Finding money for Budget 2017

BY **CHUA SUE-ANN**

As Malaysia awaits the unveiling of Budget 2017 on Oct 21, there seems to be a consensus that the federal government is walking a tightrope.

It has to contend with lower dividend contributions from national oil company Petroliam Nasional Bhd and reduced petroleum taxes due to low crude oil prices.

It also has to find the funds to continue development projects, sustain a large public-sector workforce, stimulate private-sector business activity and alleviate the citizenry's rising cost of living woes.

What is more, Budget 2017 is largely expected to be "people-friendly" ahead of what could be a general election next year or early 2018.

Recall that in January, the government took a rare step of revising Budget 2016, which was announced in October 2015.

This was after crude oil plunged to just US$30 a barrel levels. The government announced several measures in the revised budget that would enable it to save some RM9 billion.

Furthermore, the government has committed to reducing the fiscal deficit. It has already narrowed the gap from a deficit of 6.7% of GDP in 2009 to a targetted 3.1% this year.

But in the meantime, can the government strike a balance? It is in a tough spot, say policy observers.

"There is room to manoeuvre but not much, maybe a couple of billion ringgit from here and there. The government will still need to spend in line with its expected revenue and commitments," says Sunway University Business School professor of economics Dr Yeah Kim Leng.

Overall, total federal government revenue for this year is expected to inch up 1.4% to RM225.656 billion from RM222.455 billion a year ago, according to the government's revenue estimates for 2016.

These also show that the contribution from tax revenue has been increasing while non-tax revenue has been falling over the last three years.

The government has been seeing lower income tax from petroleum, which is projected to fall 2.1% to RM9.331 billion from RM9.529 billion in 2015 due to lower average crude oil prices.

This, however, has been offset by the higher collection of company and individual income tax, which are the two single largest contributors to the public coffers.

Of the four main revenue categories, tax revenue is always the largest source of income. For this year, tax revenue is expected to account for RM183.553 billion or 81.3% of total revenue (see charts).

Company income tax revenue is projected to rise 8.9% to RM74.381 billion this year while individual income tax is estimated to grow 7.5% to RM30.266 billion (see Table 1).

As for indirect tax collection, this is expected to increase by 8.9% to RM57.987 billion from RM53.258 billion a year ago.

Finding more money to spend

There are several ways the government could increase its revenue collection in the immediate term.

The Inland Revenue Board, for one, is said to have intensified its tax audits and investigations into individuals and companies to optimise revenue collection.

This is crucial, given that income tax, particularly from individuals and companies, accounts for almost half of the federal government's revenue. This year, some RM104.647 billion of income tax or about 47% of total revenue collection is expected to come from individuals and companies.

Deloitte Malaysia managing director Yee Wing Peng lauds the IRB's move to intensify tax audits and investigations.

"But in my view, there is a lot more they can do. There are still many targets, especially outside the Klang Valley. It's not about victimising people but rather about trying to create a level playing field for those who are paying taxes," says the career tax auditor.

Yee also feels that the government should consider lowering the corporate tax rate to encourage greater compliance.

This may sound counterintuitive but there are many case studies globally that show that lower tax rates do not always translate into lower revenue collection for governments. If anything, they reduce the chances of tax evasion.

As Yee points out, Malaysia's corporate tax rate is not as competitive as those of its closest economic peers in Asean. Malaysia's standard corporate tax rate was 25% for YA2016 compared with Singapore's 17% and Thailand and Indonesia's 20%.

Apart from taxation, Malaysia could introduce new business-friendly policies in order "to enlarge the economic pie", which will invariably bring in more revenue for the government, Yee observes.

He points out that over the medium term, the government could slightly increase revenue collection by rolling back its list of GST-exempted and zero-rated items.

When Malaysia implemented GST last April, analysts concurred that its structure was among the most complex in the region due to its lengthy list of exemptions.

The exemptions were believed to be the government's way of preempting public backlash against the introduction of the consumption tax.

"It is only a matter of time, in my view, before the government cuts back. The system has to be simplified and the government has to find more revenue. But we have to wait for the whole GST system to stabilise and to get everyone to accept it and for the dust to settle," says Yee.

Another way for the government to increase revenue is to monetise its assets more efficiently, for example, land sales. Yee suggests that land sales be done via auction where the highest bidder wins — akin to what is being practised in Singapore and Hong Kong — instead of direct negotiations or land swaps.

In fact, Hong Kong's government is expecting 13.4% of its revenue to come from land sales and conversion premiums in 2016 and 2017.

"Here, I think we need to have the determination and discipline to really do it," says Yee.

Sunway University Business School's Yeah notes that in previous deficit years, Malaysia's federal government was able to top up some of the shortfall via asset sales or privatisation.

One thing to watch for, according to Yeah, is the government's plan to optimise revenue from telecommunications spectrum via a redistribution process that was announced in January, when Budget 2016 was revised. The auction would bring in billions of ringgit in revenue but only from next year.

The 2.6GHz spectrum's five-year assignment period comes up for review in December 2017 while the 3G to 2.1GHz 15-year licences will be up for renewal in 2018 to 2020, according to CIMB Research.

Additionally, the upstream government-linked companies could be tapped for dividends when needed, says Yeah.

"From a broad perspective, the government will continue to stretch the limits of fiscal sustainability in order to sustain investor confidence while maintaining its commitment to fiscal prudence.

"If the RM39 billion GST target is achieved, the government will have some leeway in spending and if there is improved oil revenue, that is a bit more room," he adds.

The government has hailed GST as a lifeline for the country's public-sector finances.

In his Budget 2016 speech last October, Prime Minister Datuk Seri Najib Razak told Parliament that government revenue would have been RM21 billion lower had it not been for GST.

The previous sales and service taxes would have brought in only RM18 billion compared with the RM39 billion that GST collected.

Consequently, the fiscal deficit would have increased to 4.8% and not the 3.1% targeted for 2016.

The government would also gain more fiscal flexibility if it were able to re-prioritise development spending by postponing some of the planned projects to lower the development expenditure of the public sector, Yeah concludes. E

Direct tax revenue growth

SOURCE	SUB-SECTION	2015 REVISED ESTIMATES (RM BIL)	% OF TOTAL	2016 ESTIMATES (RM BIL)	% OF TOTAL	Y-O-Y GROWTH %
Income tax	Individual	28.155	24.11	30.266	24.1	7.5
	Company	68.32	58.51	74.381	59.24	8.9
	Petroleum	9.529	8.16	9.331	7.43	-2.1
	Withholding	2.264	1.94	2.473	1.97	9.2
	Cooperatives	0.071	0.06	0.084	0.07	18.3
	Others	0.023	0.02	0.023	0.02	0
	Sub-total	**108.362**	**92.8**	**116.558**	**92.83**	**7.6**
Other direct tax	Stamp duty	6.188	5.3	6.766	5.38	9.3
	RPGT	2.128	1.82	2.163	1.72	1.6
	Others	0.082	0.07	0.079	0.06	-3.7
	Sub-total	**8.398**	**7.2**	**9.008**	**7.17**	**7.3**
	TOTAL	**116.76**	**100**	**125.566**	**100**	**7.5**

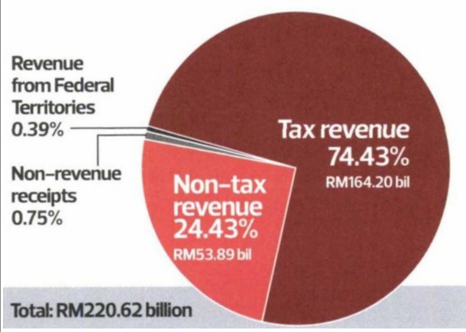
TABLE 2

Indirect tax revenue growth

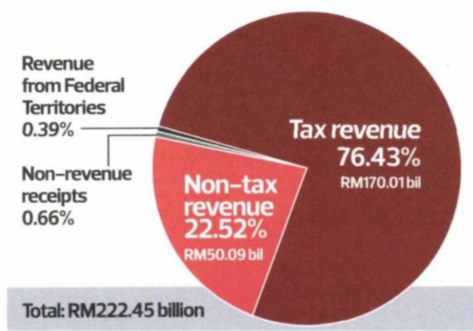
SOURCE	2015 REVISED ESTIMATES (RM BIL)	% OF TOTAL	2016 ESTIMATES (RM BIL)	% OF TOTAL	Y-O-Y GROWTH %
Export duty	1.053	1.98	1.012	1.75	-3.9
Import duty	2.727	5.12	2.791	4.8	2.3
Excise duties	12.168	22.85	12.408	21.4	2
Sales tax*	4.784	8.98	NA	NA	NA
Service tax*	2.851	5.35	NA	NA	NA
GST	27	50.7	39	67.26	44.4
Levy	0.15	0.28	0.15	0.26	0
Others	2.525	4.74	2.626	4.53	4
TOTAL	**53.258**	**100**	**57.987**	**100**	**8.9**

** GST replaced sales and service taxes in April 2015*

Major revenue components for 2014 (actual)



Major revenue components for 2015 (revised)



Major revenue components for 2016 (estimated)