PRESS STATEMENT

FMM WELCOMES GOVERNMENT'S MOVE TO INCORPORATE KEY GST FEATURES INTO SST TO REDUCE TAX CASCADING AND COST PRESSURES

Kuala Lumpur, August 19, 2026 – The Federation of Malaysian Manufacturing (FMM) welcomes the announcement by YAB Dato' Seri Anwar Ibrahim, Prime Minister and Minister of Finance, that the Government is open to studying the incorporation of selected features of the Goods and Services Tax (GST) into the existing Sales and Service Tax (SST) framework. The announcement was made at the closing session of the Budget 2027 engagement session in Putrajaya on August 18, 2026. The Government has indicated that SST will remain the foundation of the national tax system and that it does not intend to impose a broad-based tax on the rakyat at this stage.

FMM has consistently highlighted tax cascading as an inherent weakness of the SST system, particularly where taxes paid on business inputs cannot be recovered and become embedded in costs throughout the supply chain. This is also why FMM has long advocated the reintroduction of GST as the preferred long-term indirect tax framework. GST offers a more comprehensive tax structure because of its input tax credit mechanism, which allows a business to offset tax paid on its inputs against tax collected on its output, so that tax does not accumulate at every stage of the supply chain. The Government's proposal therefore opens a practical pathway to incorporate this important GST feature into SST without requiring an immediate full return to GST. On this basis, FMM supports the direction being considered by the Government.

The need to address this weakness of SST has become increasingly urgent as its scope has expanded significantly since 2024, bringing more business inputs and services into the tax net and intensifying tax cascading and embedded costs across the supply chain. Service tax on most taxable services increased from 6% to 8% on March 1, 2024, while logistics remained at 6%. From July 1, 2025, service tax was extended to additional areas including rental and leasing, construction and financial services, while sales tax was also revised to bring a wider range of goods within the 5% and 10% tax bands. Rental and leasing services were initially brought into the service tax scope at 8% from July 1, 2025, but the rate was subsequently reduced to 6% from January 1, 2026.

The Government has also had to make other post-implementation adjustments to the expanded SST framework. These include exemptions for certain critical raw materials and inputs used in the manufacture of animal feed, fertilisers and pesticides, as well as further transitional relief for qualifying construction contracts. These subsequent revisions indicate that the wider cost and supply-chain impact of some of the expanded SST measures was not fully captured at the outset and only became clearer after implementation and industry feedback. This reinforces the importance of assessing the full tax impact across the production and distribution chain before new measures are implemented.

Although FMM welcomes these adjustments, correcting individual areas after implementation does not resolve the underlying structural weakness of SST. Businesses may still incur sales tax on taxable materials, machinery and other inputs, together with service tax on logistics, factory rental, construction and other taxable business services. Where no exemption or relief applies, these taxes cannot be recovered and instead become embedded in the cost of production and distribution.

The interaction between sales tax and service tax can further compound the impact. A manufacturer may purchase taxable materials or equipment that already carry sales tax and subsequently incur service tax on the logistics, rental or construction activities required to bring those inputs into production. Each unrecoverable tax can therefore become part of the business cost base and be carried forward into the value of the next transaction. The need for repeated exemptions, rate reductions and other post-implementation adjustments reinforces FMM's view that a more systematic mechanism is needed to address tax cascading at source.

The rakyat are therefore not necessarily insulated from SST simply because an essential final product is exempt from sales tax. Where taxes incurred upstream cannot be recovered, they can become embedded in the cost of producing and distributing that product and, depending on market conditions, may ultimately be reflected in the price paid by consumers. The same embedded tax costs affect Malaysian exporters, who must compete internationally against producers operating under tax systems that allow business input taxes to be recovered.

This is why FMM sees merit in the Government's proposal to incorporate the good features of GST into SST, particularly the input tax credit mechanism. A properly designed credit mechanism would address the problem at source by allowing eligible taxes paid on business inputs to be recovered, rather than requiring repeated exemptions and corrective measures after implementation.

FMM'S RECOMMENDATIONS

FMM proposes that the Government focus the study on the GST features that directly address the weaknesses now evident under the expanded SST framework:

1. Introduce a systematic input tax credit or offset mechanism for business inputs. Eligible sales tax and service tax incurred on business inputs used in production and business operations should be creditable or offset against tax liabilities. This should cover relevant taxable inputs and costs such as materials, machinery, logistics and freight forwarding, factory rental, construction of production facilities, financing and other qualifying business services. The objective is to prevent tax paid on legitimate business inputs from becoming a permanent production cost and being carried into each subsequent stage of the supply chain.

2. Ensure essential goods are genuinely insulated from embedded tax. Keeping an essential final product exempt from sales tax does not fully protect the rakyat if sales tax and service tax incurred upstream remain embedded in its cost. FMM therefore proposes GST-style zero-rating treatment, or an equivalent credit, rebate or refund mechanism, for eligible upstream taxes directly attributable to the production and distribution of essential goods. This would ensure that the policy objective of keeping basic necessities tax-free is achieved throughout the supply chain and not only at the final point of sale.

3. Ensure export tax neutrality. Malaysian exports should not carry embedded domestic consumption taxes. Eligible sales tax and service tax incurred in producing and delivering exported goods should therefore be creditable, rebated or refunded. This is consistent with the GST principle that exports should leave the country free of domestic consumption tax and is important to protect the price competitiveness of Malaysian manufacturers in global markets.

4. Replace multiple category-specific reliefs with a more systematic mechanism. The current SST framework relies on different exemptions and reliefs depending on the type of goods, services, transactions and qualifying conditions. While these measures provide relief in specific circumstances, they do not address cascading consistently across the business supply chain. With the scope of SST already substantially expanded, a systematic credit or rebate mechanism is needed to reduce tax-on-tax effects and provide more consistent treatment across different business models and supply chains.

5. Build in a reliable, automatic and time-bound refund mechanism from the outset. One of the key lessons from Malaysia's previous GST implementation was the impact of delayed input tax credit refunds on business cash flow. Any new credit mechanism must therefore be supported by clear and enforceable refund timelines, straightforward verification procedures and risk-based audit controls. Verified excess credits, particularly for exporters and capital-intensive manufacturers, should be refunded promptly. A credit that remains outstanding for an extended period ties up business working capital and undermines the purpose of removing tax from business inputs.

6. Use e-Invoice infrastructure to support verification and compliance. Malaysia's e-Invoice system provides an opportunity to validate eligible B2B transactions digitally, strengthen transaction visibility and improve fraud controls. This infrastructure should be used to support a more efficient credit and refund mechanism while keeping compliance requirements practical, particularly for SMEs.

7. Involve FMM and affected industries from the outset. FMM and other affected industry bodies should be involved from the beginning of the Government's study and throughout the design, implementation and transition stages. Manufacturers are directly affected taxpayers and major purchasers of taxable goods and services across the supply chain. Where relief is unavailable, they bear sales tax and service tax on business inputs which can become embedded in production costs. Industry participation from the outset is therefore essential to identify where cascading occurs in actual transactions, test how the proposed credit and refund mechanisms would work across different sectors and ensure that the final framework can be implemented effectively.

FMM's position on GST as the preferred long-term indirect tax framework remains unchanged. At the same time, FMM recognises the Government's intention to retain SST as the base system at this stage. If this approach is maintained, the priority should be to incorporate the GST features that prevent taxes on business inputs from accumulating through the supply chain, particularly input tax credits, effective treatment of essential goods and exports and a dependable refund mechanism.

FMM urges the Government to commence structured engagement with industry immediately. With the expanded SST already affecting business input costs, early action is needed to address cascading before these costs become further embedded in consumer prices and exports. FMM stands ready to work with the Ministry of Finance and the Royal Malaysian Customs Department from the outset to develop a practical framework that protects revenue, contains cost-of-living pressures and strengthens Malaysia's competitiveness.

Mr Jacob Lee Chor Kok
President, Federation of Malaysian Manufacturing

FMM Advocates Transparency, Integrity, Accountability and No Corruption

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About FMM

The Federation of Malaysian Manufacturing (FMM) (formerly known as Federation of Malaysian Manufacturers) has been the voice of the Malaysian manufacturing sector since 1968, advocating policies and initiatives that drive industrial growth, competitiveness and workforce development. Representing over 13,300 member companies (4,200 direct and 9,100 indirect) from the manufacturing supply chain, FMM is actively engaged with government and its key agencies at Federal, State and local levels. FMM is also well-linked with international organisations, Malaysian businesses and civil society. Apart from benefitting from FMM's advocacy, FMM members enjoy value-added services including training, business networking and trade opportunities as well as regular information updates.

Media Enquiries:

Han Mong Ying, Senior Manager, Corporate Affairs
Tel : 03-6286 7200 | Email: webmaster@fmm.org.my