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## Complexity of the Malaysian income tax act 1967: Readability assessment

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### Abstract

This study which examines the readability of the Income Tax Act 1967 (ITA 1967) and its associated Schedules is considered important as the materials are the main references for taxpayers who have intention to comply with their tax obligations. Using FRES and F-KGL analysis, it is found that the ITA 1967 and its Schedules are complex to understand. The findings indicate that the materials under study may need to be rewritten. It is hoped that the findings will contribute not only to the body of knowledge but also to the tax authority.

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*Keywords:* Income Tax Act 1967; readability, complexity; flesch reading ease index; flesch kincaid grade level

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### 1. Introduction

The Income Tax Act 1967 (ITA 1967) is the main source of reference governing the income tax system in Malaysia. The ITA 1967 was first enacted in 1967 and frequently amended to accommodate the rapid development in Malaysian taxation. Currently the ITA 1967 contains 13 Parts with 13 Schedules and 156 Sections. While the amendment effort is commendable yet this enormous number of sections in the ITA 1967 poses a question of simplicity of the tax legislation. Thus, this research is undertaken to examine the complexity of the taxation system in terms of the level of readability of its tax legislations. This is important as when the tax legislations are overly

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and unnecessarily complex, the taxpayers may have difficulty to understand the materials and as a result, they may not benefit from whatever tax incentives offered by the government. In this case, even the most attractive incentives will not be well-functioning as intended. The impact may get even worse when such a low level of readability of the tax rules leads to unintentional noncompliance of taxpayers, which in turn pull them to the penalty regimes as stipulated under Self-Assessment System (SAS). This effort hopefully serves as a stepping stone for more research on tax complexity in the future. This study is particularly relevant in respond to the survey findings by Mustafa (1996), Saad (2011) and Isa (2014) that taxpayers faced the problem of content complexity of the income taxation materials. From the practical point of view, the insights generated from this research may assist the Inland Revenue Board Malaysia (the IRBM) to review and improvise (if necessary) the relevant tax materials in their effort to optimize their services to their customers (i.e. taxpayers), and consequently meet the national ultimate objective of high compliance.

This paper is divided into five sections. The next section sets out a review of literature relevant to the study. This is followed by a section on research method. Section 4 discusses the results of the study before the paper concludes in section 5.

## 2. Literature review

The income tax system in Malaysia commenced in 1948 under the British colonization era. It was introduced to legitimize the collection of taxes from individuals and corporations. The first income tax legislation at that time was Income Tax Ordinance 1947. This Ordinance was substantially based on the Model Colonial Territories Income Tax Ordinance 1922 (United Kingdom) (Kasipillai, 2005). The Ordinance was subsequently repealed and replaced by the ITA 1967, which came into effect on 1 January 1968. The ITA 1967 is actually a consolidation of the three laws of income taxation namely the Income Tax Ordinance 1947, the Sabah Income Tax Ordinance 1956 and the Sarawak Inland Revenue Ordinance 1960. This consolidation is one of the significant effect of the formation of Malaysia in 1963. As supplementary materials to the ITA 1967, the IRBM has, from time to time, issued the relevant Public Rulings and the tax guidelines.

Since its inception, Malaysia had adopted an official assessment system (OAS) which requires taxpayers to furnish relevant information pertaining to their incomes and expenses to the IRBM. Under that system, the duty to compute the tax payable was with the IRBM, as taxpayers were assumed to have limited knowledge on taxation. However, with effect from 2001, a self-assessment system (SAS) was gradually implemented. Under the new system, the responsibilities to compute tax payable shifted from the IRBM to taxpayers. Unlike OAS, SAS requires taxpayers to be well-versed with the existing tax laws and provisions, since they are answerable to the tax authorities in the case of a tax audit. Another prominent attribute of SAS is voluntary compliance, as the tax returns submitted by taxpayers are deemed to be their notice of assessment. In other words, penalty mechanisms will be applied if taxpayers do not submit a correct tax return within the stipulated period. Thus, the issue of tax complexity is of relevant concern under SAS.

Researchers generally agree that tax complexity arises due to the increased sophistication in the tax law (Richardson & Sawyer, 2001; Strader & Fogliasso, 1989). There are various forms of tax complexity: (i) computational complexity; (ii) forms complexity (American Institute of Certified Public Accountants, 1992); (iii) compliance and rule complexity (Carnes & Cuccia, 1996); (iv) procedural complexity (Cox & Eger, 2006); and (v) the low level of readability (Pau, Sawyer & Maples, 2007; Richardson & Sawyer, 1998; Saw & Sawyer, 2010; Tan & Tower, 1992).

In relation to the readability of tax legislations, the New Zealand government has actively undertaken various tax reforms since the mid-1980s (for details, see Hasseldine & Bebbington, 1991). However, Tan and Tower (1992) claimed that the efforts made by the tax authority at that time to simplify the tax law failed. In the study, the Flesch Reading Ease Index (FRES) was used to measure the readability level. The analysis was carried out on the New Zealand tax legislation, Tax Information Bulletins (TIBs) and Tax Return Guides. The FRES Index measures the difficulty ranging from zero (most difficult) to 100 (least difficult). Their findings indicate that there was no progress with simplification at that time, except for the Tax Return Guides. A later study by Pau et al. (2007), however, provides contrary evidence on tax simplification in New Zealand whereby significant improvements

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