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Review

Forthcoming procedure of goods and service tax (GST) in Malaysia

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Malaysia is introducing the Goods and Services Tax (GST) with effect from April 1, 2015. The idea of introducing GST was first conceived in 2005, but its implementation was delayed due to resistance from the public. As a part of the holistic program to overhaul the financial system, the government decided to implement GST from April 2015 onwards. This article looks into areas of the public's concern about GST, the government's assertions on GST and how it will affect the common man. The article also explains what GST is and how it works and other administrative aspects of GST like registration requirements, classification of supply and the requirement of tax invoice.

Key words: GST, Malaysia, Budget, Sustainable Income, Government, Public concern.

INTRODUCTION

In the Budget 2014 presented on 25th October 2013, the Prime Minister of Malaysia announced the introduction of Goods and Services Tax (GST) at a rate of 6% to replace the existing Sales Tax and Service Tax with effect from April 1, 2015. The idea of introducing GST was first conceived in 2005 and the first draft of the GST Bill was introduced in Parliament in 2009 (Beh and Ng, 2013). It was scheduled to be implemented in the third quarter of 2011 but was delayed for various political and social reasons. This article looks into the public concerns about GST, the government assertions on GST, how it will affect the common man and how GST works.

Problem statement

Malaysia is adopting Goods and Service Tax (GST) to reduce its dependence on revenue from oil and as a sustainable source of income to the government. Currently more than 40% of government revenue is from petroleum or petroleum related taxes. The government considers GST as a stable and sustainable source of revenue by widening the tax base (Narayanan, 2014). However, the public is much concerned about its impact on their family budget. The following are the major concerns of the public about GST.

1. GST will increase the price of essential commodities like food, health care, medical products, public transport, education and other essential services.
2. It will affect Malaysians in the low income group. GST being a broad based consumption tax extracts larger proportion of income from lower income group relative to higher income households. In such a way it is likely to be a regressive tax (Curtis and Kingston-Riechers 2010, Narayanan 2014)
3. It is double taxation - firstly when income is earned and secondly when the income is spent.
4. It may lead to inflation.

GOVERNMENT ASSERTIONS

At the time of presenting the Bill, the government emphasized that the GST will replace the current Sales Tax and Service Tax (SST) which has been in force for decades. The proposed rate for GST is 6% while that of sales tax and service tax ranges from 6% to 10%.(JALA, 2013; Liew, 2013). In determining the tax rate, the government is considering a number of factors like current rate of sales tax and service tax, social and economic considerations, exemptions and zero-rating, compliances costs, rates in other countries that implemented GST amongst others (Nor Hafizah and Mansor, 2013). The government also reiterated that the GST will lower the tax burden of consumers. Basic needs like rice, sugar, flour, cooking oil, vegetables fish, meat, egg, and essential services like public transport, education, health , residential properties agricultural land etc. will not be subject to GST as these items will be included in zero rated supply or exempted supply (Beh and Ng, 2013) .

Another criticism is that if GST is introduced, the people will be taxed twice, once when they earn income and another when they buy commodities and services. However, in the current tax system also the citizens are paying tax when they consume goods or services. As the tax is embedded, they are not aware of it. Currently, there is a 5% to10% sales tax on manufactured and imported goods and a 6% service tax on various prescribed services by prescribed establishments (services by professionals, food and beverages at food outlets). Goods manufacturers and service providers charge and collect the taxes and remit them to the Royal Customs and Excise Duties Department. The end consumer generally does not see the sales tax as it is a business to business tax paid at the manufacturing or wholesale level. However, one usually experiences service tax when patronizing outlets such as McDonald's or Starbucks.

The government acknowledges that inflation will increase from the current rate of 1 to 2% to 3% but will moderate at 1 to 2% by 2016 to 2017. Australian Commonwealth Treasury and various State Treasuries estimated and measured the inflationary effect of the GST on goods and services included in consumer price index and found that the impact was a one-off event which was effected in the quarter of GST introduction and the magnitude of the effect varied within a small range of 2.50 to 3% among different states (Huang and Liu, 2013). Further evidence in Australia shows that the price increase stabilised very quickly and there is no evidence of GST having an ongoing inflationary effect (Drum and Edwards, 2007).

The major source of government revenue is from petroleum and income tax. GST will be a sustainable source of revenue to the government and will reduce the dependence on revenue from oil and income tax. Increased revenue will help the government to provide more socio-economic programmes.

The introduction GST in Malaysia intends to achieve the following benefits. It avoids tax cascading, multiple taxation, transfer pricing bias, enhance tax compliance, reduce tax avoidance and tax evasion, implement self-policing, lessen the bureaucratic red tape, lower administrative cost, reduce the cost of doing business by providing tax credit on business inputs, enhance Malaysia's competitiveness in international market and improve efficiency(Nor Hafizah and Mansor, 2013).

GST is more compelling as it increases the government revenue. Being a tax on consumption it captures these who cleverly evaded income tax, when they consume goods or service. GST mechanism which gives credit for input tax minimises evasion of tax. The increased tax base of GST will bring more stable and reliable source of revenue (Narayanan, 2014). GST is an efficient and easy to implement tax system that can meet the objective of governments in broadening the tax base (Ramli et al., 2013).

GST is one measure of the holistic programme to overhaul the financial system of the government. It improves tax collection efficiency and under the system, a registered business can claim input tax on its purchases only if proper accounts are maintained. This compels businesses to maintain proper accounts. The major challenge that has been faced by many governments that has successfully introduced GST is to convince the sceptical electorate that the long-term benefit of GST will outweigh the short term pain (Drum and Edwards, 2007).

What is GST?

GST is a broad-based consumption tax. It is an indirect tax which a person pays when he spends money. It is a multi-staged value added tax, which means tax is charged on every supply of taxable goods and services at all levels in the supply chain i.e. production, manufacturing, wholesale and retail. More than 120 countries have already implemented GST which is paid by customers when they purchase goods and services are more sophisticated than the tax on retail sale (Gren, 2001). GST is a Value Added Tax (VAT). Even though GST is charged at each level of the supply chain, each business in the supply chain will charge tax only for the value he adds to the product in the supply chain. It will not become part of cost of the product as GST paid on business inputs is a tax credit claimable by registered businesses.

HOW GST WORKS

GST is collected and paid at all stages of the supply chain. All businesses pay GST when they buy supplies, assets or services for running their business. GST registrants will charge and collect GST on taxable goods and services they provide (taxable supplies). The GST paid on their purchases (input tax credit) will be set off from the GST they charged and collected (output tax). If the output tax exceeds the input tax, the difference is to be remitted to the customs authorities. On the other hand, if output tax is less than the input tax, a refund will be given by the Customs authorities. The ultimate GST is borne by the end consumer.

Example

A merchant who is a GST registrant buys timber from households for RM6,000. He will not pay GST (input tax) as households are not registered for GST. The merchant adds value of RM500 and then sells the timber to a furniture manufacturer for RM6890 ($6,500 + $390 assuming GST is 6%). The manufacturer uses the timber to make furniture

Table 1: GST collection and payment schedule

Details	Purchase price	Value added	Selling price	GST 6% on selling price	GST inclusive selling price	Input tax paid on purchase	Tax Paid to Tax office
Merchant Purchases Timber from households	$ 6000	$500	$ 6,500	$ 390	$ 6890	Nil	$ 390
Furniture Manufacturer	$ 6,500	$ 2,000	$ 8,500	$ 510	$ 9,010	$ 390	$ 120
Wholesaler	$ 8,500	$800	$ 9,300	$ 558	$9,858	$510	$ 48
Retailer	$9,300	$ 2,700	$ 12,000**	$ 720	$ 12,720	$ 558	$ 162
Consumer	$12,700	**Nil**	Nil	Nil	Nil	**$720 Total tax collection by Tax office**	

and adds value of RM2,000. He sells to a wholesaler for RM9,010 (RM8,500 + RM510 GST). The wholesaler adds value of RM800 and sells it to a retailer for RM9,858 (RM9,300 + RM558 GST). The retailer then adds value and sells the furniture to consumers for RM12,720 including RM720 GST. The customer buys it for RM12,720 for his personal use and ultimately bears the GST burden of RM720 which is the total tax paid by each business at different stages. Table 1 shows GST collection and payment schedule.

CLASSIFICATION OF SUPPLY

One of the major criticisms of GST is that it leads to an increase in the price of essential commodities. Classification of supplies into standard rated, zero rated and exempt supply seeks to address this concern. GST can be charged only on taxable supply made by a registered business. To be a taxable supply, a supply must either be standard rated or zero rated; exempt and out of scope supplies are not taxable supplies (Department RMC, 2014).

Standard supply

Standard-rated supplies are goods and services that are charged GST with a standard rate. GST is collected by the businesses and paid to the government. The tax payer can also claim a credit for the input tax he paid on his business purchase. If their input tax is bigger than their output tax, they can recover back the difference (Department RMC, 2014),

Zero rated supply

These are taxable supplies that are subject to a zero rate. Businesses are eligible to claim input tax credit in acquiring these supplies, and charge GST at zero rates to the consumer (Department RMC, 2014). These are taxable supply but the rate of GST is zero. It means a registered business cannot charge a tax from his customers, but he can claim credit for the GST he paid on his business inputs. The government is proposing to include most of the basic food items like rice, sugar, flour, cooking oil, vegetables fish, meat, egg, etc. under this category so that they will not be subject to GST.(Beh and Ng, 2013). The government can prevent increase in price of basic food items and basic services by including them under zero rated supply.

Exempted supply

These are non-taxable supplies that are not subject to GST. Businesses are not eligible to claim input tax credit in acquiring these supplies, and cannot charge output tax on the consumer (Department RMC, 2014). A business can neither charge GST on the supplies classified as exempted supply nor can't they claim a credit for the input tax they paid for business inputs. As the business cannot claim credit for input tax it will impact the price of such supplies.

The draft 2014 Budget proposes that certain financial services, essential services like public transport, public education, health services, residential properties, agricultural land, supply of the first 200 units of electricity per month for domestic consumers etc. will be GST-exempt supplies (Beh and Ng, 2013).

Supply outside the Scope GST

There are some transactions which are outside the scope of GST. Supply by state and federal government and supplies by local authorities and statutory bodies in relation to regulatory and enforcement function are outside the scope of GST. Non-business transactions and services provided by the Government are also outside the scope of GST. The bill also promotes certain tax-free areas within Malaysia, which include supplies made in Labuan, Langkawi and Tioman (Beh and Ng, 2013).

The classification of supply is the tool the government can use to control the price of a particular supply. The government can classify and make changes in the classification of supply according to requirement and conditions.

Tax invoice

A registered business that makes taxable supply has to issue tax invoice within 21 days after the supply. Tax invoice is also needed to claim credit for input tax paid on purchase of business inputs. The tax invoice must contain the details as specified by the act depending on the type of tax invoice. A business can use a simplified tax invoice, with the approval of the Director General of customs, if the value of the invoice is less than RM500. Simplified tax invoice must include the following information.

1. The name (or trade name), address and GST identification number of the supplier;
2. The date of issuance of the invoice;
3. The invoice serial number;
4. A description of the goods and/or services supplied;
5. The total amount payable including the total tax chargeable; and
6. For each rate of tax chargeable, the gross amount payable including tax and the tax rate applicable (Department RMC, 2014)

If the value of invoice is more than RM500 more information are required in the invoice thus:

1. The words 'tax invoice' in a prominent place;
2. The invoice serial number;
3. The date of issuance of the invoice;
4. The name (or trade name), address and GST identification number of the supplier;
5. The name and address of the recipient of the supply;
6. A description of the goods and/or services supplied;
7. The quantity or volume of the goods and/or services supplied, for example, litres of petrol, kilos of meat or hours of labor;
8. Any discount offered;
9. The total amount payable excluding tax, the rate of tax and the total tax chargeable shown as a separate amount;
10. The total amount payable including the total tax chargeable.(Department 2014)

Conclusion

GST is a sustainable revenue source for the Malaysian Government, which now depends heavily on income from the petroleum industry and income tax. The concerns of the public that GST will cause price inflation should hold true in the initial stage but from the experience of some 160 other countries which have implemented GST, it shows that such inflationary effect will stabilize. The success of GST depends on convincing the skeptical electorate that in the long-run GST can benefit them. The categorizing of supplies into taxable, zero rated and exempt supplies seek to address such concerns to some extent. If properly implemented, the tax system will help the government to increase its revenue by expanding the tax base and at the same time manage the tax burden of the public to a greater extent than under the current Sales Tax and Service Tax system.

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