COVER STORY

GST 1 year on

STORIES BY **YEN NE FOO** AND **ESTHER LEE**

Come April 1, the implementation of the Goods and Services Tax (GST) in Malaysia will reach its one-year mark. The anniversary represents a milestone of sorts, but not everyone will be in a celebratory mood. Some — as many have on the May Days of 2014 and 2015 — will take to the streets of Kuala Lumpur on April 2 with their homemade banners that will read "Batal GST" for a rally organised by the country's opposition leaders to express their disapproval of the consumption tax.

GST is deeply unpopular among consumers and businesses because of the widely held belief that the consumption tax is responsible for pushing the prices of goods and services upwards.

Malaysia's headline inflation, as measured by the Consumer Price Index (CPI), growth registered a decline to 2.1% in 2015, from 3.2% a year ago. Much of this was down to lower transport costs. The transport category within the CPI saw negative inflation of 4.5% in 2015, versus 2014's inflation of 4.9%, as consumers paid less for petrol and diesel after the crash in global crude oil prices.

Although inflation rose slower in 2015, consumers cry that they have hardly felt the difference. It is not hard to see why.

CPI growth was volatile in 2015. It declined sharply at the beginning of the year to a low of 0.1% in February, but climbing up post-GST to peak in July at 3.3% to give consumers a jolt in prices.

There was also a pervasiveness of price hikes across the CPI basket of goods. Bank Negara Malaysia noted in its 2015 annual report that prior to the implementation of GST, the share of items within the CPI basket with inflation of more than 4% stood at 11%. That share grew to 32% in the second quarter of the year. In the second half of 2015, 41% of the CPI goods basket saw inflation exceeding 4% as firms that had initially absorbed GST started to pass the tax on to customers.

Experts say that consumers are not likely to feel the tapering off in prices towards the end of 2015 as prices tend to be "sticky". Once up, they hardly come down. And this was proven with the release last week of the February 2016 CPI, which surged 4.2% year on year.

Meanwhile, data from the Malaysian Institute of Economic Research indicates that consumers are fearful of higher prices and increasingly reluctant to spend. Its Consumer Sentiment Index dipped to a record low of 63.8 points, falling even below what was seen after the global financial crisis in 2009.

Such weak consumer sentiment was eventually reflected in some of the country's economic indicators. In 2015, Malaysia's domestic demand growth slowed to 5.1% from 5.9% in 2014, with private consumption growth moderating to 6%, from 7% a year ago.

Numbers like these help to support the opposition-led calls for abolishing GST and the cost burdens associated with it.

But, it is important not to get carried away. GST was not the only cause of inflation last year.

According to Bank Negara, GST contributed only 0.7 of a percentage point to headline inflation in 2015, lower than originally expected. Government measures, such as the enforcement of the Anti-Profiteering Act 2011 and zero-rating or exempting essential consumer and public goods from GST have helped ensure that price increases are not excessive. In any event, other factors — the government's subsidy rationalisation plan, the depreciation in the ringgit and the invisible hand of the free market — were not blameless for rising prices.

Moreover, judging GST solely by its impact on prices paints an incomplete picture of its role in today's economic environment. Many economists and tax consultants consider GST as the "most efficient" way of widening Malaysia's tax base.

R S Raja Kumaran, executive director of PricewaterhouseCoopers Taxation Services Sdn Bhd says, "In my mind, GST is a good tax. It has brought those who do not pay taxes into the net and has helped the Inland Revenue Board bring people into the net. Now, people will have no choice (but to pay taxes)."

In that sense, GST raises government revenue at a scale and speed that existing direct tax mechanisms would not be able to achieve.

Statistics show only 1.7 million out of the 12.4 million strong workforce pays individual income tax and in 2015 they would have contributed RM28.7 billion or 12.7% of government revenue.

In contrast, the nine-month collection of GST in 2015 is expected to rake in RM27 billion with just over 400,000 companies registered for GST.

The target for 2016 is RM39 billion and few doubt that this will not be achieved. The sum represents 3.1% of Malaysia's gross domestic product (GDP).

"First, a small portion of the population pays income tax. Secondly, corporate taxes can be susceptible to external factors. For example, with the collapse in oil prices, oil and gas firms will report lower earnings, if not losses.

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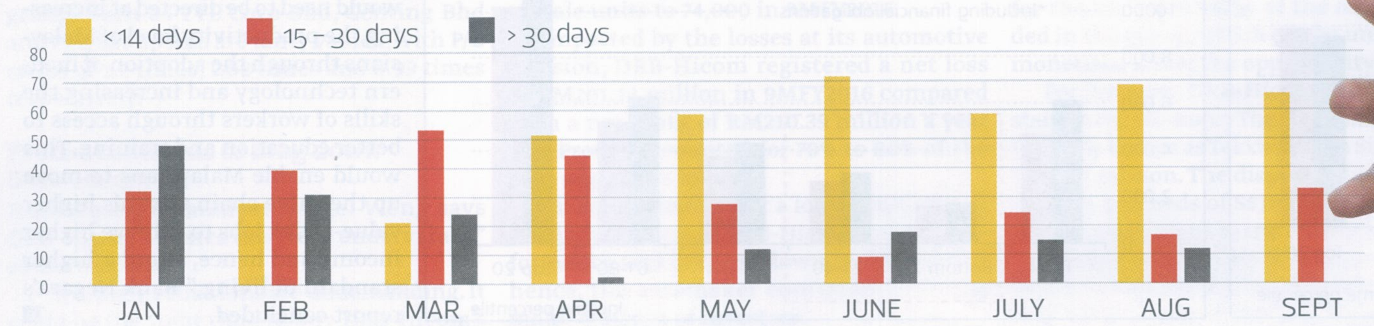
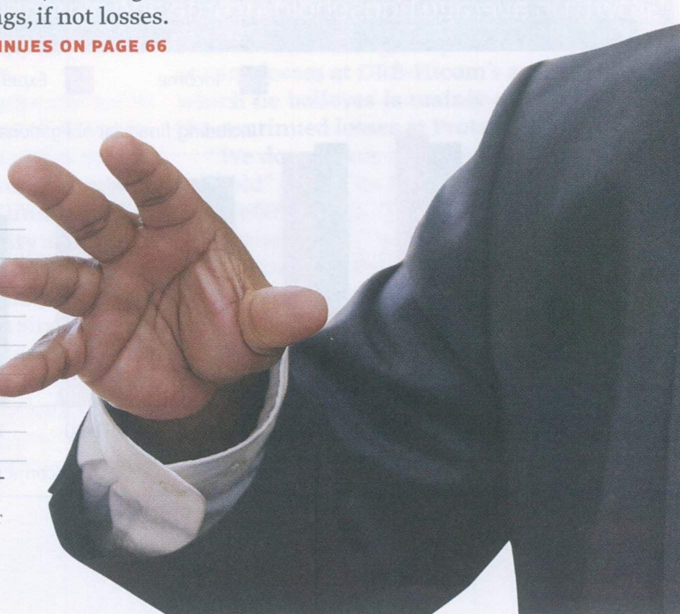
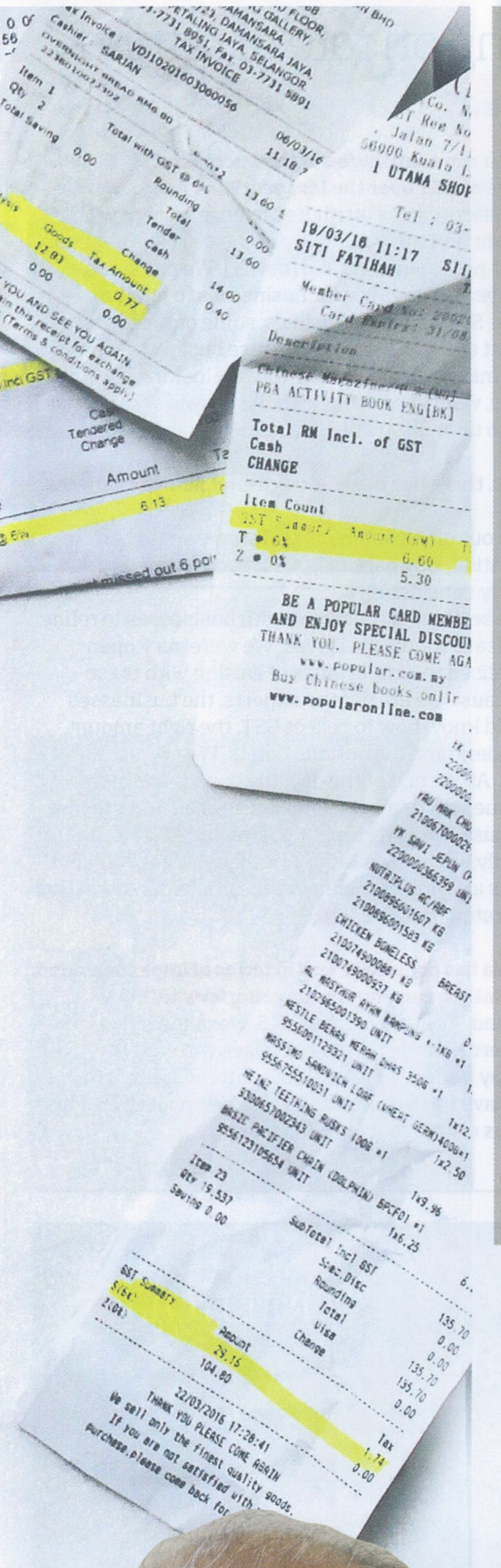
Previously, the government had very little information on margins. Sometimes, we ended up barking up the wrong tree. The GST data will provide more insights into margins. We also capture it by code, which allows us to dissect by product.
— Subromaniam

Input tax rate of refund in 2015 (%)



ROYAL MALAYSIAN CUSTOMS DEPARTMENT





Complaints about compliance

Many would agree that the implementation of the Goods and Services Tax (GST) in Malaysia has gone fairly well in its inaugural year. Statistics show that the number of businesses (400,000) registered for GST have far exceeded expectations while the amount of GST collected for 2015 went beyond the targeted RM27 billion.

Nevertheless, like any new tax system, teething problems certainly abound. While GST is known as a business friendly tax because it allows businesses to recover its input tax, many have found its implementation to be a pain.

Tax consultants share that there have been many instances when the director-general's decisions on certain issues were not consistent with the Goods and Services Tax Act, causing confusion and uncertainty.

"The DG's decisions are public. Then, there is the GST Act, which is what binds you. If there is a dispute between what the DG says and what the law says, unless you are 100% comfortable with what the DG is saying, you will choose the law. If you cannot comply with the law, then you've got a problem. Should Customs choose to penalise you for not following the law, you might end up having to defend yourself in court," says PricewaterhouseCoopers Tax Services Sdn Bhd managing consultant Tim Simpson.

Taxand Malaysia Sdn Bhd managing director Renuka Bhupalan does not deny that the Customs officers have been helpful in taking enquiries via phone calls or at meetings. But she notes that sometimes, their hands had been tied due to uncertainty in interpreting the law or in how the law should be implemented from a practical perspective.

The uncertainty in interpretation among the Customs officers themselves seem to have added to the confusion. The call centre and Customs head office have given varying replies to queries.

However, Royal Malaysian Customs Department deputy director-general Datuk Subromaniam Tholasy, who is in charge of GST, defends his staff, saying that they are generally well trained.

"I've got a good team of senior Customs officers who have been with me since the beginning of the GST process. Generally, all of my staff can reply to most questions but with more complicated issues, they would bring it up to the head office. I guess the issue that I am facing now is that a few senior custom officers are retiring soon," he says.

Elsewhere, tax consultants lament that the GST process requires businesses to acquire too many approvals, which slows down business processes and increases the cost of doing business.

PWC executive director Raja Kumaran opines that the Customs department could probably rethink the approval process going forward. "We are going towards a developed economy. So, businesses should be given the leeway to do self-policing and given clear guidelines or instructions for it," he says.

After all, he adds, there is the audit process that provides an avenue for Customs to take action against businesses that are non-compliant. "In any tax system, there will be deviants. But don't let them dictate how the others run their businesses," he suggests.

Meanwhile, some businesses continue to gripe about the one key issue that has dominated headlines since GST's implementation — input tax refunds.

Accounting firm Grant Thornton executive director Alan Chung says some of his clients continue to struggle with cash flow due to delays in obtaining input tax refunds. He says that GST was not intended to be a cost to businesses because of the availability of input tax refunds, but it became a cost for those who were buying a lot of imported materials as they had to pay import GST before the goods were physically obtained.

The Customs department, however, insists that the rate of providing refunds has improved since April last year. Statistics show that the refund rate within the promised 14-day timeframe had increased from 17% initially to 70% in November.

While that may be the case, tax consultants say the statistics should also show the value of the refund in each case, not just the number of cases refunded.

"For example, 90% of people have returns of RM100 and 10% have returns of RM5,000. You can still say it's 90% refunded but you're not talking about the money, the huge amounts of money that's not being returned," says a tax consultant who declines to be named.

However, he concedes that the relationship between the Customs department and businesses should be a two-way street. He adds that sometimes, businesses themselves should take the blame for late refunds because they had not furnished the additional information required by the Customs department. E

With GST, government now knows industry profit margins

Despite the government declaring the Goods and Services Tax a success and how it has helped shore up its coffers in the light of the slump in oil revenue, critics continue to condemn the unpopular consumption tax. Businesses are also grumbling about its execution.

However, the deputy director-general of Customs in charge of GST implementation Datuk Subromaniam Tholasy says despite some teething problems, everything has gone fairly well. The following is an interview with him a year after GST came into force.

***The Edge:* GST is often blamed for the price increases that we have seen over the last year. Do you think that is the case?**

Datuk Subromaniam Tholasy: If you really dissect it, prices went up just before GST was implemented. People tried to advance their purchases, so it became a supply and demand issue. Unfortunately, we were moving from the old tax system, the Sales and Services Tax (SST), which is insensitive to price elasticity demand. This means that once prices go up, they stay there.

The other factor is the 18-month moratorium on profit margins under the Anti-Profiteering Act 2011, which took effect on Jan 1, 2014. When businesses knew that their profit margins were going to be fixed for the next 18 months, what did they do? Increased prices before the moratorium took effect, didn't they?

There were also factors beyond the government's control, like the ringgit's depreciation. You can't blame GST for that. When the ringgit weakens, imports become expensive, which pushes up prices.

So, how much of the price increase can be attributable to GST?

It's very minimal. Our studies show that prices went up a bit after GST, but it is a one-off increase. It is not something that only happens to us. All the other countries implementing GST have seen similar increases.

Sometimes, people fail to understand the benefit that GST brings in the long term. It provides more transparency. And the cost savings [enjoyed] by businesses will flow through. More importantly, we now know the profit margins being made by every industry and every business and very soon, you will see some initiatives. Consumers should welcome this. Previously, nobody knew who was making how much and at which level.

Does this mean that the government is considering taking steps to regulate businesses?

It gives us an opportunity to look at it. Moving forward, we would know how to tackle issues, whether at the production level, the middle-man level or the retail level.

But that wouldn't be a free market anymore, will it?

It will still be. Previously, the government had very little information on margins. Sometimes, we ended up barking up the wrong tree. The GST data will provide more insights into margins. We also capture it by code, which allows us to dissect by product.

I'm not saying that we're going to regulate businesses or anything like that. What I'm saying is that the government will have a better understanding of business margins. So, when there is a need to intervene, we can do so.

Are we on track to reach the RM39 billion in GST collection as projected in Budget 2016?

I don't want to answer questions on revenue. I will leave that to the prime minister to announce when the time comes.

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GST had come 'at the right time'

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Losses can be carried into the future and a loss-making company could be paying lower taxes for years," says a private sector economist.

"With GST, almost everyone and everything is taxed. As more businesses are registered for GST, collections will improve," he adds.

More than the amount it can raise, GST is the government's most reliable and stable source of income. This is particularly important for Malaysia at this juncture. Credit rating agencies already critical of the Malaysian government's financial position saw the implementation of GST as the government's commitment to fiscal reform.

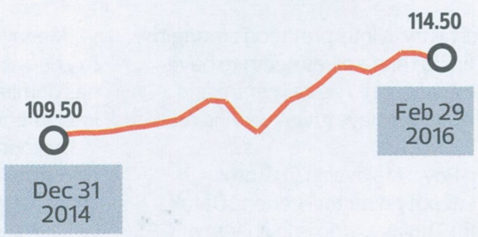
For the moment, at least, this keeps a possible sovereign credit rating downgrade at bay.

Further, the Ministry of Finance Economic Report 2015/2016 states that the government's revenue collection is anticipated to fall by 5.4% due to the sharp decline in oil-related revenue. Bank Negara reported that oil-related revenue's share of total government revenue had declined to 21.5% in 2015 compared with 30% in 2014. This is expected to drop to between 13% and 14% in 2016.

Though unintended, economists say that the implementation of GST had come "at the right time", shoring up Malaysia's otherwise stretched public finances.

While that is generally true, reluctant taxpayers footing the bill for government spending will find it hard to see what they have gained out of paying billions worth of GST.

Consumer Price Index



Part of the trade-off is the reduction of income tax post-GST. Corporate income tax will be reduced by one percentage point in 2016 and personal income tax was slashed by one to three points in 2015.

But under Budget 2016, the government took a step backwards by increasing personal income tax for the highest income earners in the country by one to three percentage points. And further increases cannot be ruled out.

The sense of being short-changed is compounded by the fact that the government has made little effort to keep to its promise of spending more efficiently, while its debt level hovers near the self-imposed ceiling of 55% to GDP.

In 2015, the government originally allocated a total of RM273.9 billion, an increase of RM9.8 billion compared with 2014's initial allocation, despite the plunge in global crude oil prices. Out of this, over 80% went towards the government's own operating expenditure (opex).

While it promised to reduce opex at the start of 2015, the government had last week requested an additional RM5.99 billion to fund 2015's spending through a supplementary budget in Parliament.

This year, the government is more ambitious. It wants to save RM9 billion from the original sum of RM267.2 billion after recalibrating Budget 2016 to reflect the low oil price environment.

Interestingly, the savings would barely scratch the surface of government opex. Instead, more than two-thirds of the cuts will impact consumers in some way. RM5 billion worth of savings will come from "reprioritisation of development expenditure", RM200 million from delayed asset purchase and another RM1 billion from lower subsidies on liquefied gas and diesel.

What is clear one year on from the implementation of GST is that the unpopular tax is here to stay. But, calls for its abolishment will be loud as households struggle with shrinking spending power while the government is seen as being unable to cut its own spending.

Before GST and the withdrawal of subsidies on tolls and other basic items, the government was seen as helping out the people. Today, the reverse is true — the public now has to pay more for everything to help out an administration whose finances are not in good shape. E

Working on rate of refund

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What would you say contributed to the successful implementation of GST over the last year?

Some of the success can be attributed to engagement with the private sector and the availability of the director-general's decision so that people understand [better]. We put in these guidelines one year in advance for businesses to prepare.

If you look at Singapore's guidelines, some of them are reviewed almost every other year because business is not static. It's dynamic and it needs new ways of looking at things and here we are, working closely with the private sector. That has helped us to understand the businesses, and vice versa.

So in your view, there has been enough engagement with the private sector?

Yes, we started our engagement on GST many years before the implementation, way back in 2005 when the government started seriously considering it.

There was a series of discussions with businesses to refine the model and [talk about] the issues. We were very open about it. We realised the importance of liaising with these businesses because we are not the experts, the businesses are. They should know how to collect GST, the right amount, they should understand the dos and don'ts. We are just the administration. At the end of the day, the onus is on them.

The only issue was that a lot of businesses did not prepare back then because the government postponed GST a couple of times. It was only when it was announced in Budget 2014 and when there was a definite timeline for the implementation that the businesses started to prepare.

Overall, Malaysia has done quite well in terms of implementation. What do you think we can improve on going forward?

The rate of refund. As at November 2015, we managed to refund 70% in terms of the number of cases within the legislated 14-day period. We can always improve this to 85% to 90%. But to have 100% is impossible as there will always be some suspicious claims that we need to verify. E