

# [Personal income tax system in malaysia](https://assignbuster.com/personal-income-tax-system-in-malaysia/)

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A tax is a financial charge or other levy imposed upon a taxpayer that known as an individual or legal entity by a state or the functional equivalent of a state such thatfailureto pay is punishable by law. Taxation is a compulsory levy that the government of a country willfinancetheir expenditure by imposing charge to the persons, individuals, businesses and other bodies to allows the government providemoneyneeded for them to run their operation and to achieve economic objective of the government. Tax is actually not meant to be paid by all people but focuses towards some class of people.

As for personal income tax, it need to be paid by the person who earns income up to certain amount and for corporate tax, it imposed on the corporate entity that makes profit from the businesses. In achieving the economic objective, government will take some action such as reduction in taxable person income by the amount paid as the interest on home mortgage loans which will generates more jobs, encourage public to purchase a local produce, reducing inflation and discourage the consumption of certain goods.

In Malaysia tax system, it comprises of corporate and personal income tax, custom duty and local tax. The personal income tax is liable for the individual who has income that derived from Malaysia or received in Malaysia from outside Malaysia for a year of assessment. The tax will be imposed to the resident and non-resident individual in different ways.

The resident individual will subject to income tax derived from Malaysia and income received in Malaysia for outside Malaysia whereas non-resident individual will be subject to income tax accruing in or derived from Malaysia. In contrast, non-resident is subject to tax at a flat rate of 25%. In additional, income that received by an individual in Malaysia which income is derived from outside Malaysia is exempted from tax with effect from the year of assessment 2004.

Under section 4 of Income Tax Act 1967, income that is subject to tax comprises of Section 4(1)(a) which is gains from a business, Section 4(1)(b) which is gains from an employment, Section 4(1)(c) which is dividends, interest or discounts, Section 4(1)(d) which is rent, royalties or premiums, Section 4(1)(e) which is pension, annuities or other periodical payment which are not falling under any of the foregoing paragraph and lastly under Section 4(1)(f) gains that not falling under any of the foregoing paragraphs. Besides that, non-resident individual are also

subject to tax of the amount paid in consideration of a service rendered by the person or employee for the use of property of any plant, machinery or other apparatus purchased from such person. Under capital gains, it will be tax in the form of real property gains tax. This tax is arising from disposal of real property in Malaysia.

Real property gain tax is known as tax on disposal of shares in real property companies which owns shares defined value of such asset not less than 75% of the company's total tangible assets.

Starting from 2010, disposal of real properties that are held for 5 years and below are subject to real property gain tax which the tax rate is 5%. In contrast, for the employment income, employer is required to deduct tax monthly from their employee’s remuneration and submit it to the Inland Revenue Board of Malaysia.

For corporate income tax, resident companies are subject to tax on income accruing in or derived from Malaysia. Income that received in Malaysia from outside Malaysia is exempted from tax except for the companies that involved on the business of insurance, banking, sea or air transportation.

Non-resident companies are subject to tax on income accruing in or derived from Malaysia only. Incomes that are derived from outside Malaysia which is foreign income will be non-taxable income. Business income of non-residents is subject to tax once it derived through a permanent establishment in Malaysia.

There is a self-assessment in the tax system in Malaysia which required individuals to file and pay their tax based on the time requirement. An individual must file and pay their tax if they has a chargeable income for a year of assessment and has no chargeable income for the year of assessment.

An individual who has a chargeable income for the year of assessment, they required to furnish a return for the immediately preceding year and have furnished a return for the immediate preceding year. Under Income Tax Act 1967 of Section 2 describe that royalty as any sums paid as right to use the artistic, patents, copyright, design, trademarks, films where such films are to be used in Malaysia. A person who is liable to pay a royalty that has a Malaysian source to an individual who is not known to him to be a resident in Malaysia and to a company, partnership or any other body of persons who does not carry a business in Malaysia.

Besides that, the royalty is said to be derived from Malaysia if theresponsibilityfor the payment lies with a resident of Malaysia and the responsibility for the payment lies between the government and state government itself.

There is a term of local tax in Malaysia which refers to as the property tax collected by the local authorities for the provision of service to the residents. The property tax is levied on all property such as agricultural, factories, residential and shops located in the areas under jurisdiction of local authorities.

Furthermore, the rate of the tax collected is different from one local government to another and it is also different in form of the property rights. Question 1(B): Examine the taxation needs of the present times (locally and internationally).

So far Malaysia is using an income based direct tax for the purpose of taxation of goods and services in the country and with international transactions. So, isn’t it better for the country to switch to a consumption based indirect taxation?

First of all, what is the difference between direct and indirect tax. The difference between a direct and indirect tax is a challenging issue. It depends on whether it is viewed on the economic way or on the legal way. In this case the interest is given to the economic view only.

Based on economic perspective, a direct tax will refer to any levy that is both imposed and collected on a specific group of people or organizations. An example of direct taxation would be income taxes that are collected from the people who actually earn their income.

In the opposite, indirect taxes are collected from someone or some organization other than the person or entity that would normally be responsible for the taxes; in other words, an indirect tax is technically an income tax levied against people, corporations, and other legal entities.

A sales tax, for instance, would not be considered a direct tax because the money is collected from merchants, not from the people who actually pay the tax (the consumers). A goods and services tax in Malaysia (GST), a value added tax, was scheduled to be implemented by the government during the third quarter of 2011.

Its purpose is to replace the sales and service tax which has been used in the country for several decades. The government is seeking additional revenue to offset its budget deficit and reduce its dependence on revenue from Petronas, Malaysia's state-owned oil company.

They estimated to four-percent the tax rate in order to replace a sales-and-service tax of between five and ten percent. The Goods and Services Tax Bill 2009 was tabled for its first reading at the Dewan Rakyat (the lower house of the Malaysian parliament) on 16 December 2009.

It was delayed amid mounting criticism. The government responded by asserting that the tax on oil income will not be sustainable in the future. National Consumer Complaints Centre head Muhammad Sha’ani Abdullah has said, “ The government should create more awareness on what the GST is.

The public cannot be blamed for their lack of understanding, and thus, their fears”. Sha’ani says that the GST will improve accounting, reduce tax fraud, and facilitate enforcement of the upcoming Anti-Profiteering Act.

Muslim Consumer Association of Malaysia leader Datuk Dr. Ma’amor Osman said the GST could help end dishonest business practices, but expressed concern about how the tax would be applied to medical products and services. A group leading the campaign against the GST, Protes which objects to the GST because of concerns about its effects on low-income Malaysians, cancelled a planned protest but has stated that they will continue to agitate against the legislation Difference between Malaysian taxation and other countries, they need to harmonize.

Most of the countries in the world currently use income based taxation. Those countries use two systems for taxation purpose: territorial or residential. Malaysia is one of the few countries in the world using territory based taxation. The tax is applied mainly over local income, in other words, income from a source inside the country. Malaysia operates under a Self-Assessment System (SAS) and income is taxed on a territorial basis.

Income tax in Malaysia is imposed on income accruing in, or derived from, Malaysia except for income of resident companies carrying on a business of air or sea transport, banking or insurance, which are taxed on a worldwide basis. Foreign-source income received in Malaysia is not taxable.

In the residential system, residents of the country are taxed on their worldwide income (local and foreign). This difference of tax systems may overlap some time, giving rise to a taxation issue. Some taxpayer may be taxed more than once.

There is another group, the United States which applies tax based on citizenship. There will be taxation conflict at the international level. For instance Malaysia and Singapore have a tax agreement in order to avoid double taxation for the same person and the same income between the two countries.

Based on the preceding, the taxation system in Malaysia should be reviewed in order to simplify the international transactions as well as multinational operations between the country and others. This could help to ease the business transactions both locally and internationally.

Taxation used as a tool to attract investors which useful to note that the Malaysian Government, in trying to attract foreign direct investment, is amiable to consider pre-packaged incentives, Factors such as the size of investment, level of spin-off, employment opportunities, andtechnologytransfer, whether of national and strategic importance will play a role for granting of the incentive. Malaysia is experiencing an increasing inflow of investors from around the world because of various reasons. One of the main reasons is the tax incentive provided by the government to attract foreign capital and know-how.

At this point the country is doing very well to gain competitive attractiveness. The tax legislature in Malaysia keeps updating the tax law very often to follow the country’s development need. Switch tax policy is a need as in a multi-stage, broad-based Goods and Service tax (GST) has been announced by the Malaysian Government to replace the existing single stage sales tax and service tax. The implementation date remains unannounced at this juncture. The Malaysian tax specialists deemed more beneficial to make this switch.

Experts also have argued that complexities due to timing and inflation adjustment should be avoided. To do so, the authorities need to switch the taxation system from an income based one to a consumption based one. Under such a system all business purchases would be deducted immediately.

Borrowing in excess of investment would be added to income, and lending would be subtracted; the resulting tax base would be consumption. Through the tax saving resulting from expensing, the government, in effect, becomes a partner in all investments; the revenues it subsequently receives are best seen as the return on its investment.

A consumption-based tax imposes no burden on income from marginal investments, because the private investor keeps all of the income relating to his share of the investment. As a result, such a tax does not favour present consumption over saving for future consumption, as the income tax does.

Some economists view the flat tax as an alternative that is even simpler than consumption-based taxation but would achieve similar economic effects. It works by exempting most capital income from taxation at the individual level that is, only labor income is taxed.

This proposal, like consumption-based taxation, suffers from the loss of progressivity those results when the tax on most capital income is eliminated. No country uses either of these consumption-based direct taxes. To sum up, the Malaysian authorities has some changes to make in order to improve its own tax system and support the economic growth of the country.

The current tax system is not bad or unproductive, but just to improve through the establishment of a tax policy that is more or less similar to at least the neighbouring countries or least extend the bilateral and multilateral tax agreement with the business partners, as well as the foreign investors.

It is also highly advisable deepen the analysis about the implementation of the consumption based taxation to determine whether the switch could be beneficial. Question 1(C): Discuss whether system of tax on goods and services is now timely and appropriate for Malaysia.

Goods and services tax (GST) is known as a consumption tax based on the value-added concept. It imposed on sales of goods and services in every production. The tax consumption which the indirect tax charged towards importations and on the value added to goods and services sold by one business to another, or to the end consumer.

The new tax system of GST is considered as more efficient tax system. The implementation of GST replaces the current Malaysian service tax and sales tax. Sales tax is a form of indirect taxation which imposed on consumers and collected by business entities while service tax is a form of indirect tax imposed on specified services called as taxable services when the services are provided to the consumer at the time. There are lots of arguments arrived on the introduction of GST in Malaysia especially from various parties who is the taxpayer whether it burden the peoples when being implement.

GST have more comprehensive, transparent tax system. It inclusive of the manufacturing and distribution stages as well as providing a tax credit claim for GST paid on business inputs while the sales tax is imposed only at the manufacturing stage when the goods are manufactured or imported.

Thus, the GST will overcome the various weaknesses inherent in the present consumption tax system such as double tax, leakages thru transfer pricing and more. The government implement GST as part of their tax reform programme.

The objective of this new system, GST is to enhance the capability, effectiveness and transparency of tax administration and management. GST covers all types of goods & services sold to Malaysian & non-Malaysian residents except for common commodities.

Government expected that the consumers will have benefit from the price reduction in most of the goods and services which has cheaper services. As a consumer, the GST will affect us as the prices of goods and services which currently have little or no taxes will increase slightly.

Although there will be slightly increase in term of pricing, the government also has decided that 40 basic goods and services will be exempted from the GST such as basic foodstuff, residential accommodation, education, healthservices, communication, water and electricity, public transportation, hardware and maintenance and more.

There are various types of businesses that charged to GST. GST is charged and collected on all taxable goods and services produced in the country including imports where they need to pay the GST at the time of importation.

To business supplying the good and services, they need to pay within one month at the end of taxable period, it depending towards the classification that done by the GST authorities. Thus, businesses registered under GST can charge and collect GST.

The social and pricing impact studies conducted by the Ministry of Finance indicated that the suitable GST rate is in the range of 4% of value added to good and services at each stage of production. Value added in this system basically is the mark-up in arriving at the selling price of a product and service.

The rate is indicated as a standard rate which is expected to give benefits and to reduce the unduly burden of the rakyat and consumers especially to whom that fall in the lower income group. A business that have annual turnover that is more than RM500, 000 needs to register for GST, this is to ensure that the small businesses are free from GST. The registration can be done by manually or online within 28days from the end of the month where the threshold is reached.

Towards businesses that are not reached the threshold, they can voluntarily apply to be registered under the GST and the businesses must remain in the system for at least 2 years followed in the policy. If the government implement it in Malaysia, they will provide a sufficient time for business and industries to make them ready as GST is the new tax system.

It will be around 18 to 24 months as various businesses have different types of primary activities in their businesses. Lots of preparation need to be done including preparing their business computer system, hardware and software to get ready for this implementation.

Who will responsible to handle the GST accounting and GST taxation as it involved setting up business records, calculation of GST taxes and more. Training is needed either done by the government or by sending the staff for external training as this will increase the rate of readiness towards this implementation.

In additional, the issues on transitional of GST tax need to be study as to avoid the double taxation and disruption. Therefore, they need to understand the detailed rules and consider how GST would apply to their own business operations to avoid any problems occur in future after the system is being implemented.

Corruption is not a rare thing in Malaysia as businesses has already included corruption prices in goods & services. How does that not reflect additional costs to consumers? Therefore, the government need to take step in controlling the prices.

They need to ensure that the businesses do not take advantage of the GST implementation to increase prices of goods to make excessive profits. A Heavier fines and penalties will be imposed to make sure that the businesses comply with the rules and procedures formulated. Towards dealing with the issues relating to non-compliance and fraud, various approaches will be used by the government.

A risk assessment programme will be used to identify types of businesses and persons with high tendency to commit non-compliance and fraud. Moreover, a comprehensive audit programmes is one of the programme that being used to all business and this programme also will be used in the system to fight non-compliance and fraud cases.

Thus, a business records and accounts need to be audit by independence auditor to give a true and fair view of thefinancial statement. Prime Minister has guaranteed that there is no inflation but with the introduction of GST, the chain of passing the cost will end up usually at the hands of consumers.

The multiple stage tax of GST would rise up the final consumption price which might lead to inflation in short while. Malaysia economic would be more conservatives and tided to move forward for low income workers with a high living cost that can be seen in present time.

A good approach can be seen when the government learn and get good references from countries that impose GST such as Singapore and Thailand before implemented the tax scheme. Last but not least, the result of GST implementation could not be seen in this current time but they need to ensure that the GST does not burden the people, especially the lower-income group.

As a business taxpayer they need to be alert and aware regarding this new implementation. Organised seminar or workshop need to be attend to have a better understanding and at the same time will reduce any conflict occur. GST awareness and education programmes need to be conducted on an on-going basis until the GST is implemented and the answer from the survey can help the government to make decision and a proper preparation need to be done as in computer system or in other medium that GST will be used in future. Therefore, the government need to give businesses ample time to be ready for GST implementation.