CHAPTER II

STRUCTURE OF INLAND REVENUE

A Brief History

During the last quarter of the 19th century the former feudal system of taxation[1] was replaced by a more rational system of taxation. The system, which began in the Straits Settlements was progressively applied to the Malay States and we thus see a completely new concept coming into existence. But apart from the abortive "War Tax" which was imposed shortly before the Second World War, and terminated with that event, there was no previous tax which had any strong affinity to modern income tax. In the modern sense income tax was brought into effect from the 1st of January 1948 by the Income Tax Ordinance No. 48 of 1947. Since then there has been a number of Amending Acts and Ordinances. The system which has been adopted, generally has 2 basic principles:[2]

1) Parliament alone can authorise taxation i.e. the supply of money should be voted annually.

2) And the executive should apply the money so voted solely to implement the general intentions of Parliament.

Furthermore with the exception of Muslim religions fees and levies, all revenue received must be paid into a Consolidated Fund maintained by the Federal and State governments.

For our purpose, we shall be interested only in the rate structure of the other territories of Malaysia prior to the Malaysia Finance Act of 1965; and the harmonisation affected after the formation of Malaysia in September 1963.

Harmonisation of Income Tax Laws

According to the Income Tax Ordinance of 1947, tax is chargeable on all income accruing or derived in the Federation of Malaya, or received in the Federation from outside the Federation. The situation in the Malaysian context is almost the same. In the Federation,

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[1] Banchi, krah, and serai - Year Book, Federation of Malaya, Government Printer. Any issue.

[2] Malaysia - The Federal Constitution, op. cit., Article 97, p. 56.

furthermore, there is only one income tax - it applies to a taxpayer's aggregate income (including that of his wife). And the same reliefs and rates of tax are operative for all types of income.[3] Income tax is not charged on prizes (as in the case of Social Welfare Lotteries) nor is there any "wealth-tax". In general liability to tax commences when a source of income is acquired and ceases when the source of income terminates. Unlike in some other countries, the assessment year is also the calendar year i.e. it runs from 1st January to 31st December except in the case of Sabah where it is from 1st July to 30th June.

As from 1963 the "Pay As You Earn" PAYE system was introduced. For 1965 the scheme was extended to employees whose income tax amounted to $50 per month (i.e. $600 per year) or more and it was then hoped that it would be further extended in due course. A provision for non-PAYE cases was allowed whereby employees not within the scheme may either pay in one sum the tax charged or make voluntary arrangements for payment by instalments.

In Malaysia, there are three classifications[4] of income for purposes of taxation. In the first place "Statutory Income" is the income as determined by the Income Tax Ordinance. Normally for any year it is based on the income of the preceding year; but there are special rules for the commencing and ending years. "Assessable Income" is that amount of the statutory income of a particular year, less deductions, losses and charitable donations. "Chargeable Income" is the assessable income less personal allowances. Since these are only applicable to individuals it follows that in the case of companies the "assessable income" and "chargeable income" is the same.

In the aggregation of income we have to note other major changes in the structure of personal taxation. Prior to the introduction of the 1965 Supply Bill, business income in Sarawak, was treated separately and therefore no personal reliefs was provided. Such income was charged at a flat rate of 10% subject to the deduction of a fixed allowance of $5,000 which diminished when the income exceeded $37,000 and finally disappeared at $42,000. Such a system may "not be unattractive to a bachelor".[5] But it is "somewhat harsh when the business is carried on by a partnership of several partners with wives and children".[6] Therefore, the Finance Minister proposed, as from 1st

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[3]Relief, however, is given for earned income at the rate of 1/10 of earned income with a maximum limit of $1,000.

[4]Rolt, S.E. - An Intermediate Course - Income Tax in Singapore and the States of Malaya, Craftsman Press Ltd. Singapore, 1964, Part 5. Also in C.T. Edwards Article "The Rate Structure of Personal Income Taxation in Malaya", Kajian Ekonomi Malaysia, Vol. I, No. 2, Dec. 1964, p. 37.

[5]Supply Bill, 1965, In Formation Department Malaysia, p. 39.

[6]Ibid.

January 1965, to harmonise this by introducing personal reliefs in the Sarawak Tax Structure and aggregation of income was done on the same basis as in Singapore, Malaya and Sabah.

In the case of company taxation, with the exception of Sabah, company profits were taxed at 40% whether profits were distributed or not. In the case of Sabah tax provisions for non-pioneer companies permitted companies to be charged at 20% on undistributed income of companies (charging a further 20% making 40% in all, when the income was distributed).[7] This anomaly was, very rightly, removed in the 1965 Supply Bill. The tax was harmonised for the whole of Malaysia, when the incomes of Sabah companies were to be taxed at the uniform rate of 40%. The Malaysia Act: Modification of Laws (Income Tax) Order 1964 provides that as from 1965, a company would be taxed on its Malaysian income once only i.e. in the territory of residence on income derived elsewhere. Before 1964, taxes on Trustees, executors and non-resident individuals and Hindu Joint Families was 30%. As from 1964, the rate was increased to 40%.[8]

As far as earned income relief was concerned, the maximum allowance in Malaya and Singapore was $1,000 of the earned income; and the rate in the case of Malaya was 1/10 of the earned income and 1/15 in Singapore. From 1965,[9] the Finance Minister, in his attempt at harmonising the rate had laid an effective limit for Malaya and Singapore at 10% of earned income. However, there is no earned income relief in Sabah and Sarawak. But it should be extended to these states in the near future if final harmonisation is a desired objective.

<u>Scope and Basis of Assessment</u>

(1) <u>Investment Income</u>

(a) In Malaysia, all types of investment income (i.e. income derived from investment) is liable to income tax. It includes among others such items as interest on money deposited in a bank, money lent, income from ownership of property which is let, and income from investment in shares and securities.

(b) Dividend income, on the other hand, is dealt with on a different basis from other types of income. If the dividuals are from local companies[10] the gross amount of any dividends received is included in a taxpayer's income for the purpose of calculating his total income

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[7] Tax Changes Within Malaysia, Information Department, Nov. 1964, p. 2.

[8] Income Tax Act, 1964, No. 21 of 1964, Government Printer.

[9] 1965 Supply Bill, op. cit., pp. 38-39.

[10] Includes Malayan Unit Trust Dividends.

tax liability. But tax at the rate of 40% is withheld at source from distribution. And this tax deducted from the dividend is allowed as a credit against the total tax payable by the taxpayer. Therefore unless a taxpayer is liable to income tax at rates above 40%, he obtains a substantial benefit from this treatment because the dividend tax of 40% reduces the tax chargeable on his other income. If as may be, where a large part of a person's income is Malaysian dividends, the excess tax deducted is refunded. To illustrate let us take an example. If a person A's gross dividends are $1,000 and his other chargeable income is $5,000, then tax would be charged on $6,000. But 40% of $1,000 would be deducted at source i.e. $400. Therefore since he is charged on $6,000, he should be paying $495. But the $400 deducted is allowed as a credit and consequently the taxpayer only pays $95 as tax.

In the case of foreign dividends, the taxpayer is chargeable with tax on such of these received in Malaysia. In the case of countries which have Double Taxation Agreement,[11] an allowance in respect of the foreign government's taxation is allowed. Investment income, other than dividends, face no difference in assessment. They come under income tax liability from the time the income first accrues to the time when the source is disposed off.

(2) Earned Income

Income from trades, businesses, professions, vocations and employments is assessable for income tax from the date the source commences to the day it ceases. We shall be dealing with it later in the chapter.

Deductions in Arriving at Assessable Income[12]

(a) Expenditure: A taxpayer is entitled to deduct from his gross income expenditure which is "wholly and exclusively incurred in producing that income".[13] The main ones are:

i) Interest on money borrowed and utilised in producing the income.

ii) Rents payable for premises used for trade, business or profession for acquiring the income.

iii) The cost of repairs (but this item excludes expenditure on alterations, extensions and

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[11] United Kingdom, Norway, Sweden, Denmark and recently Singapore.

[12] For the 2 classification of "Income", see Federation of Malaya, Income Tax Ordinance 1947, Government Press 1961, Part V.

[13] Personal Income Tax in the Federation of Malaya, Government Printer, 1965, p. 4, para. 30.

improvements).

iv) Bad or doubtful debts (during the trading period).

v) Obligatory contributions by an employer (like CPF and EPF) to employees who help in producing the income. To avoid giving a complete list of the items,[14] we can generally say that it also includes, "expenditure incurred wholly and exclusively in producing particular types of income".[15]

(b) Capital Expenditure: Although expenditure on alterations, or improvement are not deductible in arriving at the assessable income special "capital allowances" are provided for in respect of many types of capital expenditure. This we shall consider when we discuss "Depreciation" in the section "Trades, Businesses, Professions and Vocations".

Deductions From Assessable Income

(a) Loss in Trade, Business, or Profession. The different Ordinances provide for deduction of a loss incurred during the year of assessment in any trade, business, profession or vocation. It means that "only loses incurred in a trade, business, profession or vocation can rank for relief".[16] Other losses such as loss on rental property, do not rank for relief.

(b) Donations to Public Institutions, etc.: In Malaya, and generally in Malaysia, a taxpayer may claim relief from income tax for gifts of money which are approved under the various Income Tax Ordinances. Some of these donations are the National Mosque Fund; the National Monument Fund, the Red Cross and the Lady Templer's Tuberculosis Hospital Fund. The relief is for the full amount of the donation. Such relief is also accorded for these donations to both the State and Central governments. Though there is no limit on the deductions claimed, there is no provision for carrying forward the excess (when donations exceed assessable income) to future years.

(c) Reliefs:

i) Earned Income Relief. This relief is deductible

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[14]This can be found in the different Income Tax Ordinances.

[15]Personal Income Tax in the Federation of Malaya, op. cit., pp. 4 and 5.

[16]Relt, op. cit., p. 6.

only on earned income.[17] A similar provision exists in Singapore. This is claimed as reasonable by the Minister of Finance, "to ensure that income from personal exertion is more favourably treated than income from investment which accrues without exertion on the part of the recipient."[18] At present the rate is 1/10 of earned income with a maximum of $1,000. But, this is only operative in the States of Malaya and Singapore.

ii) Personal Reliefs. These are given on the basis of a taxpayer's circumstances. At present, the personal relief for a single person (defined as an unmarried individual, a widower or a widow) is $2,000 in Malaya and Singapore. In the case of Sabah and Sarawak there is a relief of $3,000 - a $1,000 discrepancy is evident. A married person in Singapore and Malaya has a further relief of $1,000 for his wife. As in the case of unmarried individual relief there is a difference in the relief in Sabah and Sarawak for a married person. In these two states, before 1965, the relief was $2,400 in Sabah and $2,000 in Sarawak. From 1965 there has been an alteration[19] of wife's allowance given in Sabah to harmonise with Sarawak and the present rate is $2,000 in both the Borneo States. Furthermore, Sabah had a relief of $2,400 for dependent parents. But with the changes in 1965, this provision was repealed. The favourable reliefs in the Borneo States relative to those in Malaya and Singapore more than compensate the absence of an "earned income relief" in their tax structure.

iii) Children's Limit. Allowance in Malaysia is given in respect of children under 16 years of age, and in respect of children above that age if they are attending school, college or university full-time". Children comprises, "legitimate children, step-children, and children formally adopted, or whose

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[17] Earned Income is defined as, "income from employment or pension, or from a trade, business, profession or vocation in which the taxpayer is actively engaged in either as proprietor or working partner". Personal Income Taxation in the Federation of Malaya, op. cit., p. 6. It is also extended to Hindu Joint Families.

[18] Supply Bill 1965, op. cit., p. 38.

[19] Taxes Changes Within Malaysia, op. cit., p. 14. See, 1965 Supply Bill, op. cit., p. 39.

adoption has been registered under some statutory provision".[20] The allowances are for 5 children:[21]

	eldest child qualifying	$ 750
2nd.	" " "	500
3rd.	" " "	500
4th.	" " "	300
5th.	" " "	300
	Maximum	$2,350

Before 1960, in the case of Malaya, children's allowance was allowed for 9 children with the maximum being $3,150.[22] The effect of the 1965 alteration was to bring in more than 30,000 taxpayers into the tax net. This also saw an increase in yield from existing taxpayers. In that same year the Finance Minister rejected pleas for allowance for taxpayers supporting parents on the grounds that it would be open to considerable abuse. Since 1960 the maximum limit of children's allowance has been $2,350 but in the case of Singapore, till 1965 the maximum was $3,150 i.e. the pre-1960 Malayan level. Sabah, prior to 1965, had no maximum limit and Sarawak had a maximum allowance of $2,100. From 1965, however, the maximum level for the whole of Malaysia has been harmonised with the rate of allowance prevailing in Malaya from 1960-1964. If viewed closely these changes have been to the benefit of Sarawak parents only.

If a person in Malaysia has more than 5 children, then the 1st. child ceases to qualify and the 6th. child becomes the 5th. "qualifying child". Further provision ensures that if a child is being educated overseas, the allowance may be increased to the actual expenditure incurred provided it does not exceed a maximum of double the relief normally due.

iv) Life Assurance. An allowance is given in respect of net premiums paid on policies on the life of the taxpayer or of his wife. It is however, restricted to 7% of the capital sum assured at death by the policy. Relief is not due for a taxpayer in respect of premiums he pays for his children or others.

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[20] Personal Income Taxation in the Federation of Malaya, op. cit., p. 6.

[21] Tax Changes Within Malaysia, op. cit., p. 3. These rates are applicable to all territories of Malaysia from 1st. January 1965.

[22] Supply Bill 1960, Information Department.

v) Approved Pensions or Provident Fund Contributions. Only compulsory contributions (like the EPF/CPF)[23] are deductible. No income tax relief, consequently, is due to voluntary contributions. The maximum relief for the aggregate of both types of payment (i.e. (iv) and (v) is $3,000. From 1965 the anomaly whereby a person could claim relief for contribution on behalf of domestic servants has been removed. The 1965 Budget also harmonised the maximum relief in all four territories for contributions to items (iv) and (v) to $3,000 which meant a reduction in the limit by $1,000 in the case of Sabah, Sarawak and Singapore.[24]

In the case of "Trades, Businesses, Professions and Vocations" where the enterprise has employees and contributions are paid on their behalf to a Provident Fund or a Pension Scheme, a deduction is due in respect of those contributions. The total deduction, however, must not exceed 15% of the employees basic pay.

As for replanting of crops, the cost of replanting is deductable. If it involves the planting of a new crop the crop must be an "approved crop". Otherwise only the ordinary cost of replanting is deductable and not the total expenditure.[25] Similarly, a deduction is due in respect of the net cost of abortive prospecting for minerals. Though no explicit reasons are given for these deductions we could well conjecture them. It might be in keeping with the policy of agricultural diversification and also to give consideration for excessive costs/losses involved in the prospection of minerals.

vi) Depreciation:

a) Industrial Buildings. Capital Allowances are given in respect of capital expenditure incurred in "providing factories and other buildings or structures used for the purpose of the trade, of storage of goods on arrival in the Federation, or storage of goods which are to be used in manufacture or processed".[26] An initial

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[23] EPF - Employees Provident Fund (Malaya).
CPF - Central Provident Fund (Singapore).

[24] In Sabah, Sarawak and Singapore the maximum relief before 1965 Supply Bill was $4,000.

[25] The "approved crops" at present are: cashew nuts, cocoa, coconuts, coffee, durians, mangostein, Manila hemp, oil palm, peper, rambutan, ramie, rubber and tea.

[26] Personal Income Taxation in the Federation of Malaya, op. cit., p. 18.

allowance of 10% is due for this. Subsequent expenditure on improving and extending also qualify for the initial allowance. In additional annual allowances of 2% are due in respect of "total cumulative cost of such building".[27] However, initial allowances are not granted in respect of second-hand buildings.

b) Plant and Machinery. Capital allowances are due for expenditure in providing plant and machinery at an initial allowance of 20%. It is, however, 60% in the case of capital expenditure for getting tin-ore or extracting or dressing tin concentrates. A comprehensive schedule is in operation and may be obtained in the Income Tax Rules 1948 or in the 1961 Reprint of the Income Tax Ordinance.

c) Capital Expenditure on Plantations. Buildings and structures, and plants and machinery qualify for allowances as in (a) and (b). But allowance for structures and buildings may be claimed separately at an annual allowance of 10% of the expenditure for 10 years. Similarly cost of clearing for planting (other than replanting) qualifies for an annual allowance of 50% per year for 2 years.

d) Capital Expenditure on Mines. Similar allowances as in (a) and (b) are due. But in the case of abortive prospecting, a deduction is granted in respect of the net cost of the abortive prospecting. Allowances for other capital expenditures are available under the Income Tax (Mining Operations) Rules, 1949.

Generally, the basis of assessment for gains or profits from a trade, business, profession, or vocation is similar to that applying to employment income. We may also note that since the assessment year is normally measured by the income of the previous year, it gives rise to an advantage i.e. tax liability can be computed at an early stage during the tax year.

Liability and Exemptions

Liability

Taxpayers who are " resident" in Malaysia are liable to income tax on the income they derive in Malaysia, and upon such of their

[27] Ibid, p. 19.

foreign income as is received in Malaysia. Non-residents who visit the Federation for less than 60 days are not subject to income tax. An exception exists for public entertainers who are subject to income tax unless they are financially sponsored by another country. Non-residents are subject to income tax only on their Malaysian income. Otherwise if they stay in Malaysia for more than 6 months, they are liable to income tax on their foreign income. The general rate of tax payable by non-resident individuals is 40%. Non-residents who are Commonwealth citizens or British protected persons are at present entitled to claim reliefs similar to those available to residents but proportionate to their ratio of local income to world income.

Exemptions

Heading the list of exemptions is the profits of a Pioneer Company during its tax relief period, and dividends out of these profits are exempt from income tax. Other exemptions include registered co-operative societies, approved friendly societies and institutions approved by the government and included in the First Schedule of the Income Tax Ordinance. Approved charities, registered trade unions and approved pensions or Provident Funds or Societies are similarly exempt from income tax. Furthermore, certain diplomats, and certain advisers and technicians supplied by the agencies of the United Nations and the Colombo Plan Technical Co-operation Scheme are exempt from tax on their official incomes. As from 1963, persons ceased to be liable to tax on the net annual value of residence owned and occupied by them; but this exemption is restricted to one residence for each person.

Briefly the reasons for such exemptions appear to be threefold. In the first place these exemptions are given because of the special character of the recipients of the income like diplomats. Secondly it may arise due to the special character of the income itself like pensions. And lastly it may be due to the government's aim to encourage savings and investment in certain government securities.

Double Taxation Agreement and the Pioneer Industries Law

As far as double taxation agreements go, there has been no attempt to view the situation in the Malaysian context. But generally if we have made arrangements for the avoidance of double taxation with the United Kingdom, then if an individual received dividends from the United Kingdom, the gross dividend before British tax is chargeable but allowance in respect of British tax deducted is due by way of the Double Taxation Relief. The situation generally is the same for other countries with which we have such agreements.[28] In actuality because of our formal Double Taxation Agreement with the United Kingdom, we acceded to the Double Taxation Conventions entered into between the United Kingdom, and Denmark, Norway and Sweden respectively. The general principle underlying these treaties is that, "where possible

[28] Denmark, Norway, Sweden, United Kingdom and lately with Singapore.

income should not be taxed both in the territory in which it arises and in the territory of residence of the recipient but that where income is taxed in both countries, one country gives relief to the tax charged in the other".[29] A recent event of relevance is the signing of a Double Taxation Agreement with Singapore. Apart from press reports, details of the agreement are as yet not available. However, presumably, the general principles would be operative in this agreement.

As for the pioneer industries, a new Malaysian Bill came into effect on the 1st of April 1965[30] to replace the existing 4 Ordinances in Malaya, Singapore, Sarawak and Sabah. Prior to this, pioneer industries were "encouraged with widely different degrees of generosity by four different laws in each of the four regions of Malaysia."[31] In general terms the laws for pioneer industries in Malaya, Singapore and Sabah were broadly similar in that they provided tax holiday. But in the case of Sarawak, the law provided enhanced capital allowances. Furthermore, in Malaya and Sabah the length of tax holiday was linked to the quantum of expenditure on factory and machinery.[32] In Singapore all pioneer enterprises could obtain 5 years exemption without statutory obligation to spend anything on factory or machinery. The new Ordinance was not only intended to harmonise the 4 existing systems but was also designed, "to provide the same type of tax incentive in all regions so as to ensure as far as possible that there is balanced development within Malaysia".[33] As ought to have been, it preserved the certificates already granted under the various Ordinances. It was also felt when introducing the 1965 budget, that it would add flexibility to a rigid piece of legislation. It was intended to give the Federal Finance Minister powers to provide tax incentives to industries that were to be encouraged. This matter is too early to be evaluated although the principle behind it is justifible in terms of national economic development.

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[29] Annual Report of the Department of Inland Revenue, Government Printer, 1961, p. 7.

[30] The amendments made by Act 30/65 have effect as regards Pioneer Certificates on or after the 1st day of April 1965.

[31] Supply Bill 1965. Ibid., p. 36.

[32] Malaya, maximum 5 years.

[33] Sabah maximum 4 years.
Tax Changes Within Malaysia, op. cit., p. 2.

At present the period of exemption is being linked with the quantum of capital expenditure incurred in providing factories and machinery in all the regions of Malaysia. The 1965 Supply Bill raised the expenditure requirements to higher levels. The tax exemptions in relation to expenditure from 1965 is as follows:[34]

TABLE 2.1

Fixed Capital Expenditure on Factory and Machinery	Maximum Period of Tax Exemption
Over $ 250,000	2 years
Over $ 500,000	3 years
Over $1,000,000	5 years

As Table 2.1 shows, the system is on a graduated scale but there exists uneveness in the period of exemption limit. As such an industry with a capital expenditure of $550,000 has the same exemption limit as one investing say $800,000 or even $900,000. A further breakdown with an exemption period of 4 years for more than $750,000 capital expenditure may be introduced to reduce the wide range between these two slabs of investment. Furthermore, the incentive (i.e. the tax exemption) is directly related to the actual profits earned. As such the government is considering introducing the principle of a development rebate into the legislation in which the "quantum of incentive would be directly related to the quantum of investment".[35] Furthermore the granting of greater incentives for investment in the less underdeveloped parts of the country is likely to induce a flow of investment to these regions.

Rates of Income Tax

Marginal Rates

The marginal tax rates in Malaya, Sarawak, Singapore and Sabah as on Malaysia day are shown in Table 2.2

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[34] Ibid., p. 2.

[35] Supply Bill, 1966. Information Department, p. 14.

TABLE 2.2

(A) RATE OF TAX ON CHARGEABLE INCOME IN MALAYA

Increase		Marginal Rate	Rate of Change
(1)		(2)	(3)
First	$ 2,500	6%	
Next	$ 2,500	8%	2%
"	$ 2,500	10%	2%
"	$ 2,500	12%	2%
"	$ 5,000	15%	3%
"	$ 5,000	18%	3%
"	$ 5,000	20%	2%
"	$ 5,000	22%	2%
"	$ 5,000	25%	3%
"	$ 5,000	30%	5%
"	$ 5,000	35%	5%
"	$10,000	40%	5%
Exceeding	$55,000	45%	5%

(B) RATE OF TAX ON CHARGEABLE INCOME IN SABAH

Increase		Marginal Rate	Rate of Change
(1)		(2)	(3)
First	$12,000	3½%	
Next	$12,000	5%	1½%
"	$10,000	10%	5%
"	$10,000	20%	10%
"	$10,000	30%	10%
Exceeding	$54,000	40%	10%

(C) RATE OF TAX ON CHARGEABLE INCOME IN SARAWAK

Increase		Marginal Rate	Rate of Change
(1)		(2)	(3)
First	$ 5,000	5%	
Next	$ 5,000	6%	1%
"	$ 5,000	7%	1%
"	$ 5,000	8%	1%
"	$ 5,000	10%	2%
"	$ 5,000	15%	5%
"	$ 5,000	20%	5%
"	$ 5,000	25%	5%
"	$ 5,000	30%	5%
Exceeding	$45,000	35%[a]	5%

[a] Subject to a ceiling tax not to exceed 10% of assessable income.

(D) RATE OF TAX ON CHARGEABLE INCOME IN SINGAPORE

Increase		Marginal Rate	Rate of Change
(1)		(2)	(3)
First	$ 1,500	5%	
Next	$ 500	6%	1%
"	$ 1,000	7%	1%
"	$ 1,000	8%	1%
"	$ 1,000	10%	2%
"	$ 2,000	12%	2%
"	$ 3,000	15%	3%
"	$ 5,000	18%	3%
"	$ 10,000	25%	7%
"	$ 10,000	30%	5%
"	$ 15,000	40%	10%
"	$ 50,000	50%	10%
Exceeding	$100,000	55%	5%

Source: For Table 2.2: Tax Changes Within Malaysia, op. cit., p. 15. Also see Finance Act 1965, No. 2 of 1965, Government Printer.

The marginal tax rates,[36] as shown in Table 2.2 are progressive in that marginal rates increase with marginal increases in income. The marginal rates increase from 6% in the case of Malaya, 5% in Singapore, 3½% in Sabah and 5% in Sarawak, to maximum rates of 45%, 55%, 40%, and 35% respectively. The application of the various marginal tax rates ensures that "individuals with the same chargeable income will be taxed equally",[37] with the exception of Sarawak. In the case of Sarawak, there was a differentiation of business income and interest.[38] Another noteable feature is that, as regards Malaya and Singapore, the marginal tax rates did not increase in stages by increasing absolute amounts. For example in the case of Malaya, there is an anomaly in the marginal tax rate increases[39] above $20,000. This necessitates a sudden increase in the marginal tax rate on chargeable income above $35,000. Such a discrepancy also occurs in the Singapore tax structure where for a chargeable income above $20,000 there is a increase of 7% in the marginal tax rate; while for a chargeable income of above $30,000 the increase in the marginal tax rate is only 5%.[40] Finally in all four tax rates, at high levels of chargeable income the increase in the marginal tax rate stops at 5% in every bracket.

In the Malaysian tax rates, which came into effect in 1965,[41] the anomaly is not overcome. In fact, very suprisingly the trend is exaggerated as can be seen in column (3) Table 2.3. For the first 3 tax brackets the increase is at a rate of 3%. For chargeable income between $10,000 and $15,000 there is a sudden jump to 5% followed by a drop to 2% in the next tax bracket. Beyond $30,000 the rate of increase in the marginal tax rate is 5% till the level of chargeable income is more than $35,000 when the increase in the rate is 10%. As such, on the point of increases in marginal tax rates the situation before 1965 was bad enough but the structural relationship of one marginal tax rate to another is even worse in the new Malaysian tax structure.

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[36] Columns (2) Table 2.2, (A), (B), (C) and (D).

[37] C.T. Edwards, op. cit., p. 38.

[38] Business income 10% tax.
Interest 5% tax.

[39] See Table 2.2 (A) column (3).

[40] See Table 2.2 (D) column (3).

[41] Supply Bill (1965), op. cit.

TABLE 2.3

MALAYSIAN RATE OF TAX ON CHARGEABLE INCOME

Increase		Marginal Rate	Rate of Change	Total	Average Tax Rate
(1)		(2)	(3)	(4)	(5)
First	$ 2,500	6%		$ 2,500	6.0 %
Next	$ 2,500	9%	3	$ 5,000	7.5%
"	$ 2,500	12%	3	$ 7,500	9.0%
"	$ 2,500	15%	3	$10,000	10.5%
"	$ 5,000	20%	5	$15,000	13.66%
"	$ 5,000	23%	3	$20,000	16.0%
"	$ 5,000	25%	2	$25,000	17.8%
"	$10,000	30%	5	$35,000	21.28%
"	$15,000	40%	5	$50,000	26.90%
Exceeding	$50,000	50%	10		

The new rate structure, however, decreased the number of tax brackets in the case of Malaya, and Singapore from 13 to 10. In the case of Sabah, the new tax rate has meant an increase in the number of tax brackets.[42] Sarawak, however, did not witness any change in the number of tax brackets as a result of the harmonisation of the 4 different tax rates.

A comparison of Table 2.2 and Table 2.3 would enable us to appraise the change in burden as a result of the new tax structure on the different components of Malaysia. Singapore, evidently was least affected by the change. Similarly, in the case of Malaya too, the increase in burden has not been very significant.[43] However, for Sabah and Sarawak, there has been a very large increase in the burden of taxation as a result of drastic differences in the new rate structure when compared to their old ones. Consequently, the federal government has found it necessary to give rebates to these two states.[44] While

[42] Sabah from 6 to 10 tax brackets.

[43] As a result the rates operate unabated in Malaya and Singapore.

[44] Finance Act 1965, op. cit., p. 16 Part I and p. 22. However, there is no rebate in respect to every dollar exceeding $50,000.

the rates operate unabated in the case of Malaya and Singapore, the rates in Table 2.3 operate with a rebate of 40% in the case of the Borneo States. This was to be deducted from the tax chargeable on the first $50,000 of chargeable income. But it was not intended to be a permanent feature of the Malaysian tax structure. Consequently, in 1966 the abatement was reduced by 10 to 30%.[45] Eventually, this rebate will be repealed.

Rate of Change in Marginal Tax Rate

Table 2.4 indicates the adjustments of the marginal tax rate structure for Malaya. The first post independence adjustment of the marginal tax rate structure occured in 1960. Column (3) (a) shows the effect of this adjustment. It resulted, like the 1957 adjustment, in an upward revision of tax rates at very low levels and very high levels of chargeable incomes, the intermediate slabs of the schedule remaining unaltered. In fact at the centre of the schedule there were downward revisions of the tax rates as can be observed from column (3) (a). Therefore this 1960 re-adjustment seems to have concentrated its emphasis upon increasing tax rates at low and high levels of chargeable income. However, quite unlike this 1960 change, the 1965 re-adjustment had concentrated on an upward revision of tax rates in the moderate and high levels of chargeable incomes leaving the low levels of chargeable income unaltered.

Comparing Table 2.2 (D) and Table 2.3, we may conclude that the 1965 adjustment has relatively left Singapore's tax rate unaltered except at the highest tax bracket where there was a downward revision from 55% to 50% - a 20% downward revision for incomes above $100,000. However, there has been drastic upward revision of marginal tax rates in the case of Sabah and Sarawak for most, if not the whole, of the tax structure as a result of the new Malaysian rates.

Average Tax Rates

As we have discussed, there have been many upward revisions of the marginal tax rates. But although this has occured quite often, one other feature becomes apparent when we discuss the average tax rates as shown in Table 2.3 column (5). The trend in the average tax rate is increasing as chargeable income increases. However, the increase in the average tax rate in the Malaysian tax structure suffers from certain irregularities. For instance the increase in the average tax rate from $10,000 to $15,000 is 3.16%. The increase, for a similar increase in chargeable income (from $15,000 to $20,000) is however only 2.34%. Furthermore, the average tax rate only increases by 1.8% for an increase of $5,000 in chargeable income from $20,000 to

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[45] Supply Bill 1966, op. cit., p. 57.

TABLE 2.4

CHANGES IN MARGINAL TAX RATES, FED. OF MALAYA AND MALAYSIA 1957, 1960 AND 1965

(1)		(2)			(3)	
Chargeable Income		Marginal Tax Rate %			Rate of Change in Marginal Tax Rate (%) Between	
Total	Increase	1957-59	1960-64	1965-	(A) 1957/59 and 1960/64	(B) 1960/64 and 1965/-
500	500	5	6	6	20.00	-
1,000	500	5	6	6	20.00	-
1,500	500	5	6	6	20.00	-
2,000	500	6	6	6	-	-
2,500	500	7	6	6	-14.29	-
3,000	500	7	8	9	14.29	12.50
5,000	2,000	8	8	9	-	12.50
7,000	2,000	10	10	12	-	20.00
7,500	500	12	10	12	-16.67	20.00
10,000	2,500	12	12	15	-	25.00
15,000	5,000	15	15	20	-	33.33
20,000	5,000	20	18	23	-10.00	27.77
25,000	5,000	20	20	25	-	25.00
30,000	5,000	20	22	30	10.00	36.36
35,000	5,000	20	25	30	25.00	20.00
40,000	5,000	25	30	40	20.00	33.33
45,000	5,000	25	35	40	40.00	14.28
50,000	5,000	30	40	40	33.33	-
55,000	5,000	35	40	50	14.29	25.00
60,000	5,000	40	45	50	12.50	11.11

Source: (1) C.T. Edwards - The Rate Structure of Personal Income Taxation in Malaya, Vol. I, No. 2, Dec. 1964, p. 42.

(2) Relevant Figures for 1965 compiled from data in 1965 budget and "Tax Changes Within Malaysia", op. cit., p. 14.

$25,000. The explanation for this is to be found in the irregular increases in the marginal tax rate in our tax system.

Table 2.5 shows the average tax rate on a single person able to take full advantage of earned income relief. It shows average tax rates on assessable incomes of $10,000, $50,000 and $100,000 both before the Malaysian tax rate and under the Malaysian tax rate. In the case of Malaya it increases very steadily from 5.05% on an assessable income of $10,000 to 19.90% for $50,000 and 32.05% for a chargeable income of $100,000. Table 2.5 shows the equivalents for the other 3 states. Comparing column (5) with column (1), Malaysia has shown a slight increase in the average tax rate at all levels of assessable income as a result of the 1965 tax changes. But the effect of the tax changes on the average tax rate of Singapore has been negligible. However, for Sarawak, and Sabah, there has been a large increase in the average tax rate for all levels. In Table 2.5 no consideration was given for the 40% rebate in those territories. C.T. Edwards observation that, "while upward adjustments in the marginal rates of taxation have occured throughout this period, the maximum possible average rate of taxation has remained moderate"[46] still holds true.

Allowances

In Malaysia, the existing opportunities of reducing the net chargeable income by taking advantage of permissible allowances are considerable. One is also tempted to agree with C.T. Edwards, Alison M. Martin and W.A. Lewis,[47] that as a result of such "generous allowances" virtually the whole of the middle-class in Malaysia, is exempted from income tax. Combined with this is the fact that, even among those who pay, the percentage of increased income liable to tax at any given level of income is moderate.

Any reduction in the allowances permitted would inevitably increase the coverage of the Malaysian tax system. At this juncture, we may question the validity of the earned income relief. There is no easy method of distinguishing what is earned income and what is unearned income - decisions invariably have to be arbitrarily made thus providing scope for abuse and evasion. The principle behind the relief is laudable but what is more important is not the principle but practicability. In fact C.T. Edwards goes as far as to suggest that such items are an "inherent bias within the Malayan tax structure to keep in step with the United Kingdom".[48]

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[46] C.T. Edwards, op. cit., p. 38.

[47] Ibid., p. 39.

[48] Ibid., op. cit., p. 49.

TABLE 2.5

AVERAGE TAX RATES

Assessable Income	Average Tax Rate in 1964 %				1965
	(1) Malaya	(2) Singapore	(3) Sabah	(4) Sarawak[1]	(5) Malaysia
10,000	5.50%	5.95%	2.45%	3.70%	6.15%
50,000	19.90%	24.49%	9.84%	14.00%	24.50%
100,000	32.05%	36.94%	24.30%	18.20%	36.95%

Table shows average rate of tax on a single person able to take full advantage of earned income relief.

Source: Calculated from Tax Rates available in:

(1) Finance Act, 1965 (No. 2 of 1965) pp. 12, 16, 22 and 27.

(2) Tax Changes Within Malaysia, op. cit., p. 14.

[1]In the case of Sarawak, for every $ exceeding $45,000 the marginal tax rate is 35% subject to a ceiling tax rate to exceed 10% of assessable income. Our calculations, however, ignores this provision.

Note: C.T. Edwards, (op. cit., p. 38) has presumably made an arithmetical error in calculating the average tax rate for $50,000 when he gives it to be 21.05%. The correct figure is 19.90%.

From the above analysis, we may conclude that, we have to adjust and considerably reduce the level of allowances and reliefs permitted. Furthermore, it is desirable for us to maintain moderate marginal tax rates and to avoid abrupt increases in the tax rates. In other words, we need a realignment of our marginal tax rate structure. Such measures appear necessary if income tax is to form any significant proportion of revenue to the government. As Edwards prefers to put it, "there is a need to adopt the appropriate, reject the inappropriate and above all evolve an income tax structure relevant to the particular characteristic features of the Malayan economy".[49]

[49]Ibid., p. 50.

TABLE 2.6

SIGNIFICANCE OF INCOME TAX IN TOTAL TAX REVENUE AND TOTAL REVENUE

Year	Income Tax	Total Tax Revenue	Total Revenue	Col. (1) as % of Col.(2)	Col. (1) as % of Col. (3)
	(1)	(2)	(3)	(4)	(5)
1958	118,682,016	559,947,925	762,465,446	21.19	15.56
1959	124,503,536	772,161,560	890,972,163	17.24	13.97
1960	186,170,162	882,640,099	1,069,020,973	21.09	17.41
1961	232,165,203	873,655,570	1,081,006,862	26.57	21.47
1962	237,435,767	880,262,622	1,097,388,798	26.97	21.63
1963	234,060,195	902,032,899	1,150,246,312	25.94	20.34
1964	261,602,412	1,033,378,113	1,338,195,777	25.31	19.54
1965	299,900,000	1,167,375,800	1,437,400,000	26.11	20.86
1966	330,100,000	1,264,348,800	1,560,050,500	27.29	21.15

Source: Financial Statements Accountant General Government Printer (1958-1964). Estimates of Federal Revenue and Expenditure Government Printer (1960-1966).

*In this exercise all figures for 1965 are Revised Estimate Figures; and 1966 are preliminary Estimates.

Significance of Income Tax

In Total Tax Revenue

In Table 2.6 column (1) what is immediately noticeable is the increase of income tax receipts over the years except in 1963 when there was a slight drop reflecting poor rubber prices in 1962. Before we proceed let us mention a peculiar phenomena operating in export-orientated economies. In such countries, high export proceeds in one year is reflected in an increase in income tax the following year.[50]

Income tax collections are expected to treble by 1966, reflecting the increasing importance of income tax in governmental revenue. (See column (1) Table 2.6). Percentage wise, (column (4) Table 2.6) except for 1959, income tax seems to have constantly contributed over 20% of total tax revenue. The low figure for 1959 was not caused by a decrease in income tax revenue, but in fact by an increase of $200 million in other tax revenue, thereby diminishing the significance of income tax. Another feature of column (4) is that the proportion of income tax in the total tax revenue increased by 6% over the years under review.

1960 witnessed a large increase in income tax collections both absolute and percentage-wise. In the first place this major jump was a reflection of the prosperous conditions prevailing in 1959 when the average price of rubber was 101¢, as against 80¢ in 1958. Secondly the reduction in allowances[51] brought in more than 30,000 new taxpayers. And thirdly 1960 also brought about the first post-independence change of tax rates. The Finance Minister, in introducing the 1962 Supply Bill maintained that in two short years income tax had nearly doubled. During this period of alteration of rates, the number of tax-paying individuals rose from 46,000 in 1959 to 90,000 in 1960. Further-more boom conditions prevailing in 1960 was reflected in increased earnings in 1961. The Federal Finance Minister also maintained that there was increasing success of the anti-evasion campaign as a result of the formation of an Investigation Unit to beat tax evaders. Over looking minor fluctuations, since 1960 income tax has contributed more than 20% and since 1961 more than 25% of total tax revenue. Notice furthermore the large amounts of income tax expected to be collected in 1965 and 1966. This trend started in 1964 with the formation of Malaysia and it is expected to have continued in 1965 as a result of the major tax changes effected in that year.

In Total Revenue

The trend that became evident in the above discussion is also prevalent in the share of income tax to total revenue for the period, but as would be expected, it is on a reduced scale. The fluctuations

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[50] This is because income tax is based on the previous year's earnings.

[51] For further details on the Amendments refer to Supply Bill (1960), op. cit.

are similar and are due to the same reasons as in the case of income tax proportion to total tax revenue. Generally it can be observed that while in the earlier part of our analysis income tax formed around 15% of total revenue; income tax contribution in the later years especially after 1961 came up to 20%. This proportion or percentage is being maintained since that year.

There is no doubt that income tax does not form a large percentage of either total tax revenue or total revenue but does contribute at the moment a sizeable proportion. The most remarkable features in Table 2.6 are firstly the tripling of the absolute amount of income tax collected over the period, and secondly the increasing trend in income tax percentage in both total tax revenue and total revenue collections. There is hardly any reason to doubt that in the future, not only will absolute income tax collections increase but also the significance of income tax both in total tax revenue as well as in governmental revenue will increase.

Estate Duty

Scope of Estate[52]

1) Estate duty is payable on the value of all properties moveable or immovable, situated in Malaysia, which are deemed to pass on death.

2) It is also imposed on all moveable property situated outside Malaysia if the owner, on whose death the property passed, was domiciled in Malaysia at the time of his death.

Rates of Estate Duty

Estate Duty is charged at ad valorem rates on the net principal value of the property comprising the dutiable estate. The objectives behind the introduction of a common tax rate were firstly harmonisation[53] and secondly to ensure a reduction in the incidence of taxation. This was felt to be equitable in that there was strong feeling not to saddle small estates with estate duty and bring to bear hardships on the beneficiaries i.e. widows and children. Furthermore, the government has found it expedient to encourage private house ownership and the reduction in the incidence and the increase in the exemption limit is consistent with this policy.

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[52] Annual Report of the Department of Inland Revenue, op. cit., 1963, p. 10.

[53] See, Tax Changes Within Malaysia, op. cit., p. 17.

The rates of estate duty since 1st January 1965 were as follows:

TABLE 2.7

RATES OF ESTATE DUTY

Value of Property		Rate of Estate Duty	Average Rate
First	$ 25,000	Nil	Nil
Next	$ 25,000	5%	1.25%
"	$ 50,000	7½%	5.0 %
"	$ 50,000	10%	6.66%
"	$ 50,000	12½%	8.12%
"	$100,000	15%	10.41%
"	$100,000	20%	12.81%
"	$200,000	25%	13.54%
"	$200,000	30%	17.65%
"	$200,000	35%	21.12%
"	$500,000	40%	27.35%
"	$500,000	45%	31.85%
Remainder (Over $2 Million)		50%	

Source: Tax Changes Within Malaysia, op. cit., p. 17. For the old rates see above booklet, p. 17. The rates for Malaya before 1965 are also obtainable in "The Estate Duty (Variation of Rates) Ordinance, 1957, Government Printer, p. 2.

Major Changes[54]

i) There has been an increase of the exemption limit from $10,000 in Sabah, Malaya and Singapore and $1,000 in Sarawak to $25,000 in all four regions.

ii) Harmonisation of the maximum rate at 50%. The 60% maximum rate in Malaya and Singapore was

[54] The data was obtained from details in the 1965 Supply Bill op. cit., pp. 50-53.

in fact very much higher than those in many developed countries.

iii) As from 1965, all Malaysian assets and foreign moveable assets is to be aggregated and charged in a single Malaysian computation i.e. only one computation of estate duty. Formerly if a Malaysian had assets in two or more regions of Malaysia, tax paid will be low because each asset will fall in a lower tax bracket. The effect of a single computation has the advantage of producing a larger tax bill by bringing the estate into a higher tax bracket.

iv) Increased the period during which "inter vivos" gifts will be aggregated, to 5 years in the whole of Malaysia. Formerly this 5 year limit only applied to Singapore.

v) There was also a change in the rates of interest to be charged on overdue estate duty. The rates were as follows:

1) First 6 months after date of death .... 3% per annum

2) Over " " " " " " .... 6% " "

However, the rate of interest may be increased to "not more than 12% per annum after 18 months in cases of "wilful delay in settlement".[55]

Viewing these changes in perspective, it becomes obvious that there is a net reduction in liability in the case of smaller and medium sized estates, while a great many very small estates will not now be liable to estate duty. Furthermore, since they are no longer confiscatory in nature, there is a hope that there will be less evasion of tax. The average rate of duty, Table 2.7, while not confiscatory rises steeply to 31.85% for an estate of $2 million. Estate duty helps to break up concentration of wealth in few hands and through this measure greater income equalisation may be achieved. Estate duty also helps to reduce the concentration of economic power. The average rates, as indicated in Table 2.7, are not excessive but at the same time they are more than merely moderate.

Generally estate duty collections has increased over the years. The reasons for every item seems unnecessary if are remember that changes may be caused by 3 basic factors:

1) Change in number of estates assessed.

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[55] Ibid., p. 53.

TABLE 2.8

REVENUE FROM ESTATE DUTY

Year	Estate Duty
1958	4,480,806
1959	4,276,201
1960	4,661,423
1961	3,971,669
1962	5,677,535
1963	5,370,094
1964	8,005,502
1965	7,700,000
1966	8,000,000

Source: As for Table 2.6.

2) Change in value of estates assessed, and

3) Changes in the rate of estate duties.

If not for a lowering of rates the figures for 1965 and 1966 could well be higher than the estimates in Table 2.8.

As a contributor to tax or total revenue, it does not have much importance since estate duty, to date, has contributed a negligible portion of government revenue.

Business Registration, Betting and Sweepstakes, Lotteries and Stamp Duties

All businesses, with the exception of those carried on by limited companies, registered societies, and in the exercise of certain professions must be registered. The certificate of registration, which is valid for three years must be displayed prominently at the principal place of business. A fee of $5 is charged for this certificate and for each renewal thereof. If, however, a business is carried on under a trade name, an additional fee of $20 is payable on first registration.

The Inland Revenue Department also administers the Stamp Duty offices in Penang and Kuala Lumpur but the overall control and responsibility for administration of the Stamp Ordinance rests with the Accountant - General.

In view of the fact that these items of revenue do not significantly contribute to the federal revenue, and also because of considerations of space, it would suffice for us to tabulate net collections for the years in our discussion.

TABLE 2.9

OTHER INLAND REVENUE

Year	Lotteries	Business Registration	Stamp Duties	Betting and Sweepstakes
1958	1,791,266		3,771,676	2,450,520
1959	2,450,060	415,315	4,833,230	2,300,569
1960	3,260,335	391,641	5,809,231	3,231,827
1961	3,553,715	285,304	5,903,315	4,669,387
1962	3,226,647	351,543	5,852,846	6,121,224
1963	4,453,717	413,080	7,213,082	8,986,158
1964	5,403,265	297,660	10,595,711	8,631,452
1965	5,700,000	337,000	8,200,000	9,000,000
1966	6,000,000	362,000	9,600,000	10,000,000

Source: As in Table 2.6.

Other New Taxes

In searching for new taxes, the government found it expedient to introduce taxes which can be handled by the existing machinery with minimum additional cost. Therefore, a few new taxes came into effect in 1965.

(1) Turn-Over Tax[56]

It was levied on the basis of the turn-over i.e. the sale and other gross earning, of all trades, businesses, professions, and vocations carried on in Malaysia. It was to apply at ½% throughout Malaysia. The Finance Minister contended it to be a "low rate on a very wide range".[57] It was originally multi-stage tax. As a

[56] See Turn-Over Tax Act 41/65 Government Printer.

[57] Supply Bill 1965, op. cit., p. 43.

corollary to its introduction, Sarawak's 1% tax on goods on consignment was repealed.

Exemptions: (i) when the turn-over is less than $36,000 per year, (ii) where the turn-over consists mainly of gross receipts from the provision of services and does not exceed $20,000, (iii) that part which consists of the production, merchanting or export of commodities which are subject to export duty and of certain other raw materials not liable to such duties, (iv) that part consisting of goods other than those in (iii) where these are exported by the trader, (v) sale of machinery or business premises made by the taxpayer who does not deal in machinery or property (vi) government departments like the Post Offices, and (vii) co-operative societies, charities, clubs, societies and trade unions.

At the time of the introduction of the turn-over tax, some anamolies were not foreseen. Hence, the tax was converted into a single-stage tax but the rate was increased to 2% from ½%. The Finance Minister contended[58] that the cumulative effects of a ½% multi-stage tax was more than the 2% single tax rate in most cases. It is now levied on the actual value of sales of goods imported other than those re-exported. If an importer instead of selling immediately processes or manufactures such goods for subsequent sale, the tax will only apply to that part of the sales proceed which relates/to the imported content of the goods. All other business transactions ceased to be liable to turn-over tax from 1966. The new single-stage tax will exempt all home manufactured goods in order to provide positive encouragement for domestic industry. In theory, however, it does not remain a turn-over tax, but has become similar to an import duty - tax on certain types of imports. Hence, it need not, in fact, be called a turn-over tax.

(2) <u>Capital Gains Tax</u>

The Minister in introducing this tax felt that considerable gains from the sale of property and shares accrued not as a result of the taxpayer's own exertion but purely fortuitously.

Exemptions: (i) gains from sale of taxpayer's own residence, (ii) gains from sale of business premises and (iii) first $5,000 of capital gains in each year.

Rates: For assets acquired on or after 1965 Budget day, and if they were disposed off within 6 months, the gains were to be regarded as income for income tax purposes. However, if it were disposed after 6 months, the tax was 20% on aggregated capital gain realised on disposal or the rate of income tax chargeable on the income if that is more favourable. In the case of assets acquired before

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[58] Supply Bill 1966, op. cit., p. 59.

budget day, the rate was to be 20%. However, abatements were provided for as follows:

If held for 3 years	- 15%
" " " 4 years	- 10%
" " " 5 years	- 5%
" " " 10 years	- Nil.

The Minister of Finance felt that there might be some "avoiding action", and warned "appropriate action will be taken to deal with any wilful obstruction to necessary development".[59] But in 1966, however, the Finance Minister considered the complexities and "loopholes" which might arise as a result of adherence to the $5,000 exemption principle. It was felt that it might result in avoidance if not evasion of tax. Therefore as from 1966, capital gain tax was repealed. But at the same time it was hoped to impose it at a more opportune time.

(3) Payroll Tax

The payroll tax was to apply initially in 1965 to employers in Malaya and Singapore at the rate of 2% of total payroll. But in 1966 it was extended to the Borneo States.[60] Small employers, where the payroll tax liability for the month is less than $5, were exempted. Governments Departments and certain statutory bodies were exempted from payment. It was originally estimated to yield $21 million in Malaya and Singapore of which $17 million was to accrue to the central government.

The tax is being collected by the Employees Provident Fund and Central Provident Fund. It was not introduced into Sabah and Sarawak in 1965 because no such national provident fund schemes exist in these states. But this seems hardly justifiable for the delay in implementation. Our aim should be to harmonise old taxes and introduce new taxes encompassing all territories of Malaysia from the same point of time. The payroll tax was, in fact, unfair to employers in Malaya and Singapore in that they had to bear it earlier than their contemporaries in Sabah and Sarawak.

(4) Film Hire Duty[61]

This Act was largely aimed at harmonising the taxpayable on imported films on an ad valorem basis. It replaced the footage tax in Malaya. It is being levied at the rate of 15% of the gross rental

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[59] Supply Bill 1965, op. cit., p. 49.

[60] Supply Bill 1966, op. cit., p. 60.

[61] For further details see Film Hire Duty Act 45/65 Government Printer.

for films paid by film exhibiters in Malaysia.[62] Since there exists no rational basis for calculating the profit element in film rentals, provision was made for deeming the non-resident producer's profits to be 15% of the net rental payable to him. Since his income tax rate is 40%, the net charge will be 40% of 15% i.e. 6% of the rental payable to him.

Not only did it replace the footage tax in Malaya, it also effected harmonisation in the Singapore system. It is a more equitable tax than the one existing before since it is directly proportionate to the actual earnings. It was expected to yield $1 million during the financial year 1965, and may well be expected to yield larger amounts.

(5) Profits Tax

The price of tin in recent years has been high and consequently the margin of profit has also been increased. Therefore the government in an effort to skim off high profits introduced the profits tax which was calculated by reference to a standard profit per unit of production. It was felt that the incidence will be greatest on the mines best able to pay it. The 1965 Budget[63] only laid down the broad pattern of the tax and details were to be worked out after discussion with representatives of the tin industry. This was to provide an opportunity for them to make representation on points of details.

Conclusion

In this chapter we have attempted to bring out the main features of our inland revenue, the most significant component of which is income tax. Having dealt with the details of rates, and reciepts, we are in position to touch on a few wider issues.

Our aim has to be one of equalising the tax burden between the same classes of taxpayers within Malaysia and therefore harmonising the somewhat complex income tax laws. To get the maximum revenue out of the existing taxes and to consolidate them, there is a need for recruitment of good quality staff. There is ample evidence of considerable tax evasion. The Department of Inland Revenue has very recently announced its intention to recruit accountants in its fight against tax evasion. Some thought should be given to the present structure of penalties. If they prove unsuccessful as deterents then new penalties are needed to keep apace with the stresses and strains of tax collection. It is also desirable that we have a unified Income Tax Ordinance for Malaysia which the Minister himself admits[64] would increase the tax yield.

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[62] Films produced in Malaysia are exempted.

[63] 1965 Supply Bill, op. cit., pp 53-55.

[64] Supply Bill 1966, op. cit., p. 56.

In our analysis, we have noted that allowances and reliefs are excessive and are open to abuse. The irregularities in the rate structure need to be corrected. Many of Malaysia's financial and tax problems arise as consequence of federalism which in itself needs constant change and modification. And finally what is needed is constant scruting of our system; to change when it is required and to accept what is useful