

# Tax planning in malaysia economics essay



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Employment is a contract between two parties, one being the employer and the other being the employee. In this relationship, the employer conceives of a productive activity, generally with the intention of creating financial revenues, and the employee contributes labour to the enterprise, usually in return for payment. Employment also exists in the public, non-profit and household sectors. An employer is any entity that hires employees; it can be a person, a company, an organisation or a corporation. There are a number of employment arrangements available, including full time employment, part time employment, casual employment, fixed term or contract employment, apprenticeships, traineeships, and probationary works. Employment allows an individual to be a valuable contributor to society and the economy, while providing for the needs of those under his/ her care. Being employed can also provide a sense of personal worth to the individual, and is a means for personal development.

### 1. 1. 1 Characteristic of Employment

There are few factors that link to make a person to be an employee such as personal services, presence of control, equipment, financial risk, basis of payment, benefits, sense of belonging to the organization, nature of contract, and intention of the parties.

When comes to employment, the duties will be perform by the employees themselves which means providing the service or task assigned by themselves but they also can hire another person to complete the task who are qualified to the job assigned. Meanwhile control is where employers take

control over the employees in directing them the way to accomplish and perform a job.

Employment also exists when the employees use tools provided by the employer to perform a duty or task. As for self-employed individuals, they use their own tools.

Financial risk is where as for self employed they faced the risk for expected return, but as for employees, they only share the profits but not the risks. A payment is given for the employees in a fixed rate of salary either on a monthly or weekly basis. As for self employed individuals, they are given a professional fee upon the completion of the task or progressively throughout the engagement based upon agreed deliverables.

An employee are entitle for benefits such as, sick pay, pension rights, Employee's Provident Fund contribution, Socso contribution, annual leave, and many more but all these benefits are not applied for self employed. Employees normally have a great sense of belonging to a particular organization that they serve. Employees duties sort of link together with their employer's business. There will be always an agreement or contract between the employers and employees, where it benefits for both parties such as for an employer they might expected the employee to perform work as promised, as for employee they want to protect the right against unfair dismissal.

## 1. 2 Employment as defined in Section 2 of the Income Tax Act 1967

An employer is defined in Section 2 of the Income Tax Act (ITA) 1967. In general, employer means the party that pays remuneration to the employees, where there is an “ employer-employee” relationship. For instance a manager, agent or person responsible for the payment of salary or wages to an employee, e. g. manager of a company, sole proprietor / partnership or any persons, whether or not statutory incorporated, e. g. an association. They also can be from Statutory Boards, Federal and State Governments.

Employment in which the relationship of master and servant subsists or any appointment or office, whether public or not and whether or not that relationship subsists, for which remuneration is payable.

As for employee, in relation to an employment, means where the relationship of master and servant subsists, the servant and that relationship does not subsist, the holder of the appointment or office which constitutes the employment.

The term employer, in relation to an employment, means where the relationship of master and servant subsists, the master and that relationship does not subsist, the person who pays or is responsible for paying any remuneration to the employee who has the employment, notwithstanding that that person and the employee may be the same person acting in different capacities.

## 2. 1 What is Business Income?

According to Internal Revenue Service (IRS), a US government agency that is responsible for tax collection and tax law enforcement, defined business income as income received from the sale of products or services. Examples of what is considered as business income are fees received by a professional person and rents received by a person in the real estate business.

Section 2 of Income Tax Act 1967 states that a business is defined when the element includes a profession, vocation, trade and manufacture, adventure or concern in the nature of trade but excludes employment. The business receipts are what you called a business income.

According to Section 4(a) of Income Tax Act 1967, states that business income is subject to income tax provided that they are revenue in nature and derived from Malaysia.

Diagram below shows how to determine a taxable business income:

Is there a business source?

Yes

Are the business transactions incomes in nature?

Yes

Business income is derived from Malaysia?

Yes

Business income to be taxed in Malaysia

Diagram 1: Taxable Business Income

Foreign source income remitted into Malaysia, on the other hand, is exempted from tax. To know whether business income is attributable to operations of the business carried on outside Malaysia is when one or more of the following exists:

Contracts are concluded outside Malaysia

Stocks are maintained outside Malaysia from which orders are filled

Passing of ownership and risk of trading stocks takes place overseas

Sales proceeds are received overseas

Services are rendered outside Malaysia.

The above factors help us determine a clearer definition of business income and in what aspects business income is subjected or exempted from income tax.

## 2. 2 What is Employee Income?

According to the “ Essential Guide to Personal Income Tax in Malaysia” a 2009th edition book by Adam Malik et al, “ employment is defined as being among else an appointment or office whether public or not and whether or not the relationship of master and servant subsist for which remuneration is payable”. In addition to the definition, an employment is deemed to exist when the relationship of master and servant subsists. The factors that can be used as a guide for employment definitions are as follows: control, personal service, equipment, financial risk, basis of payment, benefits, sense of belonging to the organization, nature of contract and intention to the parties.

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Receipts derived from one of the factors that defining employment is what you called an employment income.

Employment income derived from Malaysia is taxable both in the hands of resident and non-resident individuals. Foreign derived employment income, on the other hand is exempted from income tax. The situations wherein employment income is derived from Malaysia are as follows:

**Employment Discharged in Malaysia:** Employment income is deemed to be derived from Malaysia in the event that the employment is discharged in Malaysia.

**Attributable Leave Pay:** Leave pay is deemed to be derived from Malaysia in the event that the leave is attributable to the employment exercised in Malaysia.

**Incidental Overseas Duties:** Employment income in respect to overseas duties or assignments is taxable in Malaysia provided that the duties outside Malaysia do not serve an independent purpose but are connected to the Malaysian employment.

**Malaysian Company Director:** A director of a Malaysian resident company need not physically exercise any of the duties of his or her office in Malaysia and yet the remuneration he or she receives will be deemed to be from a Malaysian source.

**Malaysian Operated Ship or Aircraft:** Applicable upon employment exercised aboard a ship or aircraft used in a business operated by a Malaysian resident.

**Employment in Public Service or Statutory Authority Outside Malaysia:**

Income of a Malaysian citizen attributable to employment exercised in the public service or in a statutory authority outside Malaysia is deemed to be derived from Malaysia.

In regard to the types of employment income, section 13(1) (a) to 13(1) (e) of the Income Tax Act 1967 grouped employment incomes into five categories:

**Monetary or near monetary benefits:** Any wages, salary, remuneration, leave pay, fee, commission, bonus, gratuity, perquisite or allowance in respect of having or exercising employment.

**Benefits-In-Kind (BIK):** Benefits or amenities which are not convertible into money and which are provided for the employee by or on behalf of his employer. Examples include car, fuel, driver, household furnishings and appliances, mobile phone, gardener and corporate membership in recreational clubs.

**Unfurnished accommodation:** The value of any unfurnished living accommodation in Malaysia provided by an employer to his employee.

**Refund from unapproved funds:** Funds are not approved by the Director-General under section 150 of the Income Tax Act 1967.

**Compensation for loss of office and entering into restrictive covenants.**

The types of employment income stated above must be reported in the employee's tax return.



## 2. 3 The Differences between Business Income and Employment Income for Income Tax Purposes

The difference between business income and employment income when it comes to tax is employment income is taxed under the section 4(b) and business income is taxed under section 4(a)

Table below shows the differences of business income and employment income that subject to income tax.

Subject to income tax

Business Income

Employment Income

Business income derived from Malaysia for any period of time.

Exercises an employment in Malaysia for any period of time

Tax is based on accounting period

Tax is based on calendar period

Depreciation on fixed assets

Performs duties outside Malaysia which are incidental to his employment in Malaysia

Include sole proprietor, private limited companies

Is employed to work on board an aircraft or ship operated by a person who is resident in Malaysia

Table below shows differences of business income and employment income that is exempted from income tax.

Exempted from income tax

Business Income

Employment Income

All expenses and outgoings incurred wholly and exclusively in the production of the business income

Leave passages provided to the employee, his spouse and children up to a maximum of RM3, 000 for one overseas trip and up to a maximum of three local trips per year

Capital allowances

Retirement gratuities (on meeting certain conditions)

Specific provision of bad debts

Employees Provident Fund withdrawals

Interest on loan used in the business

Dental or medical treatment or child care benefit

Rental in respect of any land or building occupied

Foreign employment income remitted back into Malaysia.

Repairs and maintenance

Non- resident income that have exercised the employment for period not exceeding 60 days.

Many people try to cheat on their status of employee to any profession that is entitled to a business income, because they assumed that they can reduce their taxes more compared to being an employee. Tom Langford (2004) listed out several test by the courts in Canada to determine a person work status. First, they will look at the degree of control an employer has over the work to be performed. Second, the courts will examine whether the person, and the person's work, is an integral part of the employer's business, or whether it is just an accessory to the employer's business. Third, they examined the tools and equipment is required on the job site to complete the work. Fourth, they analyzed whether the person has the chance of making a profit and the risk of loss. And finally, they investigated whether the person has been hired to achieve a specific result, or rather than merely placing his or her services at the disposal of the employer for a period of time without reference to a specified result.

If, upon a review of these aspects, it can be determined that the person is from a business element services, the expenses which that person wishes to deduct from income must still meet the requirements for deductibility. If the person has claimed to be from business element services but later fails to meet the requirements when challenged by the courts, there may be reassessed taxes, interest, and possibly penalties on the amounts claimed as

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deductions from income. Therefore, it is highly recommended that a person seek professional advice regarding their particular circumstances and needs before attempting to make a change in their work status.

### 3. 1 What is Resident Individual?

Status of resident in Malaysia is examined according to Section 7 Income Tax (ITA) 1967 which had reatest by Inland Revenue Board (IRB). “ It should not confused with the permanent resident status granted to individuals by the Home Affairs Ministry” according to the chapter 2 “ Essential Guide to Personal Income Tax in Malaysia” a 2009th edition book by Adam Malik et all. By right, for individual to had a resident status in a year of assessment (year the income tax are reatest), individual must examine the section one after the other from Section 7 (1) (a) until Section 7 (1) (d).

The diagram shows how an individual can be granted as a resident, IRB will examined it by reference to the number of days an individual was in Malaysia by desirable quality of Section 7 of the Act. In the occurrence that if an individual does not fall under any of these circumstances in a particular basis year, therefore that individual are not resident for that basis year.

#### 3. 1. 1 Benefit for Resident

Being gratifying a resident status may earn plentiful of benefit for the year of assessment. The key benefit as resident are

Personal relief: assumption from total income in arriving at chargeable income. (table 1 as per attach)

Income tax rate: As for non-resident individual, they are subjected to flat rate of 28%. Though the resident individuals are subjected to scaled income tax rate starting with 1% on the second RM 2500 and ending the scaled income tax with 28% on the income exceeding RM 250000, an example taken from “ Essential Guide to Personal Income Tax in Malaysia” .(table 2 as per attach)

Rebate: Resident individual have right to plentiful tax rebate subject to certain condition being satisfied. In the event that the aggregate values of the rebates exceed the individual (residual) income charged, the excess will be a permanent loss. (table 3 as per attach)

Exemption: Resident can be exempted from tax only in the hands of resident individuals, most likely fall in royalties from literary or artistic work, income from cultural performance approved by Minister and / or income from musical composition. (table 4 as per attach)

Table 1 : Personal relief for individual (Resident) base year 2009. Sources from [http://www.hasil.gov.my/lhdnv3e/individuIndex.jsp?process=21000&menu=34&expandable=1&pg\\_title=Tax%20Relief](http://www.hasil.gov.my/lhdnv3e/individuIndex.jsp?process=21000&menu=34&expandable=1&pg_title=Tax%20Relief)

No.

Individual Relief Types

Amount (RM)

1

Self and Dependent

8, 000

2

Medical expenses for parents

5, 000 (Limited)

3

Basic supporting equipment

5, 000 (Limited)

4

Disabled Individual

6, 000

5

Education Fees (Individual)

5, 000 (Limited)

6

Medical expenses for serious diseases

5, 000 (Limited)

7

Complete medical examination

5, 00 (Limited)

8

Purchase of books, journals and magazines

1, 000 (Limited)

9

Purchase of personal computer

3, 000 (Limited)

10

Net saving in SSPN's scheme

3, 000 (Limited)

11

Purchase of sport equipment for sport activities

300 (Limited)

12

Interest expended to finance purchase of residential property. Relief of up to RM10000 a year for three consecutive years from the first year the interest is paid.

Subject to the following conditions:

(i) the taxpayer is a Malaysian citizen and a resident;

(ii) limited to one residential unit;

(iii) the sale and purchase agreement is signed between 10th March 2009

and 31st December 2010; and

(iv) the residential property is not rented out.

Where:

(a) 2 or more individuals are eligible to claim relief for the same property ;

and

(b) total interest expended by those individuals exceeds the allowable amount for that year ,

Each individual is allowed an amount of relief for each year based on the following formula:

$A \times B$

C

where;

A = total interest allowable in the relevant year;

B = total interest expended by the relevant individual in the relevant year;



C = total interest expended by all the individuals.

10, 000 (Limited)

13

Husband/Wife/Alimony Payments

3, 000 (Limited)

14

Disable Wife/Husband

3, 500

15

Ordinary Child relief

1, 000

16

Child age 18 years old and above, not married and receiving full-time tertiary education

1, 000

17

Child age 18 years old and above, not married and pursuing diplomas or above qualification in Malaysia @ bachelor degree or above outside Malaysia

in program and in Higher Education Institute that is accredited by related Government authorities

4, 000

18

Disabled child

Additional exemption of RM4, 000 disable child age 18 years old and above, not married and pursuing diplomas or above qualification in Malaysia @ bachelor degree or above outside Malaysia in program and in Higher Education Institute that is accredited by related Government authorities

5, 000

19

Life insurance dan EPF

6, 000 (Limited)

20

Insurance premium for education or medical benefit

3, 000 (Limited)

Table 2: Income tax rate for individual (Resident) base year 2009. Sources from [http://www.hasil.gov.my/lhdnv3e/individuIndex.jsp?process=21000&menu=13&expandable=1&pg\\_title=Income%20Tax%20Rate](http://www.hasil.gov.my/lhdnv3e/individuIndex.jsp?process=21000&menu=13&expandable=1&pg_title=Income%20Tax%20Rate)

Chargeable Income

Calculations (RM)

Rate %

Tax(RM)

0-2500

On the First 2, 500

0

0

2, 501-5, 000

Next 2, 500

1

25

5, 001-10, 000

On the First 5, 000

Next 5, 000

3

25

150

10, 001-20, 000

On the First 10, 000

Next 10, 000

3

175

300

20, 001-35, 000

On the First 20, 000

Next 15, 000

7

475

1, 050

35, 001-50, 000

On the First 35, 000

Next 15, 000

12

1, 525

1, 800

50, 001-70, 000

On the First 50, 000

Next 20, 000

19

3, 325

3, 800

70, 001-100, 000

On the First 70, 000

Next 30, 000

24

7, 125

7, 200

100, 001-150, 000

On the First 100, 000

Next 50, 000

26

14, 325

13, 000

150, 001-250, 000

On the First 150, 000

Next 100, 000

26

27, 325

26, 000

More 250, 000

On the First 250, 000

Next RM

26

53, 325

.....

Table 3: Rebate for individual (Resident) base year 2009. Sources from [http://www.hasil.gov.my/lhdnv3e/individuIndex.jsp?process=21000&menu=42&expandable=1&pg\\_title=Tax%20Rebate](http://www.hasil.gov.my/lhdnv3e/individuIndex.jsp?process=21000&menu=42&expandable=1&pg_title=Tax%20Rebate)

Income tax rebates for resident individual with Chargeable Income Less than RM35, 000

Year Of Assessment

2001 - 2008

Year Of Assessment

2009 Onwards

No

Tax Rebate

(RM)

(RM)

a

Separate Assessment

Wife

Husband

—

350

350

—

400

400

b

Combined Assessment

Wife

Husband

—

350

350

—

400

400

Total

700

800

b

Assessment Where Husband Or Wife Does Not Has Any Total Income



Wife

Husband

—

350

350

—

400

400

Total

700

800

Other tax Rebates

No

Tax Rebate

(RM)

a

Zakat/Fitrah

Subject to the maximum of tax charged

b

Fess/Levy on

Foreign Workers

Subject to the maximum of tax charged

Table 4: Tax exemption for an individual (Resident). Sources from

[http://www.hasil.gov.my/lhdnv3e/individuIndex.jsp?process=21000&menu=2&expandable=1&pg\\_title=Tax%20Exemptions](http://www.hasil.gov.my/lhdnv3e/individuIndex.jsp?process=21000&menu=2&expandable=1&pg_title=Tax%20Exemptions)

3. 2 How a resident individual is charged under income tax if he derives income from employment and businesses.

Malaysia income tax is 'territorial'. This mean all revenue income derived or accruing from Malaysia is subject to tax unless specifically exempted. More over, foreign source incomes remitted into Malaysia are exempted from being tax. The resident individual which had derive their income from employment and business, by right are be delineated by Section 4 of the income tax act 1967. According to Inland Revenue Board, the residual individual may need to commence a business in the year of assessment. The residual individual also has to declare their income using

Form B. If the residual individual has received Form BE, have it changed to Form B at the nearest branch or at the Processing Centre or

E-Filing. Select e-B although previously income has been declared in e-BE thru online application.

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All the forms may be downloaded from the Inland Revenue Board website or collected from the head office.

The way to determine the individual income before a tax is determine the exact income and then subtract personal debt. The most formula using is Individual income - Personal Debt = residual Income. Most of the financial institution makes an assessment on individual residual income. However if there is a case where an individual would like to obtain a loan, they may need to determines how much money as the individual had left after paying off their entire obligation.

#### 4. 1 Conclusion

Employees in relation to an employment according to Section 2 of the Income Tax Act 1967 are defined as where the relationship of master and servant subsists, the servant. Second determination is where that relationship does not subsist the holder of the appointment or office which constitutes the employment. Beside that, employees a paid as salaries for service rendered. Nowadays, there are a number of employment arrangements available, including full time employment, part time employment, casual employment, fixed term or contract employment, apprenticeships, traineeships, and probationary works. The employee's duties sort of link together with their employer's business. An employer is defined in Section 2 of the Income Tax Act (ITA) 1967. In general, employer means the party that pays remuneration to the employees, where there is an " employer-employee" relationship. The business receipts are what you called a business income. According to Section 4(a) of Income Tax Act 1967,

states that business income is subject to income tax provided that they are revenue in nature and derived from Malaysia. Foreign source income remitted into Malaysia, on the other hand, is exempted from tax. Contracts are concluded outside Malaysia Services are rendered outside Malaysia. The above factors help us determine a clearer definition of business income and in what aspects business income is subjected or exempted from income tax. Receipts derived from one of the factors that defining employment is what you called an employment income.

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The types of employment income is classified into section 13(1) (a) to 13(1) (e) of the Income Tax Act 1967 grouped employment incomes into five categories. The types of employment income stated above must be reported in the employee's tax return. The difference between business income and employment income when it comes to tax is both are tax under different section and based on different period system. The high lights of benefit being as resident individual are personal relief, assumption from total income in arriving at chargeable income. Income tax rate, as for non-

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resident individual, they are subjected to flat rate of 28%. Though rebate, resident individual have right to plentiful tax rebate subject to certain condition being satisfied.