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Tax Incentive for Islamic Housing Loans in Malaysia

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Abstract

In the assessment years 2009-2010, Malaysia's Income Tax Act 1967 allowed deductions for interest paid on individuals' housing loans up to RM10,000 for 3 years of assessment. Data from Inland Revenue Board Malaysia revealed that RM1.609 billion of exemptions was allowed from 2012 to 2014. Majority with annual income of less than RM100,000 have benefited from this exemption but the tax relief was later repealed. This study showed that any reconsideration of similar tax incentives would be beneficial to several stakeholders. Using the psychological theory the study explains why taxpayers are keen to respond favorably towards any incentives on housing loan.

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1. Introduction

Tax incentives are exemptions given to an individual or company for the tax charges that was supposed to be imposed (MIA, 2012). Meanwhile, United Nations Conference on Trade and Development (2000) defines tax incentives as exemptions allowed to the enterprise, to stimulate investment in certain projects, sectors or geographic areas, other than reducing their tax burden. These tax incentives intend to reduce tax rates on profits, decrease tariff of imported goods, raw materials and components and also to protect the domestic market by increasing the tariffs for imported investment projects.

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Tax incentive is clearly an important aspect in developing and promoting the Islamic financial market. A wide range of tax incentives across the Islamic finance market in promoting Malaysia as an international Islamic financial center has been implemented by Malaysia government. This includes the exemption from Real Property Gain Tax (RPGT) for the disposal in relation to the *Sukuk* issued by the Malaysia Global Sukuk and Bank Negara Malaysia and the issuance of private debt securities if the disposal of the chargeable assets is under Islamic principles. The exemption is also given for the stamp duty imposed to the customer by financier on all documents under *Shariah* law related to the movable property under *Al-Ijarah* Head Lease Agreement. The term financier refers to banks, leasing companies or financial institutions. The issuance of credit cards from financial institution to customer under *Bai'nah* Sale or *Bai'nah* Purchase agreement is also exempted from stamp duty for all documents issued. All documents related to the renewing of any Islamic revolving financial facility under an Asset Sale Agreement or an Asset Lease Agreement under *Shariah* and also those that are related to purchases of property under sales and purchase agreement or the *Shariah* principle for the purpose of lease back are exempted from stamp duty.

In year 2009 and 2010, Malaysia government implemented tax deduction on housing loan made by individuals, provided the sales and purchase agreement of the residential property was completed or signed on or after 10 March 2009 to 31 December 2010. Other eligibility criteria include that the individual must be a Malaysian citizen and a resident in Malaysia. To qualify for the tax incentive, the residential property purchased such as house, condominium, and apartment or flat must be a residential property per individual. Those properties under construction were also qualified for the deduction and all individuals who had fulfilled the stipulated the conditions were entitled to an annual tax deduction of RM10,000 for three consecutive years of assessment as provided under S46B of the Income Tax Act 1967. For jointly purchase property by more than one person, all of them are entitled for the relief but restricted to the maximum of RM10, 000. However, the tax deduction of housing loan in Malaysia is only applicable to those who bought a house during the stated period and any transaction after 31 December 2010, the tax payer is not eligible for this special relief. Consequently, after 2010 and until present the legal provision of tax deduction on housing loan was repealed.

Besides Malaysia, India and Thailand are also among the countries that provide such incentives to their citizens. The Indian government has revised the budget for 2014-2015 on the tax deduction for interest on housing loan from Rs 1.5 lakh to Rs 2 lakh. The tax incentive was given for self-occupied property. Meanwhile, Thailand government provided tax relief for mortgage interest on home loan know as tax relief at source (TRS). The tax relief is given to mortgage holders for the interest paid on qualifying home loans taken after 1 January 2004 and or before 31 December 2012. The mortgage holders are qualified for tax relief up to year end 2017 based on general rates and thresholds. However, the eligibility depends on the condition whether the buyer is a first time buyer, non-first time buyer and others. This interest paid allowed can either be for a new mortgage for a home and also for the purposes of improving the home (Revenue, 2013). The current study is an attempt to answer mainly the following research questions:

- RQ 1: Do demographic profiles of the individual taxpayers have any association with the type of housing loan financing in Malaysia?
- RQ 2: Is there any difference in the perceptions on the benefits of granting tax incentives for Islamic housing loans in Malaysia?

The next section of this paper will review the relevant literature, followed by the explanation on the methodology. The results and conclusion will be discussed in the fourth and fifth sections.

2. Literature Review

2.1. Malaysia property market

Based on the property market report from Valuation and Property Services Department, Ministry of Finance Malaysia (MOFM), overall transactions volume and value for market activity in the first half of 2015 have decreased by 3.5% (186,661 transactions) and 6.6% (RM76.61 billion) against the corresponding period. The challenging economic and financial environment faced by the country in the past months were the main factors of the declining

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