such building. Hence, the construction contract normally stipulates that the contractor is required to deliver the completed construction work within the period stipulated in the construction contract. Failure to deliver the completed construction work within the stipulated time will result in such contractors being liable to pay the client liquidated damages for the period during which the relevant works remain incomplete.

Rectification of defect

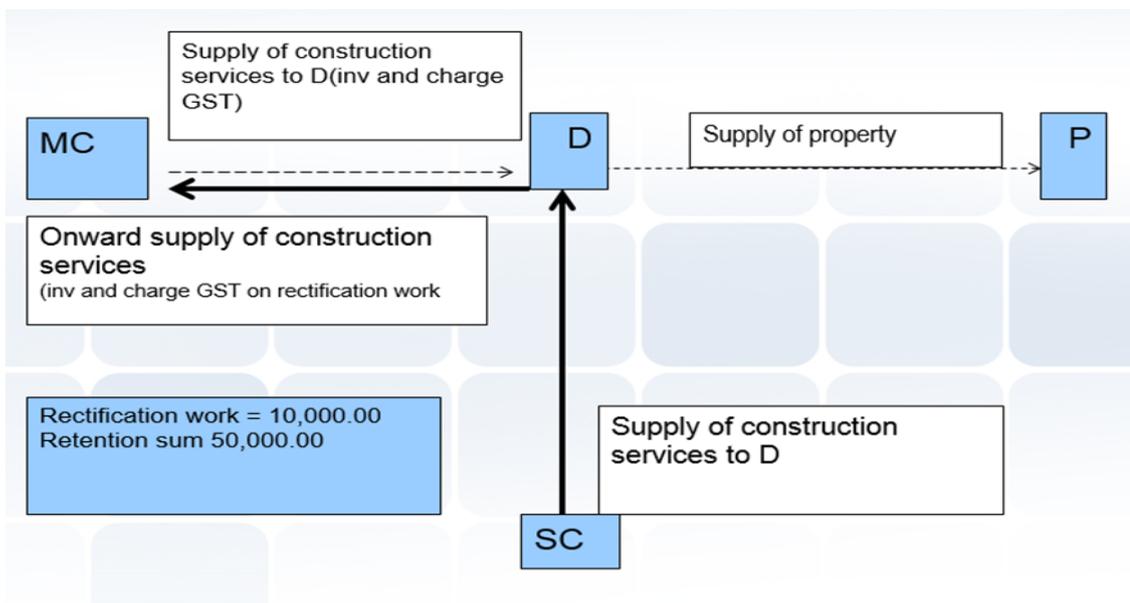
19. Rectification of defect is one of the provisions in the construction contract. It is allowed even after the issuance of Certificate of Compliance and Completeness (CCC) and the purchasers will take possession of the properties, if there may be defects in the new units that need rectification. Such contract stipulates that the main contractor is required to carry out such rectification works during the defect liability period. Hence, such rectification of defect are compensatory in nature, and cannot be treated as taxable supplies.

20. However, if the main contractor fails to rectify this defect and another contractor is hired by developer to rectify the poor workmanship done by the main contractor resulting an additional cost being incurred. GST treatment is as follows:-

- (i) if the main contractor does not perform the rectification works, the developer may engage another contractor to do the job and subsequently deduct such costs from any payment due to the main contractor.

Illustration 1

The developer ("D") hires another sub-contractor ("SC") to do the rectification. As such, the sub-contractor ("SC") is supplying his construction service to ("D"). If the sub-contractor ("SC") is registered for GST, he has to charge ("D") GST on the rectification works performed. ("D") then supply of the construction services onwards to the main contractor ("MC"). ("D") has to charge "MC" GST on the said works.



- (ii) At times, the purchaser may engage his own contractor to do the rectification and claim compensation for the costs or deduct the amount from any payment due to the developer. The developer in turn deducts such amount from any payment due to the main contractor. In either situation, the developer is making a supply of rectification works to the main contractor. The developer has to charge and account for GST on the amount he has claimed or deducted from the main contractor.

Illustration 2

If the purchaser ("P") hires his own sub-contractor ("SC") to rectify the defects, there is a supply from the purchaser ("P") to the developer ("D") because the purchaser ("P") is making good the defects that should have been done by the developer ("D"). If the purchaser ("P") is registered for GST, he has to charge the developer ("D") GST on the cost of the rectification works carried out by his subcontractor ("SC"). "D" will in turn onward supply this construction service to the main contractor ("MC") and charge him GST accordingly. Please refer to Q26 for details.

FREQUENTLY ASKED QUESTIONS

Registration

Q1. Who is liable to be registered?

A1. All contractors and subcontractors in the construction industry, whether they are companies, partnerships or self-employed individuals are liable to be registered if their annual turnover involving taxable supplies exceeds the prescribed GST threshold in the past 12 months or within the future 12 months.

Q2. If my annual turnover of taxable supplies does not exceed the GST threshold, can I apply to be registered?

A2. You may apply for voluntary registration, but once registered you must remain registered for a minimum of two years.

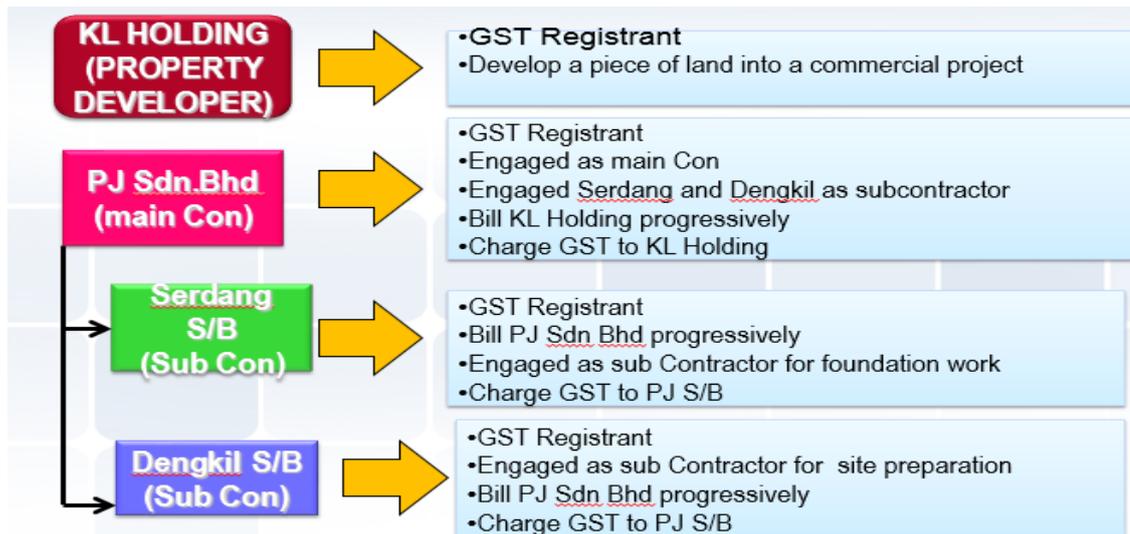
Taxable Supplies

Q3. What supplies are subject to GST in the construction industry?

A3. All types of construction services including construction of residential houses or agricultural buildings are subject to GST. This is because **construction services are standard rated** and it does not matter that residential houses are exempt.

The illustration below shows the supply of the construction services;





Example 1

A property developer, KL Holding acquired a piece of land in Kuala Lumpur to be developed into commercial properties. He engaged a main contractor, PJ Sdn. Bhd. to be fully in charge of the project. As the main contractor, PJ Sdn. Bhd. engaged subcontractor Dengkil Sdn. Bhd. for site preparation work and subcontractor Serdang Sdn. Bhd. for foundation work on such project.

Dengkil Sdn. Bhd. and Serdang Sdn. Bhd. as the subcontractors billed PJ Sdn. Bhd. progressively for their work done. As both are registered under GST Act, they will have to charge GST on the amounts billed to PJ Sdn. Bhd. for the work performed.

PJ Sdn. Bhd. bills KL Holdings progressively for the work done for the whole project. Upon certification by KL Holding's architect, PJ Sdn. Bhd. will bill KL Holdings for the agreed amount of work done. GST is chargeable on all these amounts if PJ Sdn. Bhd. is a person registered under section 20 of GST Act.

Q4. What charges are subject to GST in the construction industry?

A4. The charges which are subjected to GST include the value of all works and materials permanently incorporated in or affixed on the site of the building or construction project, and any other movable goods that the contractor may charge to the customer.

Example 2

KLM Sdn. Bhd. awarded a contract to DEF Construction Sdn. Bhd. to build a commercial building. Under the contract agreement, the value of construction services including value of materials and work done is RM60,000.

The total amount of GST chargeable is RM3,600 (RM60,000 X 6%).

However, if the contractor gives to the customer movable furniture and charge him separately over and above the amount contracted above, this charge is also subject to GST. If he charges the customer RM2,000, he also has to charge GST of RM120 (RM2,000 X 6%).

Time of Supply and Accounting Period

Q5. When do I have to account for GST?

A5. Your account for GST is based on the two situations:

- (a) Where the construction work does not involve the issuance of a certificate in relation to any work done, you have to account for GST at the earlier of the following:
 - (i) when a tax invoice is issued; or
 - (ii) when a payment (wholly in money) is received by you.

- (b) Where the construction work involves the issuance of a certificate in relation to any work done, you have to account for GST at the earlier of the following:
 - (i) when a tax invoice is issued;
 - (ii) when a payment (wholly in money) is received by you; or
 - (iii) when the certificate in relation to any work done is issued, if no tax invoice has been issued within 21 days after the certificate in relation to any work done is issued.

Example 3

In cases which do not involve issuance of certificate in relation to any work done and assuming you are on a monthly taxable period, if you

issue a tax invoice on 15th June, you have to account for GST in your June GST return. However, if you issue a tax invoice on 3rd August, you have to account for GST in your August GST return.

In cases which involve the issuance of certificate in relation to any work done, if such certificate was issued on 12th June, and the invoice was issued after 21 days, that is on 9th July, the GST has to be accounted in your June GST return. However, if the invoice was issued on 2nd July (within 21 days from the date of issuance of certificate of work done), the GST will be accounted in your July GST return.

Q6. When do I have to submit GST payment to Customs?

A6. On or before the last day of the month subsequent to the taxable period.

Example 4

Based on the above example, if you are on a one month taxable period, the last date to submit the June GST return is the last day of July. The last day to submit the July GST returns is the last day of August.

Place of Supply

Q7. If I have a construction business registered outside Malaysia, do I have to account for GST?

A7. No. If the business is registered outside Malaysia, the supplies are considered as out of scope.

Example 5

X, a foreign contractor registered outside Malaysia provides construction services in Singapore. The supplies provided by X are regarded as out of scope and is not subject to Malaysian GST.

Q8. If a contractor provides construction services on the islands of Langkawi, Tioman or Labuan, has he to account for GST?

A8. No, construction services provided within or between these islands are not subject to GST. These islands are called designated area. Even though these supplies are treated as no tax chargeable, the contractor can claim input tax

incurred in providing construction services in the designated area. However, GST shall be charged on taxable supply of construction services made by the contractor from a designated area to Malaysia or on construction services supplied by any contractor from Malaysia to a designated area.

Q9. If I am registered in Malaysia and provide construction services outside Malaysia, is the supply subject to GST?

A9. Yes, this type of supply is a taxable supply but it is zero rated. You charge your customer GST at zero rate, and you are eligible to claim input tax for all supplies related to such construction services.

Example 6

Y, a local contractor provides contract works outside Malaysia. The value of the contract works is RM100,000. The GST to be charged is zero. In the course of providing the above the contract works, Y incurred input tax in the form of materials to be used or incorporated into the contract works. The value of the materials is RM50,000 and the GST incurred was RM3,000 (RM50,000 X 6%). Y is eligible to claim the RM3,000 as his input tax.

Progress Payment

Q10. When and how do I account for GST for progressive payment contracts which involve the issuance of certificate in relation to any work done?

A10. GST has to be accounted for after the end of each successive progressive payment schedule and after you received the certificate in relation to any work done (progress certificate) from the architect, engineer or surveyor who values the amount of construction work done. You have to account for GST either based on payment received, tax invoice issued or certificate in relation to any work done be issued. The time to account for GST is at the earlier of the following:

- (a) when payment is received;
- (b) when tax invoice is issued;

- (c) when the certificate in relation to any work done is issued, if no tax invoice has been issued within 21 days after the certificate of work done is issued.

Example 7

A contractor AB Sdn. Bhd. enters into a construction contract to construct a project for BC Sdn. Bhd.. Such construction contract entered by both parties allows BC Sdn. Bhd. to withhold 5% from the payment of each progress billings pending satisfactory completion of the entire contract as a retention sum. It also stipulates that the work is scheduled for 4 successive intervals and the estimated value of the contract work is as follows:

Date of claim	Estimated value by contractor
1 st interval (31 March 2016)	RM40,000.00
2 nd interval (30 June 2016)	RM100,000.00
3 rd interval (30 Sept 2016)	RM160,000.00
4 th interval (31 Dec 2016)	RM300,000.00

AB Sdn. Bhd. issues the letter of claim for the respective date and amounts as above.

The architect issues such progress certificate after each interval period as follows:

Progress Payment - 1st interim certificate

Value of material and works = RM30,000.00

Less: Retention sum (RM30,000 X 5%) (RM1,500.00)

Amount Paid RM28,500.00

Progress Payment – 2nd interim certificate

Value of material and works = RM90,000.00

Less: Retention sum (RM90,000 X 5%) (RM4,500.00)

Less: 1st interim certificate (RM28,500.00)

Amount Paid **RM57,000.00**

Progress Payment – 3rd interim certificate

Value of material and works	=	RM150,000.00
Less: Retention sum (RM150,000 X 5%)		(RM7,500.00)
Less: 1st interim certificate		(RM28,500.00)
2nd interim certificate		(RM57,000.00)

Amount Paid **RM57,000.00**

Progress Payment – 4th interim certificate

Value of material and works	=	RM300,000.00
Less: Retention sum (RM300,000 X 5%)		(RM15,000.00)
Less: 1st interim certificate		(RM28,500.00)
2nd interim certificate		(RM57,000.00)
3rd interim certificate		(RM57,000.00)

Amount Paid **RM142,500.00**

The contractor, AB Sdn. Bhd. received the respective amounts as follows and has to account GST accordingly:

1st interval

Payment received	=	RM28,500.00
Invoiced issued		12 April 2016
GST (RM28,500.00 X 6%)		RM1,710.00

2nd interval

Payment received	=	RM57,000.00
Invoiced issued		18 July 2016
GST (RM57,000.00 X 6%)		RM3,420.00

3rd interval

Payment received	=	RM57,000.00
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<i>Invoiced issued</i>	<i>16 October 2016</i>
<i>GST (RM57,000.00 X 6%)</i>	<i>RM3,420.00</i>
4th interval	
<i>Payment received</i>	<i>= RM142,500.00</i>
<i>Invoiced issued</i>	<i>31 January 2017</i>
<i>GST (RM57,000.00 X 6%)</i>	<i>RM8,550.00</i>

The contractor accounts for GST base on the date the payment is received. In the above example, the contractor AB Sdn. Bhd. has to account for GST on the values and dates as stated above, that is account for GST of RM1,710.00 on 12 April 2016 for the first interval, account GST of RM3,420.00 on 18 July 2012 for the second interval, and so on.

Q11. How do I account for the GST if my client has paid less than the amount of progress claim?

A11. If you issue a tax invoice equivalent to the value / amount stated in the certificate in relation to any work done (progress certificate) issued by any authorized person but is less than the amount stated in the progress claim, you may issue a credit note and shall make adjustment in the GST return. In this scenario the contractor shall reduce output tax in the return for the taxable period in which the credit note was issued.

Example 8

You issued tax invoice for services performed amounting to RM70,000 based on such progress certificate issued by the architect or engineer. However, the amount that should be due to you was estimated to be RM80,000 (contract amount). Under this situation you could issue credit note for the balance RM10,000 and account for GST based on RM70,000.

Payment not in the form of money

Q12. How do I account for the GST when payment is not in the form of money?



A12. You have to account for the GST based on the open market value of the consideration received.

Example 9

You provide construction services valued at RM5,000. In return, your client give you furniture. The open market value of the furniture is RM5,200. You account GST based on RM5,200 (GST inclusive) in the following manner:

$$GST = RM5,200 \times \frac{6}{106}$$
$$GST = RM294.34$$

Input Tax Credit

Q13. Can I claim input tax for the services related to the supply of construction project? For example, professional services of architects.

A13. Yes, you can claim input tax on services incidental to the construction project regardless whether the project is residential housing or commercial building. It is because all construction services are standard rated. However, if you are developer of residential properties and supply such construction services on such project, you cannot claim input tax because the supply of residential house is an exempt supply.

Q14. Can I claim input tax credit on landscaping work constructed on the residential property which is required by Planning Authorities?

A14. Yes, you can claim input tax credit because the inputs are attributable to a taxable supply .All construction services done in Malaysia are subject to GST, regardless of whether such services in relation to residential or non-residential properties and such services may include landscaping services constructed by the contractors. GST will be imposed on the supply of such services at standard rated even though residential properties are exempt supplies.

Q15. Can I claim input tax on built-in-furniture supplied together with the construction of building?

A15. Yes, if you are a contractor you can claim input tax if the built in furniture is supplied by you in the course of construction project. Any furniture and fittings that are supplied together with the construction of building are subject to GST.

Contra Payment or Counter Supplies.

Q16. I provide construction services to a land owner who in return (after completion) leases the land and building to me for a period of 5 years. Can I contra the payment of the construction services with the lease payment? When do I have to account for GST?

A16. No, there are 2 supplies involved; the supply of construction services from the contractor to the land owner and the second supply made by the land owner to the contractor i.e. leasing services. You have to account GST on the open market value of the 5 years lease of the land and building. The time to account GST is when the lease is given to you. The land owner has to account for the open market value of the construction services. Both the land owner (if taxable person) and contractor should issue a tax invoice for the gross value of the supply made to each other and account the GST accordingly. It is incorrect to contra the payment of the construction with the lease payment. The contractor as GST registrant has to charge land owner GST for the supply of construction services which the land owner can recover as input tax credit. The landowner also has charge GST for the leasing services and the contractor may recover it as his input tax.

Q17. I provide construction services to a landowner who in return gives to me 20 units of the commercial building. How and when do the land owner and I have to account for GST?

A17. You have to account for GST on the open market value of the 20 units of commercial building. The time to account is when the building was given or made available to you. The landowner (if GST registered) would account for GST on the open market value of the construction services provided by you. The landowner has to account for GST when the construction services is completed.

Q18. The developer purchased and supplied the contractor with building materials and workers. Can the contractor deduct the value charges for these supplies from the amount of progressive payments due to him?

A18. No, there are two separate supplies in this instance; the supply of building material and worker from the developer to the contractor and the second supply made by the contractor to the developer for the construction services. Both the developer and contractor should issue a tax invoice for the gross value of the supply made to each other and account the GST accordingly. Hence, it is incorrect to charge and account the output tax only on the amount being payment made by the developer being net off value of building material and worker. The developer as a GST registrant has to charge the contractor GST for the supply of building materials and workers which the contractor can recover as input tax credit.

Q19. In relation to the question above, how should the developer and contractor account for the GST?

A19. (a) On the part of the developer:

The developer, DK Sdn. Bhd. supplies building material and workers amounting to RM50,000. DK Sdn. Bhd. has to issue the contractor a tax invoice of RM50,000 and account for GST amounting RM3,000 (RM50,000 X 6%).

(b) On the part of the contractor:

Contractor may recover the GST above as input tax.

The progressive payment due is RM100,000. The contractor has to issue tax invoice of RM100,000 to DK Sdn. Bhd. and account for the output tax of RM6,000 (RM100,000 X 6%).

Construction Works Relating To Exempt Properties.

Q20. Supplies in form of sale, lease or rental of residential properties are exempted from GST. Does it mean that all construction works related to such residential properties, being an exempt supply, are exempted from GST too?

A20. No. All construction services are subject to GST, irrespective of the types of property the construction works are carried out. Construction works related to residential properties will also be standard rated even though residential properties are exempt supplies.

Retention Amount

Q21. The construction contract allows the client such as the developer or an individual to withhold a percentage from the payment of each progress payment pending satisfactory completion of the entire contract. Is this withholding or the retention amount subjected to GST?

A21. The retention amount is not subjected to GST until the money is released to the contractor. The amount of the progress billings, excluding retention money, has to be accounted for GST based on the date the payment is received as stated in the construction contract entered. For retention amount/sum, the contractor has to account for GST after he received the money. Normally, construction contracts which have been agreed by both parties normally provide for a contractor to render, from time to time, progress billings as work progresses. Such contracts also normally stipulate that the contractor be paid, usually after the relevant part of the work has been satisfactorily completed, as certified by the client, the client's architect or engineer. It may also require the client to withhold a percentage from the payment of each progress billings pending satisfactory completion of the entire contract. The retention money/sum withheld is not paid to the contractor until the conditions for the payment of the money or sum as specified in the contract are met.

Example 10

A contractor BB Sdn. Bhd. enters into an agreement to construct a project for BC Sdn. Bhd. and the project cost is RM84,000. The construction contract entered by both parties allow BC Sdn. Bhd. to withhold 5% from the payment of each progress billings pending satisfactory completion of the entire contract as a retention sum. It's also stipulates that the work is scheduled for 2 successive intervals. In his billing BB Sdn. Bhd. will have to account for GST as follows:

Progress Payment - 1st interim certificate

Value of material and works	=	RM30,000.00
Less: Retention sum (RM30,000 X 5%)		(RM1,500.00)
Amount Paid		RM28,500.00
GST (RM28,500 X 6%)		RM1,710.00

Progress Payment – 2nd interim certificate

Value of material and works	=	RM84,000.00
Less: Retention sum (RM84,000 X 5%)		(RM4,200.00)
Less: 1st interim certificate		(RM28,500.00)
Amount Paid		RM51,300.00
GST (RM51,300 X 6%)		RM3,078.00
Total retention sum		RM5,700.00
GST on retention money/sum		RM342.00

Q22. When do I have to account GST for the retention sum?

A22. You have to account for GST after you get the amount of retention sum, or when you issue an invoice related to the retention sum, whichever is the earlier.

Example 11

Based on Example 10, the retention amount is RM5,700 exclusive of GST. You must account for GST of RM342 (RM5,700 X 6%) after you received that amount from your client, or when you issue an invoice for the retention sum.

Q23. When can my client claim input tax on retention sum?

A23. When the retention sum is released to you and you issue him a tax invoice, or you give to him a receipt of payment.

Damages and Out of Court Settlement

Q24. What is GST treatment for damages and out of court settlements?



A24. Damages and out of court settlements which are paid for the breach of warranty or delays in completion of contract, are compensatory in nature. Hence such settlements cannot be treated as taxable supply and GST need not be charged for such recovery. However GST is chargeable for settlements that are payments for taxable supplies made.

Liquidated damages

Q25. Are liquidated damages such as delay in completion of work subject to GST?

A25. No, liquidated damages due to delay in completion of the construction project is not subject to GST.

Example 12

The Main contractor, AMC Sdn. Bhd, did not complete the building project by the stipulated completion date stated in its contract with its developer, DEC Pemaju Perumahan. It is required to pay liquidated damages to the DEC Pemaju Perumahan at a rate of RM3,000 per calendar day (including Sundays and public holidays) for every day where the completion of the project is delayed. Such liquidated damages are not subject to GST as it is compensatory in nature.

Rectification of defect

Q26. Under the contract, the main contractor is required to carry out rectification works during the defect liability period. However, since the main contractor did not want to rectify this defect, another contractor is hired by developer to rectify the poor workmanship done by the main contractor and as a result additional cost is incurred. What is the GST treatment on this?

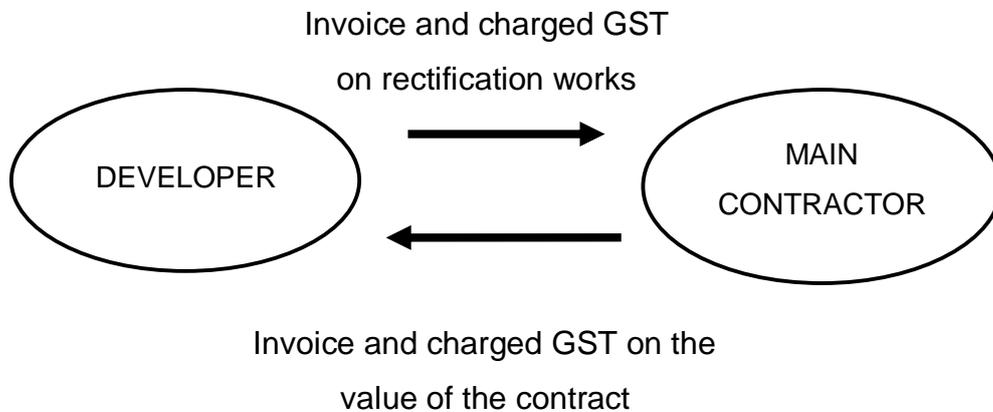
A26. The developer can recover the amount for rectification of defect in two ways:

- (a) Deduct the cost of rectification work from the retention sum.

Such supplies will be treated as two separate supplies. One supply is from the main contractor for completing the entire job (though not entirely

to the developer's satisfaction) on the full value of the contract (including the retention sum).

Another supply is from the developer to main contractor for the full value of the rectification works because the developer is making good the defects that should have been done by main contractor.



- (b) Claim payment from the main contractor.

The developer may go to court to seek payment from the main contractor for the rectification cost, or this may be agreed by an out-of-court settlement. Such payment is subject to GST as it is in relation to taxable supplies made from the developer to the main contractor for making good the defects which should have been rectified by the main contractor. The main contractor should still charge the developer GST on the full value of its supply, and the developer should charge the main contractor GST for the rectification works, similar to (a).

Q27. What is the GST treatment if the compensation only relates to the poor work done and does not involve any rectification works?

A27. If no rectification work is going to be carried out and the developer is only claiming compensation from the main contractor for the poor work done, such compensation is not subject to GST as there is no supply made. The main contractor will still have to bill the developer for the full value of the contract including the retention sum.

Please refer to Paragraph 17 and 18 of this Guide.

Tender, Liquidated Damages and Contract Deposits

Q28. Are tender and contract deposits subject to GST?

- A28. (a) The deposit for payment of contract documents is subject to GST because it involves the supply of goods.
- (b) No GST is payable, if the deposit serves as a security to ensure the contractor proceeds with the contract or to ensure that the contractor carries out all the obligations detailed in the contract.
- (c) Yes, if a deposit is intended to be used to offset against the future payments (partly or fully) once the supply has been made, GST is chargeable on such a deposit.

Example 13

A property developer, DZ Sdn. Bhd., calls for main contractors to tender for a large scale project in Puchong. Interested tenderers have to purchase the tender documents containing details of the project (e.g., plans, specifications, schedule of quantities) for a fee of RM250. This fee is non-refundable and is subject to GST as it is a sale of tender documents. GST should be charged on this supply.

DZ Sdn. Bhd. then awards the building contract to main contractor, MS Sdn. Bhd. MS Sdn. Bhd. is required to submit a security deposit in the form of a banker's guarantee of 5% of the contract sum for non-performance. This deposit will be refunded upon the completion of the contract. This security deposit is not subject to GST as there is no supply made.

Since this is a large-scale project, DZ Sdn. Bhd. is required to give MS Sdn. Bhd. an advance payment (akin to a deposit) which will be used to offset against future progress payments. GST should be charged on this advance payment.

Bad Debts

Q29. What will happen if my customer does not pay me after I have issued tax invoice after completion of work?



A29. You can claim bad debts relief on the GST output tax paid in respect of taxable supplies. The GST portion of the bad debt can be recovered subject to certain conditions:

- (a) The tax is already paid;
- (b) You have not received any payment 6 months after the supply has been made, or the debtor has become insolvent; and
- (c) Sufficient efforts have been made by you to recover the debt.

Q30. Do I have to make a formal claim to recover GST due to bad debts?

A30. No, you only need to make adjustment by increasing your input tax in your GST return after you have satisfied all the conditions for bad debt relief.

Q31. What happen if my customer pays me back the bad debt after I have claimed bad debt relief?

A31. You have to make adjustment by increasing your output tax in your GST return.

Supply of workers or services of personnel from overseas

Q32. What is the GST treatment if I were to employ workers or services of personnel from overseas?

A32. The treatment is as follows:

- (a) If the foreign worker works for you under contract of employment, it is not subject to GST.

Example 14

DEF Sdn. Bhd. is a registrant and hires foreign worker under contract of employment to work in their company. This supply of foreign worker is not subjected to GST.

- (b) GST is chargeable if you supply the foreign worker under your employment to another company.

Example 15

ABC Sdn. Bhd. is a contractor that has a pool of foreign workers. XYZ Sdn. Bhd. requires workers in his construction industry. ABC

Sdn. Bhd. provides foreign workers to XYZ Sdn. Bhd. in return for payment. Therefore ABC Sdn. Bhd. should charge GST when they provide foreign workers to XYZ Sdn. Bhd.

- (c) If a foreign consultant does work for you, but is not under your contract of employment, you have to account for GST by reverse charge mechanism. Under this mechanism, the GST liability shifts from the supplier to the recipient if the recipient's fixed or business establishment or his usual place of residence is in Malaysia. Hence, as the recipient of the services, the contractor is liable to account GST on the supply made for the purpose of any business.

When such contractor receives a supply of imported services for the purpose of business, he is treated as if he is making and receiving the supply. Since he is treated as making a supply, he is required to account GST on the supply of imported services as his output tax. Since, construction services is a taxable supply, the contractor is entitled to claim the GST incurred as his input tax and have to declare both input tax and output tax in his GST return. The contractor as the recipient of the services is liable to pay the tax not later than the last day of the month following after the end of his taxable period where the payment for the supply of imported services is made to the supplier.

Example 16

KK Sdn. Bhd. hires a foreign consultant in building a bridge. Payment to the foreign consultant will be subject to GST. KK Sdn. Bhd. has to account for it by reverse charge mechanism. Reverse charge mechanism will shift the GST liability from the supplier to the recipient. Thus, when KK Sdn. Bhd. receives a supply of imported services (foreign consultant) for the purpose of business i.e. to construct a bridge, he is treated as if he is making and receiving the supply of consultancy services. Since he is treated as making a supply, he is required to account GST on the supply of imported services as his output tax. As construction services is

a taxable supply, KK Sdn. Bhd. is entitled to claim the GST incurred as his input tax.

Contracts

Q33. Are contracts signed which span the transitional period (pre and post GST implementation date) liable for GST?

A33. The value of contract works performed before GST implementation is not subject to GST. However, the value of contract works performed after GST implementation will be subjected to GST.

Q34. What are the consequences if I do not make a provision to include the element of GST in my contract?

A34. Failure to include the GST provision may result in the contractor, if he is registered under GST, unable to recover the GST from the client.

Transitional Provisions

Q35. I bought goods that were subject to sales tax and I still have these goods in my trading stocks on 1 April 2014. Can I be refunded the amount of sales tax paid on those goods?

A35. If you are registered under GST, you can claim special refund of sales tax paid on those goods provided you have documentation such as invoices and custom documentation to show sales tax have been paid.

Q36. What is GST treatment on progress payment on any construction contract made before 1 April 2015?

A36. Generally, GST is only payable on any supply of goods or services to the extent that it is made on or after 1 April 2015. Basically, the value of work and materials permanently incorporated in or affixed on the construction site before 1st April 2015 will not be subject to GST. In order to determine whether the performance of the service is subject to GST or not, a contractor is required to value all works and materials permanently incorporated in or affixed on the construction site of the building or civil engineering work at the beginning of 1 April 2015.

This value must be determined on or before the end of the first taxable period after 1 April 2015. Such valuation must be certified by an authorized person e.g. registered engineers, architects or quantity surveyors as in question 37. In the case where, the value of the supply after 1 April 2015 exceeds the value certified, then GST will be chargeable on the exceeded amount (apply GST on the margin). Whereas, if the value of the supply after 1 April 2015 is less than the certified value, no GST is chargeable on such amount. However, if the taxable person fails to comply on the certified value within the specified time, GST will not be charged on the margin but on the full value of the supply.

Q37. How do I calculate GST on value of construction work for project that straddles between two periods that is before and after GST implementation?

A37. There are 2 situations:

- (a) For projects above RM1,000,000 and which requires the issuance of certificate in relation to any work done.

You must apportion the value of construction works pre and post GST. GST is only chargeable for construction work done after GST implementation. A recognized person such as engineer and architect has to verify the value and amount of work and the materials permanently incorporated or affixed on the site of the building or civil engineering work for the period prior to commencement of GST.

Example 17

KLM Sdn. Bhd. has a contract above RM1,000,000 with JKL Sdn. Bhd. to build commercial building. The contract is scheduled to begin on 1 May 2014. Under the contract of agreement, KLM Sdn. Bhd. will receive payment inclusive of GST based on monthly progress billing. On 1 July 2015, the architect does the valuation and certifies the value of work done till 31 June is RM1,000,000. After completion of the project on 15 July 2015, KLM Sdn. Bhd. lodges a claim amounting to RM1,100,000. GST due is based on RM100,000 (RM1,100,000 – RM1,000,000) for the construction work done after GST implementation.

$$\text{GST} = \text{RM}100,000 \times 6\% = \text{RM}6,000$$

- (b) For projects below RM1,000,000 and which do not require issuance of certificate in relation to any work done.

As the contract value is below RM1,000,000 and does not require certification by the architect or engineer as a recognized person, you have to apportion the value of work done before and after commencement of GST. You have to account for GST for the value of work done after the period of commencement of GST.

Example 18

TJK has a contract with an individual to build a residential building. The contract is scheduled to begin on 15 March 2015. Under the contract of agreement, TJK will receive payment on completion of work. Upon completion of the project on 14 July 2015, TJK lodges a claim amounting to RM42,000. GST due is based on RM34,615 (RM42,000 X 75/91) for the construction work done after GST implementation.

$$\text{GST} = \text{RM}34,615.00 \times 6\% = \text{RM}2,076.00$$

Total number of days undertaken for project = 91 days

Construction work done after GST = 75 days.

Q38. What is the GST treatment on Retention amount that straddles between two periods that is before and after GST implementation?

A38. Where such retention amount under a construction contract relates to a supply of construction services made before 1 April 2015, such retention amount is not subject to GST. However, if such amounts relates to a supply made after 1 April 2015, it shall be subject to GST.

Example 19

A contractor makes a supply of services from 1 December 2014 to 31 May 2015. A sum of RM48,000 is retained for the satisfactory performance of the construction work. Since part of services are

performed before 1 April 2015 (four months) and part of it is performed after 1 April 2015 (two months), the amount of GST payable on the retention sum is:

$$RM48,000 \times 2 / 6 \times [6/106] = RM905.66$$

Please refer to the GST Guide on Transitional Rules for further details about the transitional issues.

FEEDBACK OR COMMENTS

21. Any feedback or comments will be greatly appreciated. Please email your feedback or comments to either Zaizah bt Zainuddin (zaizah.zainuddin@customs.gov.my), Raizam bt. Mustapha (raizam.mustapha@customs.gov.my) or Haslim Eairon bin Mat (haslim.mat@customs.gov.my).

FURTHER INFORMATION

22. Further information can be obtained from:

- (a) GST Website: www.gst.customs.gov.my
- (b) GST Tel: 03-88822111
- (c) Customs Call Centre:
 - Tel : 03-78067200/ 1-300-888-500
 - Fax : 03-78067599
 - E-mail : ccc@customs.gov.my