Budget 2016 and income distribution disparity

by Tham Lih Jiun

WHILE it was anticipated that with the implementation of the Goods and Services Tax, a further reduction in personal income tax rates or a widening of the income tax band would be announced, but such measures were left out in Budget 2016. Instead, Budget 2016 sees an enhancement of existing personal reliefs and the introduction of two new reliefs.

Personal relief enhancements are on tuition fees for higher education from RM5,000 to RM7,000, spouse relief from RM3,000 to RM4,000, child relief from RM1,000 to RM2,000, child and disabled child above 18 years old and pursuing higher learning from RM6,000 to RM8,000. All of these reliefs will be effective from year of assessment 2016. A new parental welfare relief of RM1,500 per parent is introduced for the years of assessment 2016 to 2020 for those who are not claiming medical treatment and care of parents who are ill. A relief of up to RM250 will be given to those who contribute towards Socso, available from year of assessment 2016. These reliefs could provide some tax savings for those eligible to claim them.

In Budget 2015, we saw the widening of the tax band together with a reduction of 1% to 3% across the scale rates in personal income tax rates which was a much welcomed move. Amid a trend of reducing tax rates, Budget 2016 has proposed instead the addition of the RM600,001–RM1,000,000 and above RM1,000,000 income brackets taxed at 26% and 28% respectively, which will be effective from the year of assessment 2016. This would be a 1% and 3% increase from the rates announced in Budget 2015.

Meanwhile, for the lower income group, the prime minister announced the continuation of the 1Malaysia People's Aid (BR1M) which is expected to benefit 4.7 million households and 2.7million single individuals with an allocation of RM5.9 billion. BR1M is increased by RM50 for each of the category of persons eligible for the aid.

While the measures announced above seem to be taxing the rich to help the poor, it is not likely that the higher tax collection from high-income taxpayers would be enough to sufficiently shift resources to the lower income group considering that the group of taxpayers in the above RM600,000 chargeable income category is relatively small compared with the rest of the taxpayers. It will take a substantial commitment of resources to reduce the overall disparity in income distribution to have an impact.

On the flip side, increasing the income tax rate for the upper bracket and for non-resident individuals from 25% to 28% could have adverse effects on attracting talent to build a knowledge-based economy. The increase in the income tax rates coupled with the ringgit's depreciation and dwindling skilled jobs availability may lead to a talent exodus and increase competition with our neighbouring countries for talent.

Moving to Singapore where the current highest personal income tax rate is 20% for income above S$320,000 (approximately RM975,000) may give rise to an immediate increment of 20% arising from currency exchange alone.

Should this happen, the pool of individual taxpayers contributing tax revenue would contract further. As it stands, in Malaysia, less than 6% of the population pay income taxes in 2013. The widening of the lower income tax bracket presented in the 2015 Budget could reduce 300,000 people in the low income group from paying income tax further, shrinking the pool of taxpayers.

It would seem that raising the top income tax rate for the higher income tax bracket may not effectively reduce the overall disparity in income distribution unless the income can be sufficiently shifted to the lower income groups. It would take a significant shift in resources to address the income disparity and ensure that the B40 group is not left out in Malaysia's vision to be a high-income nation.

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