



ROYAL MALAYSIAN CUSTOMS

GOODS AND SERVICES TAX

GUIDE ON PAWNBROKING

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INTRODUCTION

1. This industry guide is prepared to assist businesses in understanding matters with regards to Goods and Services Tax (GST) treatment on pawnbroking.

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 or relieved. 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.

GST TREATMENT ON CONVENTIONAL PAWNBROKING

Provision of Pledge

5. The provision of the pledge by the pawner to a pawnbroker / *Ar-Rahnu* operator and the compensation made by the pawnbroker / *Ar-Rahnu* operator to the pawner in the event the pledge is destroyed, damaged, stolen or other acts of negligence by the pawnbroker / *Ar-Rahnu* operator is not a supply and is not subject to GST.

6. In addition, the provision of the loan by the pawnbroker / *Ar-Rahnu* operator is an exempt supply.

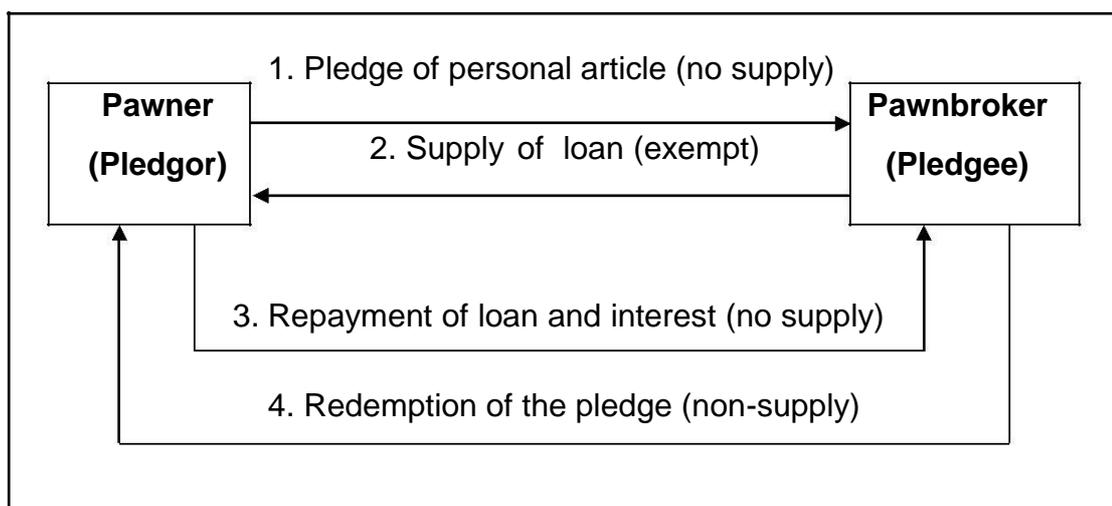
Accounting for GST on sale of pledges in conventional pawnbroking

7. The GST implication on the transactions involving a redeemed pledge and an unredeemed pledge is as follows:

(a) Redeemed pledge

Under section 18(1), Pawnbrokers Act 1972, the usual redemption period is within six (6) months from the date of pawning. The extension of time for redemption is allowed as may be agreed upon by the pawnbroker and the pawner under section 19, Pawnbrokers Act 1972. Should the pawner recovers the goods or redeems a pledge within the agreed redemption period, this redemption would not trigger any GST implication because there is no transfer of ownership. A pawnbroker is not making a supply and is not required to account GST on the redemption.

Figure 1: Illustration of Pawning and Redemption



(b) Unredeemed pledge

Pursuant to section 23(1), Pawnbrokers Act 1972, for unredeemed pledge, the GST treatment is as follows:

(i) Pledge not exceeding RM200.00

If the pledge is not redeemed within the redemption period, the pledge automatically becomes the property of the pawnbroker.

The GST implication here is:

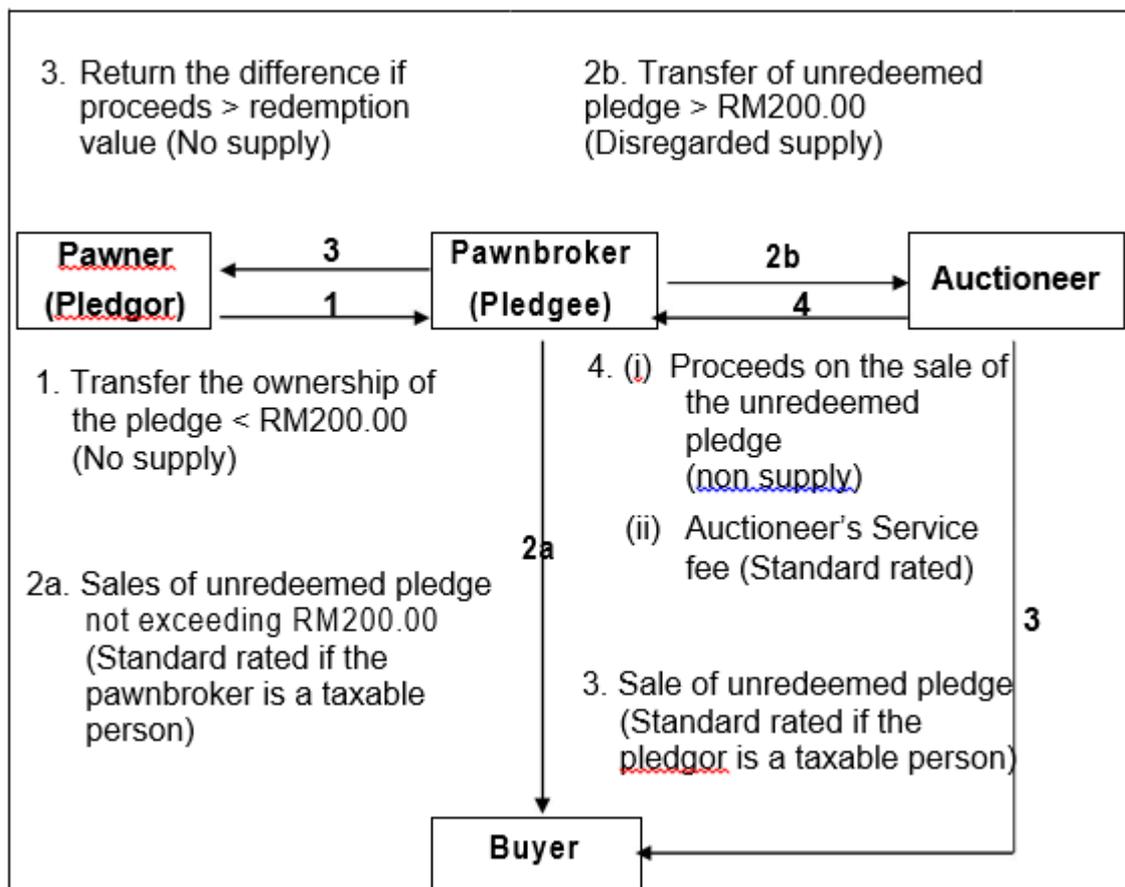
- If the pawnbroker disposes the pledged goods to a third party (e.g. goldsmith), the pawnbroker is making a taxable supply. The pawnbroker must account for GST on the sale of the pledge if the pawnbroker is a taxable person.

(ii) Pledge exceeding RM200.00

If the pledge is not redeemed within the redemption period, the pledge will be transferred to the auctioneer who will auction the unredeemed pledge. The transfer of the unredeemed pledge to the auctioneer is not a supply and therefore he does not need to account for GST.

When the auctioneer auctions the unredeemed pledge, the sale of the unredeemed pledge is regarded as a supply made by the pawner. The auctioneer should charge and account for GST on the sale of the unredeemed pledge provided that the pawner is a taxable person. If the pawner is not a taxable person, GST is not charged on the sale of the unredeemed pledge. If the auctioneer is a registered person, the auctioneer will charge GST on his services to the pawnbroker.

Figure 2: Illustration of Unredeemed Pledge



GST TREATMENT ON ISLAMIC PAWNBROKING

Islamic Pawnbroking

8. Islamic pawnbroking is known as *Ar-Rahnu* and is a collateralized borrowing. *Ar-Rahnu* means “to put something (gold articles of purity exceeding 18 carat)” as a collateral to secure a loan and the collateral is used to pay the loan when the borrower does not pay his loan at the end of the agreed redemption period.

9. The collateral entrusted to the lender and the subsequent return of the collateral upon repayment by the borrower is not a supply.

10. The loan to the borrower is an exempt supply and not subject to tax.

11. *Ar-Rahnu* is based on three Islamic concepts:

- 11.1 ***Qardhul Hasan*** which refers to a loan granted to the borrower who wishes to pledge his valuable item when he is only required to pay the amount borrowed.
- 11.2 ***Al-Ujrah*** is the commission or fee charged for the services rendered. Thus, in pawnbroking, *Al-Ujrah* is the safekeeping fee charged on the pledged items.
- 11.3 ***Al-Wadiah Yad Dhamanah*** is the concept of custody of the valuable asset whereby a promise to keep the valuable asset in a safe place. Thus, the customer will be charged for the services rendered in keeping the valuable asset.

Safe keeping fee

12. Unlike the conventional pawnbroking, there is no interest element on the loan, but there is a **safe keeping fee** where a lender is allowed to charge a reasonable fee for keeping the pledged items safe and in good condition. The fee is charged at a fixed rate on the value of the pledge. The supply by the lender to safe keep the pledges is an exempt supply.

13. If a safe keeping fee is charged on a pledge where no loan was secured by the pledgee, the fee will also not be subject to GST.

14. If the lender fails to keep the agreement, he will be responsible to replace the missing or stolen items to the owner or borrower. The replacement of collateral by the lender is not a supply for GST purposes.

Sale of unredeemed pledges

15. Under *Ar-Rahnu*, the initial redemption period is 6 months. However, it can be extended to a period to be determined by the *Ar-Rahnu* operator. After the maximum extended period, the unredeemed pledge will be disposed by the *Ar-Rahnu* operator on behalf of the borrower through an open auction which is treated as a taxable supply. However, the sale of the unredeemed pledge may be disposed by the *Ar-Rahnu* operator or an appointed auctioneer irrespective of the value of the unredeemed pledge. This is unlike the position of a sale of unredeemed pledge under the

conventional pawnbroking i.e. a cap on the value of sale of unredeemed pledge at RM200.

16. When the *Ar-Rahnu* operator or an auctioneer auctions the unredeemed pledge, the sale of the unredeemed pledge is regarded as a supply made by the borrower. The *Ar-Rahnu* operator or an auctioneer should charge and account for GST on the sale of the unredeemed pledge provided that the borrower is a taxable person. If the borrower is not a taxable person, GST is not charged on the sale of the unredeemed pledge.

17. However, in the case of a sale made by the *Ar-Rahnu* operator, he is required to account for output tax and in the case of a sale made by the auctioneer, the auctioneer is required to account for output tax. For further obligations of the auctioneer, please refer to the **Guide on Auction Services**.

18. Net sales proceeds on the auction of the pledges returned to the borrower or his beneficiary by the *Ar-Rahnu* operator is not a supply. However, the auction services provided is a taxable supply by the auctioneer and subject to GST at a standard rate.

19. Expenses such as takaful, transport charges and security services on the pledges borne by the operator for the auction exercise, the input taxes incurred are claimable by the operator.

Calculation on the sale of unredeemed pledges

20. Assuming the *marhun* (value of the item pledged) is worth RM1,000 and the bank (*Ar-Rahnu* operator) releases a loan of RM650 (65% of *marhun*) with a repayment period of six months. The safekeeping fee is RM0.65 for every RM100.00 of *marhun* then the fees will be RM6.50 per month or RM39 for six months.

21. Under regulation 14(g), Pawnbrokers Regulation (Control and Licensing) 2004, the reserve price for unredeemed pledges must be set at 10% on top of the loan for pledges to be auctioned. Thus, the reserve price is RM715.

22. If there is a bid at the value of RM1,000, the bank will deduct RM650 for the loan, RM58.50 for safekeeping fees (9 months), administration fees and postage fee

for the auction at RM30.00, and then the balance will be returned to the customer. The illustration below will show you the transactions subject to GST.

Bid price of the sale by auction			1,000.00
GST (6%)			56.60
Loan unpaid	650.00		
Safekeeping fee	58.50		
Administration Fee and Postage Fee*	30.00		
GST (6%)	<u>1.80</u>	31.80	740.30
Balance returned to customer			203.10

*If the auctioneer is a registrant, he will charge GST for his services to the borrower.

RATES AND CHARGES

23. Generally the treatment of GST on the rates and charges below are as follows:

(a) Not subject to GST:

- (i) Search fee @4.00 (list of pawners or information of the pawner);
- (ii) Licence Fee;
- (iii) Advertising permit;
- (iv) Surplus paid to pawner when pawnbroker sell his pledge;
- (v) Disposal of unclaimed pledge to Accountant General.

(b) Subject to GST at a standard rate:

- (i) Pawn ticket fee;
- (ii) Handling charges;
- (iii) Insurance (Acquisition).

INPUT TAX CREDIT (ITC)

24. Input taxes are incurred on expenses such as insurance / takaful, transport charges and security services for the pledges under safe keeping or for an auction exercise.

25. Since a pawnbroker / *Ar-Rahnu* operator is making both taxable supply and exempt supply, he is entitled to claim input tax incurred on input that are directly attributable to taxable supply. For the residual inputs such as electricity and insurance premium, etc., he can claim input tax based on the apportionment rules. For further details, please refer to the General Guide on Input Tax Credit.

FREQUENTLY ASKED QUESTIONS

Registration

Q1. What are the taxable supplies do I take into account for the purpose of GST registration?

A1. The supplies are:

- (a) Sales of unredeemed article
- (b) Handling / administration charges
- (c) Other taxable supplies.

Input Tax Credit

Q2. I incur expenses on repairs and cleaning of broken unredeemed goods before I sell them. Can I claim GST on the expenses incurred on the sale of these unredeemed goods?

A2. Yes, you can claim the GST in full as input tax credit because the inputs are directly attributable to the sale of unredeemed goods (standard rated supply).

Q3. What about overhead expenses incurred such as electricity and office rental?

A3. Since electricity and office rental are residual inputs, you need to apportion these expenses by using the turnover method because as pawnbrokers, you are supplying both exempt and taxable supplies. Residual inputs are inputs which you cannot directly attribute to either taxable or exempt supplies.

Q4. The pawnbroker incurs GST on auctioneer's service fee. Can the pawnbroker claim input tax credit on this service fee?

A4. Yes, the pawnbroker is allowed to claim GST incurred on the auctioneer's service fee

Handling Charges

Q5. A pawnbroker charges RM0.50 per ticket as handling fees. Is the fee subject to GST?

A5. Yes, it is subject to GST at a standard rate.

Disposal on Imitation Items

Q6. Sometimes the pawnbroker without knowledge accepts an imitation item as pledge from the pawner. When the pawnbroker sells the imitation item and subsequently suffers losses, is this sale subject to GST?

A6. The disposal of any unredeemed article whether genuine or imitation is a taxable supply. Therefore, the pawnbroker must charge GST on such sale.

Loss on Disposal

Q7. Sometimes the sales proceed of the unredeemed pledge does not cover the value of the loan and interest, and subsequently the pawnbroker suffers a loss. Can the loss be exempted from GST?

A7. Any disposal of an unredeemed pledge is a taxable supply irrespective of whether there is profit or loss.

Disposal of Pledge through Open Tender/Auction under Ar-Rahnu

Q8. I dispose an unredeemed pledge through a tender exercise. In the tender process, I sell tender forms to the public. Is the sale of the tender form subject to GST?

A8. Yes, the sale is subject to GST at a standard rate.

Q9. I charge a service charge of 1% on the sales price for a disposal of a pledge. Is the service charge subject to GST?

A9. Yes, it is subject to GST at a standard rate.

Unredeemed pledge under conventional pawnbroking

Q10. When a pledge valued at RM150.00 is not redeemed after the redemption period, the ownership of the goods is transferred to the pawnbroker. Is the transfer a supply of goods from the pawner to the pawnbroker?

A10. The ownership transferred is a result of a default in repayment of the loan and the goods were confiscated. Hence, no supply is made when the goods is not redeemed.

Relief for second-hand goods

Q11. Can a pawnbroker secure a reduction on the tax charged i.e. relief for second-hand goods, when he disposes an unredeemed pledge?

A11. No, such reduction is not allowed in your business as it only applies to disposal of motor vehicles (cars, motorcycles, buses, etc.). Please refer to the GST General Guide for further details of the scheme.

Invoicing and Record Keeping

Q12. Is the auctioneer required to issue a statement for sale in satisfaction of debt under regulation 64, GST Regulations 2014 since the selling of unredeemed pledge is for that purpose?

A12. Yes, the auctioneer is required to do so. Prior to this, the auctioneer shall issue a document containing the prescribed particulars under regulation 24, GST Regulations 2014 to the buyer of the pledges and such document shall be treated as a tax invoice.

Q13. Is a pawnbroker supposed to add new column of GST 6% in Schedule N, Sales List for transactions on or after 1st of April 2015?

A13. No, Schedule N, Sales List is regulated under regulation 16, Pawnbrokers Regulation (Control and Licensing) 2004.

INQUIRY

1. For any inquiries for this guide please contact :

Sector IV

GST Division

Royal Malaysian Customs Department

Level 3 – 7, Block A, Menara Tulus,

No. 22, Persiaran Perdana, Presint 3,

62100 Putrajaya.

Email: gstsector4@customs.gov.my.

FURTHER ASSISTANCE AND INFORMATION ON GST

2. Further information on GST can be obtained from :

(a) GST website : www.gst.customs.gov.my

(b) Customs Call Center :

- Tel : 03-7806 7200 / 1-300-888-500
- Fax : 03-7806 7599
- E-mail : ccc@customs.gov.my