



Income Tax How It Affects You

Ladies and Gentlemen,

Persatuan Wanita Universiti

UNIVERSITI MALAYA

Seminar On Income Tax Laws

Income Tax: HOW IT AFFECTS YOU

Basis Of Malaysian Income Tax by

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Ladies and Gentlemen,

This paper seeks to lay out for participants of this seminar the general principles of Income Tax law in this country. This is done with the objectives of making participants of this seminar aware of the relevant provisions of the Income Tax Act 1967 and other relevant legislation and how they can affect us all. For those who have been working without paying any income tax or under declaring their income to the revenue authorities, the maxim "Ignorance of the Law is no Excuse" (Ignorantia Legis neminem excusat) is only too true to them. These people will inevitably be jolted from their bliss when the revenue authorities come down hard on them with a tax demand spread over a few years amounting to a good few thousand ringgit, if not more.

Basis Of Malaysian Income Tax

The Income Tax Act, 1967 (Act 53 Revised 1971) is the current legislation governing the imposition of income tax in this country. Section 3 of the Act provides as follows:

Para 28 Schedule 6, Income Tax Act, 1967. Section 7 of the said Act determines the resident status of an individual taxpayer. It should be noted that citizenship of an individual is irrelevant in determining his resident status. For companies and trade associations, section 8 of the Income Tax Act, 1967 applies. Section 8 of the Income Tax Act, 1967 provides that:

"Subject to and in accordance with this Act a tax to be known as income tax shall be charged for each year of assessment upon the income of any person accruing in or derived from Malaysia or received in Malaysia from outside Malaysia."

Income which is exempt from tax is provided for in

Schedule It can be seen that it is only income accruing in or derived from Malaysia that is taxable under the Income Tax Act 1967, whether a taxpayer is resident in Malaysia or not. Income derived from outside Malaysia is not taxable unless it is remitted to Malaysia by a resident taxpayer.¹

Section 4 of the Act provides for the classes of income on which tax is chargeable. Briefly, tax is chargeable on income from business, employment, dividends, interest, rents, royalties, pensions, annuities and gains or profits not falling under any of the foregoing classes of income. In the Privy Council case of Director-General of Inland Revenue v A L B Co Sdn Bhd² it was held that the various paragraphs of section 4 which sets out the different classes of income overlap each other. In other words, rentals from the letting of property may be regarded as constituting income from a business source under paragraph (a) of section 4 notwithstanding that such rentals may also be classified as rents under paragraph (d) of the same section. Thus, the various paragraphs in section 4 are not mutually exclusive. Instead, there is room for overlapping between one paragraph and another.

¹ Para 28 Schedule 6, Income Tax Act, 1967. Section 7 of the said Act determines the resident status of an individual taxpayer. It should be noted that citizenship of an individual is irrelevant in determining the resident status of an individual taxpayer. For companies and bodies of persons (such as a club, society and trade association) their resident status is determined under section 8 of the Income Tax Act, 1967.

² [1979] 1 MLJ 1.

Income which is exempt from tax is provided for in Schedule 6 to the Act.

The Income Tax Act, 1967 employs the preceding year basis of taxation. Thus, income which is to be charged to tax for a particular year of assessment is that earned in the basis year which is the calendar year immediately preceding the year of assessment. For example, the tax for the year of assessment 1986 is based on the income earned in the calendar year 1985.³

Who Is Liable To Pay Tax

Taxation Of Individuals

The Income Tax Act 1967 imposes tax on individuals, bodies of persons (such as clubs, societies and trade associations), companies and trusts.

In the case of an individual, he will be taxed in his name⁴ and in the case of an incapacitated person in the name of the person having the direction, control and management of the property or affairs of the incapacitated person.⁵ Following the death of an

³S 20.

⁴S 66.

⁵S 69(1). If an incapacitated person happens to be a minor, he may be assessed and charged in the name of his parent or guardian or in his own name (S 69(3) and (4)).

⁶Ss 3 and 75. See the definition of "person" in section 1 of the Income Tax Act, 1967.

individual, the deceased's estate is liable to tax and the executor or administrator will have the responsibility to account for his taxes.⁶ For a trust, the income of the trust body will be liable to tax on the trust body and the trustees thereof, so long as they remain to be so, are responsible for all liabilities.⁷ As for bodies of persons, they are also liable to tax and the responsibility lies with the principal officer such as the manager, treasurer and secretary.⁸ In the case of a company, it will be liable to tax in its own name by virtue of its legal entity.⁹

Taxation Of Individuals

In the case of individuals, it is important to determine the resident status. An individual who is resident in Malaysia for tax purposes will suffer income tax at graduated scale rates on his chargeable income as set out in Schedule 1 to the Act. Resident status is quantitatively determined by section 7 of the Income Tax Act 1967. At present, the scale rates ranges from 5% on the first \$2,500 ringgit of the chargeable income to 40% for chargeable income exceeding \$100,000 ringgit. This graduated scale of tax also apply to a wife who has elected for separate assessment. In addition to income tax,

⁶S 74.

⁷S 73.

⁸S 75.

⁹Ss 3 and 75. See the definition of "person" in section 2 of the Income Tax Act, 1967.

an excess profit tax of 5% is also levied on the chargeable income of an individual which exceeds \$300,000 ringgit.¹⁰ Where the wife has elected for separate assessment, the \$300,000 ceiling is apportioned between the husband and the wife by reference to the fraction arrived at by dividing the chargeable income of the husband or the wife over their total chargeable income.¹¹

For a non-resident individual taxpayer, a flat rate of 40%¹² is imposed. If an individual derives income from a business source or from rental received from the letting of properties situated in Malaysia, a further tax known as development tax is leviable at the rate of 5% in respect of development income exceeding \$5,000.¹² In the case of separate assessment, both the husband and wife will each obtain \$5,000 exemption.

If the non-resident taxpayer is a Malaysian citizen, he will be given. In the case of income derived from overseas which is remitted to Malaysia to a resident individual, a double taxation relief in respect of income which has suffered tax in a country which has a tax treaty with Malaysia will be granted to the said individual. The double taxation relief will be given to the extent of the tax that is suffered in the foreign country on income that is brought to tax in Malaysia subject to the incidence of tax in

¹⁰S 3A.

¹¹S 45(6).

¹²S 16(b), Supplementary Income Tax Act, 1967 (Act 54 Revised 1971).

Malaysia.¹³ For income derived from a country which does not have a tax treaty with Malaysia and which is received and taxed in Malaysia, a unilateral relief will be given which is equivalent to half of the foreign tax suffered on such income or the effective tax suffered in Malaysia, whichever is the lower.¹⁴

For a non-resident individual taxpayer, a flat rate of 40%¹⁵ is imposed on his chargeable income without any deduction of personal reliefs. As is the case with a resident individual taxpayer, he is also liable to excess profit tax at a rate of 5% on his chargeable income exceeding \$300,000 and a development tax in respect of his development income in excess of \$5,000 if any, at the rate of 5%.

If the non-resident taxpayer is a Malaysian citizen, he will be given a non-resident relief.¹⁶ The relief is the difference between the tax suffered calculated as if he were a resident and the tax he would otherwise pay at the rate of 40% on his Malaysian income. However, non-resident relief would not be given if the tax calculated as if he were resident is in excess of the tax payable at the rate of 40%.

¹³ Para 5, Schedule 7, Income Tax Act, 1967.

¹⁴ Paras 13-15, Schedule 7, Income Tax Act, 1967.

¹⁵ Para 2(b), Schedule 1, Income Tax Act, 1967.

¹⁶ S 130.

²² Para 2(c), Schedule 1, Income Tax Act, 1967.

²³ S 13(1) Supplementary Income Tax Act, 1967.

A non-resident individual is exempted from paying tax on income arising abroad and remitted by him into Malaysia.¹⁷ Furthermore, a non-resident taxpayer is exempt from tax in respect of income from employment exercised in Malaysia for a period or periods amounting to not more than 60 days.¹⁸

Taxation Of Companies

A company deriving income from Malaysia is liable to tax on its chargeable income at the flat rate of 40%.¹⁹ Development tax at the rate of 5% is imposed on a company's business income and rental from property situated in Malaysia.²⁰ In addition, excess profit tax of 3% is levied on a company's chargeable income which exceeds \$2 million ringgit.²¹

Taxation Of Trusts

A trust is liable to tax at the rate of 40% on its chargeable income.²² Where it has development income, it will also be liable to development tax.²³ In this case, however, the exemption of \$5,000

¹⁷Para 28, Schedule 6, Income Tax Act, 1967.

¹⁸Para 21, Schedule 6, Income Tax Act, 1967.

¹⁹Para 2(a), Schedule 1, Income Tax Act, 1967.

²⁰S 16(a), Supplementary Income Tax Act, 1967.

²¹S 3A.

²²Para 2(c), Schedule 1, Income Tax Act, 1967.

²³S 13(1) Supplementary Income Tax Act, 1967.

ringgit will not apply. A trust is also liable to excess profit tax on its chargeable income in excess of \$300,000 ringgit.²⁴

A beneficiary of a trust will be liable to tax on income distributed by the trust.²⁵ However, the beneficiary is entitled to the tax credit attributable to the tax paid by the trust on its chargeable income.²⁶

Taxation Of Body Of Persons

A body of persons such as clubs, society, trade association and a deceased's estate are liable to income tax at scale rates.²⁷ In appropriate cases, development tax and excess profit tax will also be levied.

For co-operative societies, they are exempt from tax for a period of five years commencing from the date of registration and thereafter if the members' funds of the co-operative society concerned are less than \$500,000 ringgit on the first day of the basis period for a year of assessment.²⁸

²⁴S 3A.

²⁵S 61(1)(d).

²⁶S 110(8).

²⁷S 6 and para 1 of Schedule 1 to the Income Tax Act, 1967.

²⁸Para 12, Schedule 6, Income Tax Act, 1967.

A husband is entitled to a deduction of \$2,000 as wife's
Personal Reliefs/Deduction as the wife throughout the year. However,
 where the wife elects for separate assessment, the husband is not
 entitled to any wife relief.³¹

Resident individual taxpayers are given personal reliefs or deduction in arriving at their chargeable income. It should be noted that non-resident individual taxpayers are not given any such reliefs or deduction. This is also the case for companies, trusts, estates under administration and body of persons.
 It should be noted that in cases where the wife is supporting the husband there is no relief given to the wife.

Where there is permanent separation or death, the husband is given a prorated amount based on length of time.³²

(i) Deduction for Individual

An individual is entitled to a personal deduction of \$5,000 ringgit for a year of assessment.²⁹ This is made up of \$4,000 ringgit for the individual and \$1,000 ringgit for dependent relatives. Where the wife elects for separate assessment, both the husband and wife are each entitled to a deduction of \$5,000 ringgit respectively.
 payments cannot exceed \$2,000 ringgit.³³

(ii) Wife Relief

Under section 2 of the Income Tax Act, 1967, a wife is defined as "a woman (whether or not she has gone through any religious or other ceremony) is regarded by virtue of any law or custom as the wife of a man or as one of his wives".

²⁹S 46.

³²S 47(i) provision.

³³S 47(i).

For tax purposes, the wife's income is aggregated with that of the husband's income and the total amount is taxed jointly. The relief³⁰ where he maintains the wife throughout the year. However, where the wife elects for separate assessment, the husband is not entitled to any wife relief.³¹ Separate assessment is more fully discussed in the next seminar paper.

It should be noted that in cases where the wife is supporting the husband, there is no relief given to the wife.

The Income Tax Act, 1967 defines "child" to mean a legitimate child or Where there is permanent separation or death, the husband is given a prorated amount based on length of time.³² is not given to a taxpayer in respect of his illegitimate child although in practice

child-rel Where the husband has made payments of alimony pendente lite or made alimony or maintenance payments in accordance with a court order or deed of separation, such payments are allowed as relief to the husband but the total of the relief given as wife relief and alimony payments cannot exceed \$2,000 ringgit.³³ at any time in that basis

Alimony paid to the wife pursuant to a deed of separation or court order is income of the wife under section 4(e) of the Income Tax Act, 1967. years at the beginning of the year for

which a claim is being made.³⁷

³⁰S 47.

³¹S 47(4).

³²S 47(1) proviso.

³³S 47(3).

³⁷S 48(1)(a).

For tax purposes, the wife's income is aggregated with that of the husband's income and the total amount is taxed jointly.³⁴ The wife could, however, elect to have her employment or professional income assessed separately.³⁵ Separate assessment is more fully discussed in the next seminar paper.

(iii) Child Relief

The Income Tax Act, 1967 defines "child" to mean a legitimate child or stepchild of the taxpayer or a child who has been legally adopted by the taxpayer.³⁶ Accordingly, child relief is not given to a taxpayer in respect of his illegitimate child although in practice child relief is given for such a child when the parents get married subsequently.

A resident individual taxpayer is given child relief if he pays (wholly or in part) for the maintenance at any time in that basis year of

- a) a child who is unmarried and below sixteen years at the beginning of the year for which a claim is being made.³⁷

³⁴S 45.

³⁵S 45(4).

³⁶S 48(9).

³⁷S 48(1)(a).

b) a child who is unmarried and above the age of sixteen years and is receiving full-time instruction at any educational establishment.³⁸

c) a child who is unmarried and serving under articles or indentures with a view to qualify in a trade or profession.³⁹

d) a child who is unmarried and above the age of sixteen years and not receiving full-time instruction at any educational institution by reason of physical or mental disability.⁴⁰

The term "unmarried child" was considered in the case of Director-General of Inland Revenue v T.⁴¹ The issue in this case was whether an annulment of a marriage reverted a married woman to that of an "unmarried child" so as to qualify for child relief. The marriage in this case was annulled on the ground of the wilful refusal of the daughter of the taxpayer to consummate the marriage. The learned trial judge held that the annulment of the marriage did not revert the daughter of the taxpayer to the status of an unmarried

³⁸S 48(1)(b).

³⁹S 48(1)(c).

⁴⁰S 48(1)(d).

⁴¹[1974] 1 MLJ 99.

child because wilful refusal to consummate the marriage renders the marriage voidable and not void ab initio. In other words, there is a valid marriage until the court sets it aside.

Under the Income Tax Act, 1967, child relief is given as follows:⁴²

First child	\$650 ringgit
Second child	\$750 ringgit
Third child	\$800 ringgit
Fourth child	\$800 ringgit
Fifth child	\$800 ringgit

For each handicapped child, the relief given is \$400 ringgit.

It should be noted that if the child is studying overseas in a university, college or other educational establishment similar to a university or college, the taxpayer concerned can claim child relief to a maximum of four times the normal child relief or the amount so expended whichever is the lower.⁴³ However, no child relief will be given if the child has income in his own right exceeding the child relief due.⁴⁴

⁴²S 48(2)(a).

⁴³S 48(3).

⁴⁴S 48(5).

(iv) Deduction For Insurance Premium And

Pro It is important to note that overseas education does not include education in Singapore.⁴⁵ However, taxpayers in Sabah and Sarawak can make a claim for increased child relief for their children together is \$3,500 ringgit per annum only which applies to insurance premiums and provident fund contributions made by both the husband and wife. The insurance premium and the contributions made by the wife are deemed to be paid by the husband.⁵⁰ In the case of separate child for purposes of child relief.

Nevertheless, the total reliefs given to the wife and husband should not exceed \$3,500 ringgit.⁵² The amount for child relief is deducted from the total income of the husband to arrive at his chargeable income for tax purposes. Where the wife elects for separate assessment, no child relief is allowed to her eventhough she may have made payments for the life of either the husband or wife or their joint lives.⁵³ As the child's maintenance.⁴⁷

Where the parents are divorced, the child relief due may be apportioned between the parties in the ratio of each contribution over their total contributions.⁴⁸

⁴⁵S 48(3)(a).

⁴⁶S 48(3)(b).

⁴⁷S 48(1) proviso.

⁴⁸S 48(4). and (c).

⁵³S 49(3).

⁵⁴S 49(2)(a).

(iv) Deduction For Insurance Premium And
Provident Fund Contributions

The maximum deduction allowed for these payments considered together is \$3,500 ringgit per annum only, which applies to insurance premiums and provident fund contributions made by both the husband and wife.⁴⁹ The insurance premium and the contributions made by the wife are deemed to be paid by the husband.⁵⁰ In the case of separate assessment, however, the actual payments made by the wife are allowed to her.⁵¹ Nevertheless, the total reliefs given to the wife and husband should not exceed \$3,500 ringgit.⁵²

The insurance premiums that may be deducted should be on the life of either the husband or wife or their joint lives.⁵³ As such premiums for motor insurance policy or a policy against fire and theft of property will not qualify. The premiums under an insurance policy which qualify for deduction are limited to 7% of the capital sum payable on death.⁵⁴ Thus if the capital sum payable on death is \$20,000 ringgit, the maximum amount of the premiums paid which would be allowed is 7% of \$20,000, that is, \$1,400 ringgit. Any portion of the premiums paid which is in excess of \$1,400 ringgit will not be allowed.

⁴⁹S 49(1).

⁵⁰S 50(3)(b) and (c).

⁵¹S 50(4).

⁵²S 49(1) proviso.

⁵³S 49(3).

⁵⁴S 49 (2)(a).

In regard to contributions to provident or pension fund, they would be allowed as a deduction if the payments made are obligatory and such payments are made to such a fund approved by the Director-General of Inland Revenue.⁵⁵

It is important to note that the various deductions and reliefs referred to above, in order to be deductible, must be claimed by the taxpayer concerned.⁵⁶

Double Taxation Agreements

Tax Rebate

Currently, Malaysia has agreements for avoiding double taxation with the following 20 countries: Singapore, Japan, Denmark, Sweden, Norway, United Kingdom, France, Switzerland, Sri Lanka, Belgium, New Zealand, India, Canada, West Germany, Finland, Australia, South Korea, Philippines, Pakistan, Bangladesh, East Germany, Italy, Iceland, Thailand, Romania and China.⁵⁷

Where the taxpayer's wife elects for separate assessment, the wife is still entitled to a rebate of \$30 ringgit if her chargeable income does not exceed \$10,000 ringgit.⁵⁸

In the case of a taxpayer who has been allowed a deduction for wife relief or for payment of alimony or maintenance, a rebate of \$30 ringgit is granted to him where his chargeable income does not exceed \$10,000 ringgit.⁵⁹

⁵⁵S 49(2)(c).

⁵⁶S 51.

⁵⁷S 6A(2)(a).

⁵⁸S 6A(2)(a) proviso.

⁵⁹S 6A(2)(b).

A rebate is also granted in respect of any zakat, fitrah or any other Islamic dues, the payment of which is obligatory. The payment must be evidenced by way of a receipt issued by the appropriate religious authority.⁶⁰

Where the rebate exceeds the income tax charged, the excess is not paid to the individual nor can it be carried forward.⁶¹

Double Taxation Agreements

Currently, Malaysia has agreements for avoiding double taxation with the following 26 countries: Singapore, Japan, Denmark, Sweden, Norway, United Kingdom, France, Switzerland, Sri Lanka, Belgium, New Zealand, India, Canada, West Germany, Poland, Australia, South Korea, Philippines, Pakistan, Bangladesh, East Germany, Italy, Finland, Thailand, Romania and China.

Basically, most of the agreements between Malaysia and these countries follow the source principle⁶² but with exceptions. Some of the basic principles found in these agreements are as follows

⁶⁰S 6A(3).

⁶¹S 6A(4).

⁶²That is, income derived from Malaysia will be taxed in Malaysia.

- (a) tax is leviable on business profits only if the enterprise of the other State has in Malaysia a "permanent establishment".⁶³ Furthermore, the tax is leviable only on "so much of that income as is attributable to the "permanent establishment".

Tax Returns And Assessments

- (b) tax is also leviable in Malaysia on other sources of income according to the various Agreements. The general principle adopted is the source principle whereby income derived from Malaysia will be taxed in Malaysia and not the resident principle under which tax is leviable only in the country of the recipient's residence.

- (c) income on which tax is leviable in Malaysia may be exempt in the other country. In cases where the income is also subject to tax in the other country, some relief may be given in the other country.

⁶³The concept of "permanent establishment" includes, inter alia, a place of management, a branch, an office, a factory, a workshop, a warehouse, a mine, oil well and a quarry.

- (d) Where an item of income is accorded special treatment under the double tax agreements, the tax consequences follow that of the double taxation agreements and not that of the provisions in the Income Tax Act, 1967.

Tax Returns And Assessments

Section 77(1) of the Income Tax Act, 1967 provides that a person who receives a tax return should complete and submit the tax return within the time period specified therein (not being less than 30 days from the date of service of the notice) to the tax authorities. A person chargeable to tax who has not receive his return forms from the tax authorities due to various reasons is under a duty to give notice to the Director-General of Inland Revenue within 14 days after the expiry of March for that year that he is so chargeable.⁶⁴ Failure to do so will bring grave consequences such as the imposition of a penalty.⁶⁵

The duty is on the taxpayer to furnish his tax returns. Contrary to popular belief, it is not the duty of the Inland Revenue

⁶⁴S 77(2).

⁶⁵S 112(3).

Department to send the taxpayer the return forms. Accordingly, it is not true that where no form is received, no tax is payable.

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by

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National Tax Director
HRM (Tax Services) Sdn. Bhd.

in

Association with
Touche Ross International

Saturday, 2nd August 1986. At Rumah Universiti, Universiti Malaya.