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Goods and Services Tax (GST) Governance in the Malaysian New Tax Environment

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Abstract

The government had implemented Goods and Services Tax (GST) starting from 1st April 2015 with 80% to 90% compliance from a taxable person on the first day of its execution with little commotion from end customers. The understanding and awareness of people and taxable person about GST can be seen from the success of the advertisements and programs held by the Royal Malaysian Custom Departments (RMCD) and other government agencies throughout 2014 onwards. GST is known as a multi-stages tax affected to each stage of products or services circulation. In other words, there will be 6% tax imposed on all goods and services with some exception on certain items. Therefore, RMCD shall look after GST governance to ensure that taxable entities are continuously complying with all the regulations enforced under GST Act 2014, GST Rules 2014 and GST Order 2014. The efficiency and effectiveness of tax collection are very important for government to support the socioeconomic development of the country. GST governance as a process in guiding an entity with regards to their tax responsibilities will lead the entity to be more concerned about their contributions to the nation building. This study discusses the GST governance from overseas practices such as governance and risk management, processing and reporting, resources and capabilities and assurance that can be adapted into Malaysian context for best practice actions. It will contribute to the GST literature from the Malaysian perspective which might differ from other countries.

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Keywords: Goods and Services Tax; governance; risk management; compliance; assurance.

1. Background of Goods and Services Tax in Malaysia

Malaysia is moving from Sales and Service Tax (SST) to Goods and Services Tax (GST) starting from 1 April 2015 as one of the government's effort to become a high income nation in tandem with Vision 2020, New Key Result Area (NKRA) and 11th Malaysia Plan 2015- 2020. GST is a consumption tax levied on goods and services at multi stages of businesses while SST levied at a single entry. It has been implemented in 169 countries worldwide. It has started to become a subject of interest when it was first introduced in France in the 1950s. An announcement by

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Prime Minister and Minister of Finance of Malaysia, Dato Seri Najib Bin Tun Abdul Razak during the 2014 Budget on 25th October 2013 stated that GST will be implemented at 6%. GST for Malaysia will be governed by GST Act 2014, GST Regulation 2014 and Goods and Services Tax Order 2014.

The objectives for GST to be introduced in Malaysia are twofold; as first, to enhance the revenue collections and second is to use the GST system as a mechanism to mitigate transfer pricing manipulation (BNM, 2013). Both aims are to reduce the tax collection leakage that has happened yearly. Failure to meet both objectives will make tax collection leakage happen continuously. Furthermore, it will affect the distribution of government allocation for the social, economic and country's development programs. It is because efficient and effective tax collection is a prerequisite for our country's welfare programs. Therefore, GST governance may help Royal Malaysian Custom Department (RMCD) to manage the GST efficiently.

RMCD was appointed under Ministry of Finance (MOF) to handle all the legislations with regard to GST implementation starting from the law enactment creation to the law enforcement for wrongdoers. Achieving higher revenue collection through voluntarily high compliance among taxable person is certainly preferable for them in order to meet the GST objective. A simple and stable system will help the tax administrations to collect taxes from the public. Hence, RMCD will only need to put an extra effort on those taxpayers who try to evade taxes.

1.1. Good and Services Tax Governance

Governance refers to the process of interaction and decision making among the people undertaken by any formal or informal institution that leads to the formation, reinforcement or reproduction of social norms and institutions (Bevir 2013). In the public context, it can be defined as the government's ability to make, enforce laws and provide goods and services to the public regardless of any constitution they hold (Fukuyama 2013). The issue of governance has become the headlines of the world and economic business press in a few years back until now, especially in the U.S, UK, Continental European Countries and West Asian Countries (Al-Janadi, Rahman, & Omar, 2013) due to some bankruptcies and business failures among giant companies worldwide in the early of 2002.

Governance in taxation is considered as informative context in which key issues of tax evasion and tax avoidance can be reduced if the government knows how to tackle the problems (Morrell & Tuck 2014). However, it is not a simple process due to the legal framework surrounding the system and also the pressure between enforcement and compliance. It is also linked with mutual relationship with other government agencies and regulatory bodies. Governance in GST can be discussed from many angles which cover the same part of corporate governance. Internal control and monitoring system inside the organisation, technology being used and policy and procedures are the examples of governance that can be discussed in the taxation.

Governance will shape the tax system of the country. Taxes are raised for the development of the society in terms of education, military, infrastructure, economic growth and so on (Everest-Phillips & Sandall 2009). Good governance will deliver a good tax system and a better revenue collection. Good governance will depend on efficient administration; trust in government and political stability. Lack of the three conditions mentioned will make the development of effective and efficient tax system slow. However, studies on tax governance have only received a little attention in international economy area.

There are discussions on global tax governance since there are borderless in doing business nowadays (Rixen 2011b). Global tax governance will require government in each country to pool and delegate some of their tax autonomy to worldwide level and restraint the reality that taxation should be solely belonged to their own country. Since there is World Custom Organisation established in 1994, the discussion might be realistic in the future.

2. The application of GST Governance Worldwide

History of Goods and Services Tax or some countries called it as a Value Added Tax (VAT) began in France in the 1950s (Lin, 2008; Palil & Ibrahim, 2012). Presently, 160 companies were implementing Goods and Services Tax as a part of their indirect tax collection. A variety of VAT rates are used worldwide with the highest rate is for Gambia at 40%, Argentina and Belgium at 21%, Bulgaria, Austria, United Kingdom and Albania at 20%, Cameroon 19.25% Angola and Australia at 10%, Singapore 7% and the lowest goes to Canada, Niue and Nigeria at 5%. Most countries are using a simple structure comprised of a few rates and a few codes such as Japan and Nigeria (Ezeoha & Ogamba, 2010; Onji, 2009). Japan implemented VAT in 1989 and the tax was uniform at 5% with a few items exempted (Onji, 2009). As for Nigeria, VAT rate is at 5% of all eligible goods and services (Ezeoha & Ogamba, 2010). However, GST rate does not indicate that the government manage their revenue and expenses efficiently. It all depends on the government structure itself.

Countries worldwide can be separated between the high, middle or low tax performers. Examples of high tax performers worldwide include the United Kingdom, USA, Australia, Denmark, Brazil, Oman, United Arab Emirates and Guyana. Many Latin America and Caribbean countries such as Venezuela, Guatemala, Panama, Paraguay and Colombia are in the group of low tax performers while Bangladesh, Pakistan, Nepal, Malaysia, Cambodia, Indonesia, Laos, Sri Lanka, India and the Philippines represent South and Southeast Asia as low tax performing countries (Von Haldenwang & Ivanyna 2012). Malaysia is in the list because the focus is on non-tax revenue collection.

It is proven that tax compliance is low among developing countries where people neither believe that the government looks after their interest nor trust that the revenue is used wisely (Everest-Phillips & Sandall 2009). For example, less than 25 percent of Latin American citizens believe that taxes are well spent. It shows people's lack of trust to the government in handling their collection. Low trust undermines a weak legitimacy of the government from the public views. It will make the tax collection less cost effective and finally reduces the revenue to be distributed for public spending.

In the UK, value added tax (VAT) handled by the Her Majesty Royal Custom (HRMC) and they are required to change for a better process due to competitiveness in the world market (FTSE tax director, D3, 2006). They have to be concerned with the overseas traders and foreign direct investment (FDI) if they want to compete with other countries, even though some scholars claim that FDI is not affected by tax policy (Rixen 2011a). The rationale of UK shifting from existing indirect tax system to GST on 1973 was due to promotion of harmonisation as a prerequisite for entry in the common market environment of Continental Europe, reduction of tax burden on exports and most importantly is the self-enforcing system as opposed to other tax system (Jamaludin & Ming Ling 2012). It is similar to other countries such as Malaysia, in which GST might be the best solution to promote harmonisation since all its regional partners other than Brunei and Myanmar have already established GST in their own countries.

For Australia that has more complex system than a few countries such as Singapore and New Zealand, having a higher marginal tax rate is required to support their government programs (Bobek, Roberts, & Sweeney, 2007). Thus, tax governance shall be effective and efficient to manage all related processes with regards to VAT. It was introduced in Australia on 1st July 2000 with the aim to promote economical collection, neutrality, simplicity, economics of growth and efficiency. They wanted to shift from heavy reliance on direct tax to indirect tax as to simplify the system. However, rather than broadening the existing tax based, their objective to be a simpler tax system becomes more complicated due to the system which does not introduce a consumption tax (Jamaludin & Ming Ling 2012). The Australian Tax Authorities has also failed to analyse the simplification of tax changes from social perspective and underestimated the compliance cost increasing for business person which differ from their existing system. Therefore, Australia is still struggling to rectify the issues surrounding their tax system.

Singapore introduced GST on 1st April 1994 with the same purpose to shift the tax burden from direct tax to indirect tax as well as to enhance the market competitiveness in the regional area. Their rate currently is at 7% modelled from New Zealand's system with only one positive rate. Zero rating is limited to export products and some specific international services. Strong economic condition with large budgetary surplus helps Singapore to establish a modern and efficient tax system in the country. They efficiently use the tax collection received to narrow down the gap between the low and the high income families. Therefore, Singapore can be a good role model to other countries wishing to reform their tax system.

In other developing countries, tax collection might be low because they have an alternative collection from other sources of finance or due to societies have chosen to limit the action by their government. It is also shaped by other conditions such as natural disaster or long term violent conflicts inside the country (Everest-Phillips 2010). Societies with low level of governance are particularly hard to believe in terms of their transparency, democratic and capable decision making. In some cases, some powerful groups are imposing tax governance, according to their interest or initiate a tax reform obstruction (Von Haldenwang & Ivanyna 2012).

If the public sector is governed in a democratic and transparent manner, the tax collection will not be an issue in that country. From the World Governance Indicators (WGI) Voice and Accountability index, which has been used to determine whether the public policy and democratic political being are implemented effectively, a few countries such as Singapore, Malaysia, Bahrain, Kuwait and Qatar are considered as democratic countries but low on voice and accountability scores. Therefore, they fall under borderline cases. On the other hand, if the tax revenue spends fairly for the sake of the society, the confidence level of the taxpayer will increase and the compliance level will get higher. Therefore, transparency within the government bodies is very important to build up confidence among the taxpayer and the public.

3. The Effectiveness and Efficiency of GST Governance Implementation

Efficiency and effectiveness of GST governance are important to enhance the reliability and expectation from the society. The objective of a tax transformation designed from Sales and Service Tax with GST is to build transparency of their responsibility. Transparency can be built by publishing an accessible tax regulation, such as GST Act 2014, GST rates and exempted goods procedures for GST process. Therefore, it may constrain the tax officer from wrongdoing or receiving bribes from the taxpayers.

Public-private dialogue on tax policy through private sector engagement with the government will also enhance the transparency of the RMCD. Visible links between the flows of the tax collection until distribution of the tax revenue will help to increase the compliance rates among the taxpayers. It is because the firms and citizens know how the taxes are used. Training and courses on GST education together with incentive strengthening shall be conducted by the RMCD to all parties with exposure on the benefits received on working in the formal economy and avoiding tax shadow.

In order to do so, the government has to change the perception of the people and taxpayers on the benefits that they will receive with the GST implementation. Convincing taxpayers is not easy but is has to be done to change their perception. Many programs can be set up by the RMCD such as improving outreach as well as services and opening dialogue between public and private to engage the private sector as an external party in the transformation process.

Accountability of GST will help to improve the confidence level among taxpayers. Government should invite many parties such as business, taxpayers associations, media and civil society to participate in any tax policy formulation and implementation. The tax administrator shall be accountable with complaints lodged by the taxpayers and take fast actions through the appeal procedures for any unsatisfactory cases. GST Tribunal was established at the same date of GST implementation in Malaysia and they cater to all minor cases for any disappointing decisions made by the RMCD to the taxpayers. This tribunal will help to expedite the court cases to be solved in a shorter time. However, administration, laws and regulations with regard to GST also shall be simplified.

Among the elements required in the effectiveness of GST governance are implementation of an overall compliance strategy and focus on the audit for the revenue with the largest risk. Compliance among tax payers is very important for RMCD benchmarking. High compliance shows that the tax reforms are successfully implemented and vice versa. Audit program shall be done frequently in order to ensure that the taxpayers are complying with the rules and regulations. Even though there is no indictment towards taxpayers within these two years, audit awareness shall be in place to enhance the understanding of taxpayers and to reduce the mistake done when filing for submission.

In addition, services provided for those who voluntarily pay their taxes and for those who do not should be distinguished. Undeniably, enforcement to comply with taxes will create many excuses to evade tax. Thus, control measures and laws can be used to justify their action. It is not easy for taxpayers to pay the tax voluntarily. Tax morale plays an important role to encourage the taxpayer to carry out their responsibility to the government. Government incentive such as reducing the percentage of corporate tax and individual tax might help to solve the problems. Information received from third parties such as banks, individual, immigration, ministry of domestic trade, cooperation and consumerism shall be used comprehensively to limit the taxpayer's ability to evade taxes (Jensen & Wöhlbier 2012).

4. GST Governance Overview for the Malaysian Tax System

GST governance will help the administrator on their daily work and process. It will help to identify the risk management and assurance process that might happen later. It also will guide the RMCD whether their processes follow the best practice worldwide and it may improve the system if the sign of deficiency is reduced. On the other hand, governance may identify any additional measures that they can take in order to reduce the risk of GST compliance failures. According to the research done by Von Haldenwang & Ivanyna (2012), Malaysia was ranked among a low tax performing country based on the gross domestic product (GDP) last twelve years. Hence, something must be done to improve our tax performance in the future.

First of all, clear documents with regards to policies and procedure must be in place as a guideline for the staff to work on. Top management shall be highlighted about the procedures since they make the final decisions. Later on, documented policies and procedure shall be updated to all staff to reflect changes to the law. This is to ensure that they are aware with the new policies and guideline posted by the management.

While policies and procedures are in place, staff shall implement the input into their daily works. They shall recognise any unusual event or issues that they have to cater before any risk occurrence. Management shall ensure that RMCD officers have clear picture of GST governance and are kept updated with the changes of law. Therefore, one way to increase their understanding is through training or courses conducted by the experts. This is important for resources and capabilities of the human capital building.

RMCD officers also shall have a separate responsibility if the staffing resources are sufficient and available. Segregation of duties is important to reduce internal fraud inside the department since RMCD is in charge of monetary and valuable items. Counter check against each other's work may reduce errors and mistake created unintentionally or intentionally. Technology and computerised system shall be manipulated up to the maximum level. It is to ensure that all information is stored securely, backed-up regularly and installed with anti-software.

Regular test on the accuracy and the reliability of the information systems and internal controls are required for assurance processes. RMCD might compare their actual performance with the benchmarking worldwide to ensure that their practices are in line with World Customs Organisation. Another suggestion to improve governance is by setting up a large taxpayer office within the revenue headquarters. It is because large corporate taxpayers carry the biggest revenues and the biggest risk for tax assessment (Jensen & Wöhlbier 2012)

Parts of the above governance process can be used by other organisation in handling their GST system. Small, medium enterprise, large corporation and other institutions may use the above processes to suit their organisation. Elements of governance and risk management, processing and reporting, resources and capabilities and assurance can be adjusted to improve their GST system.

5. The Impact of Good GST Governance to the Society

Good governance in any institution relating to any process is important for a better performance. The key performance index will be measured by the improvement beyond the effort being done by the organisations which gives an impact internally and externally. External impact on good GST governance will improve the GST ecosystem.

Ecosystem is defined as an interaction between organism and their environment. Therefore, GST ecosystem can be described as GST interaction community which covers all related stakeholders including their environment in the circle. It includes the government as a body to collect and distribute the tax revenue and business organisation as a medium to support the collection process. This is continued with people as the end consumers to pay the GST and also to receive the benefits from it. It also will give an impact to the tax system itself as a part of the environment to be adopted by the people. A good impact on the system will improve the tax system and finally reduce the economic shadow that has always been a big concern in the government assortments.

Issues of tax shadow and tax evasion might be reduced while good governance is implemented in the country. Both issues occur due to misguidance of tax policy as well as the weaknesses of the local and state government (Prinz & Hokamp 2015). On the other hand, transparent government with clear objectives of GST implementation will influence the taxpayer's willingness to pay their tax liability (Everest-Phillips & Sandall 2009). Taxpayers are willing to cooperate for the sustainability of the public because they are also a part of the public.

Sustainability is how the system remains diverse, endurance and productive. It can be seen from the development of the system that gives impact to the society. It will require some interconnection with the economic process, politics and culture. Good tax governance is central to sustainable development because they can mobilise the domestic tax base as a dependency key mechanism for developing countries. By having good tax governance, they may achieve a fairer sharing of the cost and benefits of globalisation. Economic prosperity will only be achieved with cooperation from the government and the public. Therefore, the government shall always negotiate with taxpayers for the better public expenditure policy (Everest-Phillips & Sandall 2009). Cooperation between both parties will increase the tax revenue collection and consequently increase the country's development programs (Von Haldenwang & Ivanyna 2012).

6. Conclusion Remark

In implementing GST and to gain the benefits from the system established, the Malaysian government shall look after all the effect of the tax system changes. They shall consider from the bottom up of all the parties involved in the implementation of GST since it will involve not only the rich person, but, also the low and middle income earners, who have already been suffering with a high living cost especially in the urban area. They shall consider the tax rate, the compensatory package, the accounting process, economic and political conditions and many more. This is important to achieve a high satisfaction from all the GST stakeholders and to maintain the sustainability of the public.

In terms of GST governance, RMCD shall focus more on the regulation enforcement since the acts and policy have been well established from 2014. They shall hire more staff for governance process to be more effective and efficient if existing officers are not capable to cover all of outstanding issues.

No matter what, good collection, smart management and fair distribution of government revenue are very important in order to be a developed country with less dependence on overseas loan. It will create a decent environment in the country to live in. Therefore, good governance in GST administration is a part of the government process to achieve the above objective. Good governance of tax administration will enhance the confidence level of taxpayer and it leads to improvement of tax compliance and finally increases the revenue of the government for the society's development.

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