A Comparative Study on the Environmental Taxation Policy in Malaysia as compared to British and Australian models

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ABSTRACT

Environment degradation has been a subject of debate between administrators both in developed and developing nations since the 1980s whereby the degradation of the ozone layer has been a contentious and continuing topic of discussion. The Langkawi Declaration in 1996 was one of the first major international declarations Malaysia signed. Since then Malaysia has become a signatory for various including the Kyoto Protocol.

In this paper we will review current Malaysian tax laws especially the Income Tax Act 1967 to see how the Malaysia Government has used taxation to remedy the problems of the environment. We shall look at the environmental policies of two British Commonwealth nations, United Kingdom and Australia whereby the countries have a historical connection to the Malaysian Legal System. We will see how they use taxation to tackle and remedy the issue of the environmental degradation. With this study we will identify the issues that Malaysian Tax Law needs to address so that Malaysian Tax Law will be comparable to international tax practices on Environmental Taxation.

The paper sites relevant laws, treaties and policies as they stood on 1 April 2010.

1.0 Overview of the Environmental Taxation Policy

1.1 Malaysian Environmental Policy

The main environmental law in Malaysia was introduced in 1974 with the Environmental Quality Act 1974. Various regulations were introduced to supplement the act beginning with the Environmental Quality (Prescribed Premises) (Crude Palm-Oil) Regulations 1977 and Environmental Quality (Licensing) Regulations 1977 in the 1977. The various regulation cover issues such as Control of Petrol And Diesel Properties, Scheduled wastes, its treatment and disposal facilities , Dioxin And Furan, Control of Emission From motorcycles ,petrol engines and diesel engines, halon and refrigerant management, prescribed premises and sewage.

Unleaded petrol was introduced in the late 80s in Malaysia. The Environmental Quality (Control of Lead Concentration in Motor Gasoline) Regulations 1985 was introduced whereby the import and production of petrol which contains lead or lead compounds in excess of 0.40 gram per litre on and is banned.

In 1996, Malaysia hosted the Commonwealth Heads of Governmental Meeting. One of the major successes of the meeting was the Langkawi Declaration, the first declaration from the British Commonwealth concerning the environment.

In 2009 Malaysia introduced a comprehensive policy on the environment the National Green Technology Policy. The New Economic Model introduced in 2010 envisions Malaysia as a leader in green technology through the commercialisation of the country's biodiversity into high-value products and services and to cut the country's green house emissions to 40% of 2005 levels by 2020.[1]

1.2 Environmentalism in the United Kingdom

British Green issues go back as far as the 50's with the introduction of the Clean Air Acts (1956 & 1968).In the 70's that these issues began to emerge on the governmental scene with the 1972 Limits to Growth Report and the Stockholm Conference.
The EU is the leading authority in Environmental policy. It is one of the most important and far-reaching areas of EU legislation with up to 80% of UK legislation on environmental affairs estimated to come from the EU.

British Environmental Law was sourced from British legislation and the European Union directives. As a response to the 1989 case of Commission vs. Denmark – the European Packaging and Packaging Waste Directive harmonised the national rules on waste management in the EU member states. In 1990, Community Law on waste management was introduced and as a response to the law the UK introduced various environmental laws in 1996 such as the Landfill tax and Special Waste Regulations. The UK Landfill tax was introduced in a form similar to VAT with a charge of GDP7 per tonne of general waste. In 1999 European Climate Change Programme implemented measures mentioned in the Kyoto Protocol to tackle climate change. To support the Kyoto Protocol various measures suggested by the protocol were implemented between 2000 and 2003 including Climate change levy passed into law in the Finance Act 2000, tradable green certificate introduction, integration of environmental policies as stated in the Kyoto Protocol in the EU, ensure 22% electricity from renewable resources by 2010 in 2002, Treasury paper proposing climate change levy and the introduction of the Waste and Emissions Trading Act 2003.

British Environmental Policy especially the tax law covered local issues such as landfill, traffic congestion and employment taxation to issues covering national and international level such as climate change levy.

Economist Nicolas Stern commissioned by the British Government released The Stern Review on the Economics of Climate Change is a 700-page report released on October 30, 2006, which discusses the effect of global warming on the world economy. This report acts as a major influence on British Environmental Policy thereafter.

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[1] Malaysia committed this level of green house emissions reduction at 15th Conference of the Parties (COP 15) to the United Nations Framework Convention on Climate Change in Copenhagen in 2009.

1.3 Environmentalism in Australia

Being a country with huge rural mass, Nature and the Environment comes hand in hand with life in Australia.

The environmental movement started in the 19th century with bushwalking clubs whereby members were interested in protecting the natural landscape of rural Australia. In the next century, environmentalism dwelled on preserving the wild from destruction from economic endeavours such as logging, mining, farming and housing. Environmentalists were campaigning for the creation of national parks to protect the wilderness.

In the 1960s and 1970s biodynamic and organic farming became important issues to activists as a reaction to the widespread use of artificial chemicals in agriculture. As a reaction to the destruction of the environment in the Franklin River in Tasmania, activists grouped up to form the Greens, the first green party in Australia with the mission statement to "Peace and Non Violence, Grassroots Democracy, Social and Economic Justice, Ecological Sustainability".

Before the 1980s Australian environmentalism deals with local environmental issues detailed above. Since then activists included international issues such as global warming and the ozone depletion together with local issues as part of their activism.

The Australian environmental legal system consists of international law; Commonwealth Law i.e. laws enacted and administered by the federal government; State law and the common law system. Article 38 of the Australian *Statute of the International Court of Justice* recognises customs i.e. the general practice of nations which may be legally bound) and treaties and conventions which are formal agreements between nations and the Commonwealth of Australia. In the case *United States of America v Canada (1941) 9 Annual Digest and Reports of Public International Law Cases 315* imposes a liability on countries that pollute across the border. In 1992, Australia signed the Convention on Biological Diversity[2], an international legally binding treaty that was adopted in Rio de Janeiro in June 1992. Australia have also signed and ratified among others *Convention on the International Trade in Endangered Species 1973, International Convention for the Regulation of Whaling 1946*[3] and *The United Nations Framework Convention on Climate Change 1992*

Commonwealth law is the legislation includes the *Environment Protection and Biodiversity Conservation Act 1999 (Cth).* The federal government known as the Commonwealth exercises control on customs and export controls for trade in endangered species, fisheries, ozone and greenhouse issues, aboriginal issues, heritage issues, energy efficiency and biodiversity issues. The same issues mentioned above are also covered by State Law with the exception the aforesaid are covered from a local perspective. Other issues covered by State Law are issues concerning land, mining and petroleum

[2] Except for Andorra, the Holy See and the United States, the other members of the United Nations have signed and ratified the treaty as at 31 March 2010. The United States have signed the treaty but not ratify it.
[3] Malaysia is not a signatory to this treaty. Australia and the United Kingdom are signatories.

exploration inshore and offshore. Common law or laws coming from court decisions covers issues comprising private and public nuisance, Riparian user rights[4], negligence and native law[5].

2.0 The Comparison of Malaysian Environmental Tax Laws against Its Foreign Counterparts: A Critical Analysis by Major Sectors

British Environmental Policy especially British Tax Law is more comprehensive and structured as compared to the Malaysian Environmental Policy as the British were strongly influenced by the comprehensive European Law. EU membership requires Britain or any other member states to respond quickly to any change in any of the directives.

Australian Environmental Policy like their British counterpart has a long history since the 19th century dealing with local and international issues. Unlike both the British and Australia models, Malaysian Environmental Policy including Environmental Tax Laws is not as comprehensive or systematic with Australia and the United Kingdom.

2.1 The Energy Sector

The promotion of environmental measures and use of renewable energy especially in the form of biomass in the private sector through incentives was first introduced 8th Malaysia Plan/Five Fuel Policy which covered the period 2001-2005. The incentives in budget 2004 are

- Pioneer status

  An exemption of 70% (100% for value added products and promoted areas) of increased statutory income for 5 years for any manufacturing company which reinvests in the machinery by utilising oil palm biomass in the 2004 Budget

- Investment Tax Allowance

  Tax exemption up to 70% of statutory income for each year of assessment from ITA computed at 60% of additional qualifying capital expenditure incurred within 5 years for any manufacturing company which reinvests in the machinery by utilising oil palm biomass

For the energy related measures, companies can also qualify for higher exemptions or allowances if the activities take place in ‘promoted areas’. Originally the four fuel diversification policy focused on oil, gas, coal and hydro. In the 8th plan, it was broadened to include renewables as a fifth in the new Five Fuel Strategy.

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[4] This is a system of allocating water among those who possess land about its source. This comes from British Common Law.

[5] These are laws enacted to protect the interests and rights of indigenous Australians.

In 2003-2006 the Phase I Biogen Project came to effect in the form of Grid-Connected Power Generation and Co-Generation (Biogen) Project aims to reduce the growth rate of greenhouse gas emissions from fossil fuel by promoting biomass-based power generation and combined heat & power generation system using wastes from palm oil mills. Phase II of Biogen Project was implemented between 2007 and 2009.

In the United Kingdom various measures were taken by the government to encourage the usage of biofuel. In 2003, the price of biofuels was set a price 20p lower than low sulphur fuel. From a non-taxation perspective, the government introduced the Biofuels Directive which promotes the usage of biofuels to replace diesel and petrol for transport purposes

The Government concentrates of the promotion of the supply side of biomass through tax incentives but has not come up with the promotion of the usage of biomass from the demand side except for power generation through the two Biogen projects. In Australia tax incentive is given to vehicle owners who use biomass and Liquefied Natural Gas (LNG)/ Liquefied Petroleum Gas (LPG) vehicles.

As Malaysia is a major producer of palm oil (and biomass fuels) and the LNG/LPG, incentives to encourage the production of biomass and LNG/LPG vehicles and machines should be introduced. This will tackle the demand side of the energy sector.

2.2 Green Buildings

The Malaysia Building Integrated Photovoltaic Technology Application (MBIPV) (2005-2010) project was introduced to promote increased use of photovoltaic (PV) technology to tap solar energy and generate electricity for buildings. The project is expected to increase Malaysia's installed BIPV capacity by about 330% (2MWp by 2010), and to lower the technology unit cost by some 20% than at present.

In Budget 2010 owners of buildings awarded the Green Building Index certificates are entitled to tax exemption of 100% of the additional capital expenditure and exemption from stamp duties for first owners.

This exemption is currently implemented in Hong Kong and Malaysia. I predict Green Buildings and related incentives will be introduced to many other countries.

2.3 Transportation Sector

The Mini budget introduced the incentive to encourage the purchase of local cars the Government introduced an RM5,000 discount to encourage owners of cars 10 years or older to trade in their cars. The same measure is introduced in the United States where vouchers up to $4500 are given to owners of old cars to trade in their cars in 2009.

In the Budget of 2009 franchise holder of hybrid cars given 100% import duty and 50% excise duty exemptions on new CBU hybrid cars.

The scrappage discount both in the US and in Malaysia aims to boost sales of the lagging motor industry rather than a catalyst to take out old environmental unsafe vehicles from the roads.

The duty exemption of the import of hybrid cars is a first step towards getting Malaysian to own hybrid vehicles. However the government should encourage Malaysia vehicle manufactures to produce hybrid or electric vehicles through tax incentives such pioneer status or investment tax allowances.

2.4 Public Transport

Governments around the world give various incentives to encourage usage of public transport. In Australia to encourage businesses to invest in public transport transport, accelerated depreciation is given to taxpayers for the purchase of transport equipment. In Malaysia, instead of tax incentives, the government invests in government linked transport companies such as RapidPenang and RapidKL.

In the Budget 2009, the Malaysian government will provide a soft loan facility of 3 billion ringgit under the Public Transportation Fund, to finance the acquisition of buses and rail companies.

To encourage private transport providers to modernise their fleet, the government should consider giving the reinvestment allowances to the providers so that they can buy newer fleets.

2.5 Landfill and Waste

2.5.1 Plastic Bags

The reduction of the used of plastic bags are done at the state government level in Penang and Selangor. In Penang retailers are not allowed to provide plastic bags to their customers on Mondays to Thursday. Customers who want plastic bags will be charged 20sen per bag. The collections are donated to the poor in Penang. In Selangor plastic bags are not provided on Saturdays.

Similar measures to ban the use of plastic bags can be seen in China where plastic bags are banned since January 2008. The act of restricting the use of plastic bags through taxation or other methods is nothing new. The Republic of Ireland imposed a tax on plastic grocery bags in 2002, San Francisco became the first U.S. city to ban conventional plastic bags and the City of Los Angeles planned follow suit in 2010.

The concept of plastic bag taxation in Penang works similarly to the concept of Baitul mal[6] which is unique in Malaysia whereby the monies collected are redistributed to the poor.

2.5.2 Landfill levy

Landfill tax was introduced in a form similar to Value Added Tax (GDP7 per tonne of general waste) in 1996 in the United Kingdom. In 2001 an Aggregates Levy was introduced where GDP1.60 per tonne of garbage is charged on landfill use. Similar forms of landfill levy are also practiced in Australia.

Currently there is no similar form of taxes in Malaysia. Garbage disposal is under the jurisdiction of the local government and financing of garbage disposal activities are done through local government taxes. Malaysian introduced the integrated solid waste management system in the National Strategic Plan in 2005 and Solid Waste and Public Cleansing Management Act in 2007 but no mentioned was made on landfill taxation.

2.5.3 Waste recycling

To promote waste recycling in industry Malaysia introduced various incentives in the form of Pioneer status, Investment Tax Allowances, Accelerated Capital allowance and Reinvestment Allowances. Accelerated depreciation for selected capital works and accelerated deductions for environmental expenditure are the two incentives for the Australian taxpayer.

In the United Kingdom, the government concentrates on recycling even up to the level of the householders. The Climate Change Bill enables local authorities to pay rebates to householders for good performance on recycling and waste minimisation. They also allow an authority, if it chooses; to collect incentive based payments from householders for their waste collection. Authorities will also be able to pay back rebates, and collect any payments, through the Council Tax system, should they wish to do so.

It is commendable that Malaysia is starting to encourage its citizens beginning with the business sector to recycle. However a more comprehensive recycling policy which includes the household should be introduced. Like the recycling rewards system, measures like the compulsory separation of garbage should be introduced. Recycling at the household level is done through associations and not at government level. For example, Rukun Tetangga organises a monthly recycling collection day and the Turn Rubbish into Cash by the Penang First Assembly of God.

6 The national treasury. Taxes go into the baitul mal (the house of currency). The money from this is used to fund the state, its endeavours and to support the poor.

2.5.4 Water and sewerage disposal

Indah Water Konsortium Sdn Bhd , is a government owned national sewerage company which has been entrusted with the task of developing and maintaining a modern and efficient sewerage system in Malaysia with the exceptions of Kelantan, Sabah, Sarawak and the Majlis Perbandaran Johor Bahru. Various tariffs for sewerage are charged to domestic, commercial, industrial and governmental users.

Similar systems managing sewerage exist in countries such as the United Kingdom, United States and Australia.

2.5.5 Used oil recycling

In Australia the government introduced a fund to encourage companies to get them involved in the industry of used oil recycling.

No such effort exists in Malaysia. In fact used oil especially motor oil recycling and cooking oil recycling is a good industry Malaysians should get involve in.

2.5.6 Deposit-Refund System

A deposit-refund system is whereby a refund is paid to the consumer when they return an item to a collection centre. In the United States, California, Connecticut, Delaware, Hawaii, Iowa, Massachusetts, Michigan, New York, Oregon and Vermont enacted deposit-refund systems for drink containers. This was practiced in Malaysia until the 1980s where beverages were now supplied in aluminium containers.

Creative usage of the deposit-refund system is practiced in Europe. Germany subjects the buyer of lubricating oil with a tax which will be refunded when the buyer returns used oil. In Sweden and Norway, buyers of new cars pay a deposit at the time of purchase for the car. When the car is scrapped, the owner must send the car to an authorised junk dealer to claim his deposit.

Currently in Malaysia, trading of cooking gas in canisters is the only system in Malaysia that still retains the deposit-refund system.

2.6 Employment Taxation

In Malaysia, the provision of employee transport is a deductible expense under section 33 of the Income Tax Act 1967. In Australia, employee transport claims if the employee uses public transport is a deductible business expenses. In the United Kingdom to encourage employees to use public transport car parking facilities provided for employees are considered non-deductible in 1997. This expense was previously considered of deductible in 1988.

2.7 Certified emission reduction units

Malaysia exempted the income from the sale of certified emission reduction units from tax from the year of assessment 2008 to 2010. However this exemption might be revoked beginning the year of assessment 2011. However there are plans for the Malaysian government to incorporate certified emission reduction units with "Green Palm Oil". However according to the New Economic Model for Malaysia Part 1 report this initiative can work if a more comprehensive and binding global carbon trading and emissions regulation is set up.

2.8 Land Protection Incentives

To encourage farmers to practice sustainable farming, the Australian Government provides tax incentive for landcare, accelerated depreciation for equipment to reforest and tax subsidy for farmers to divide their land between agriculture and reforesting.

The Malaysian Government can take a queue from the Australian Government by encouraging the production of Green Palm Oil, whereby palm oil is produced in an sustainable manner. Green Palm Oil incentives could be given to palm oil producers to produce green palm oil. Large buyers of palm oil such as Unilever require their suppliers to produce sustainable products. Sinar Mas of Indonesia from terminated as a Unilever supplier in December 2009 as Sinar Mas was accused to have produce palm oil in a non sustainable manner.

2.9 Other issues

Apart from the issues mentioned above, Australian tax law dealt in issues such as Aircraft noise a levy and ozone protection levy. In China, the local government in Hangzhou introduced a tax to protect the beauty of parks in Hangzhou. A survey on the public in Hangzhou found that the public are willing to pay the tax in order to protect the heritage of Hangzhou.

Malaysia in the past years have been concentrating a lot on Islamic Banking with the hopes of establishing Malaysia as an international hub for Islamic Banking. The Malaysian Government through the New Economic Model plans to introduce Green Banking to Malaysia. [7]Green banking is a banking system whereby funds are channelled by the financial institution to fund environmental or ethical projects. This form of banking exists in the United Kingdom and France. An example of a big player in this form of banking is Crédit Agricole which came about through the merger of local French banks dedicated to providing financing to farmers. Currently AgroBank (the former Bank

7 Malaysia plans to "develop banking capacity to assess credit approvals for green investment using non-collateral based criteria, liberalise entry of foreign experts specialising in financial analysis of viability of green technology projects and support green technology investment with greater emphasis on venture capital funds" through the New Economic Model launched on 30 March 2010.

Pertanian Malaysia Berhad) which is similar to Crédit Agricole in terms of objectives do not have similar schemes available to customers.

3.0 Recommendations and Conclusion

As a fellow signatory[8] to the Kyoto Protocol, Malaysia has agreed to cap emissions in accordance with the Protocol. To operationalize the protocol, a change in environmental policy including tax law is needed by the Malaysian government. The change in Malaysian tax law when dealing with the environment deals more towards industry rather towards the individual tax payer. Among the major tax incentives Malaysia has put in place to encourage industry to be more environmental friendly are initiatives such as

- Double Deduction
- Research Expenditure under Section34A
- Technical services - payment of usage of testing equipment in FRIM, universities
- Travelling costs
- Research expenditure - Cash contribution
- Expenditure incurred on International trade Fairs
- Capital allowances
- Special rates for plants
- Plant and machinery for recycling wastes
- Plant and machinery for conservation of energy

The United Kingdom has a very systematic form of environmental taxation framework partly thank to the pressures of the needs of the EU which has one the most comprehensive framework in the world on environmental protection. British environmental taxation laws cover not only the needs of the business sector but also from the individual taxpayer. The same goes for Australian tax law which is comprehensive. To review British environmental policies including tax law, apart from the requirements of the EU, special national studies were made such as the The Stern Review on the Economics of Climate Change were made. This system of review allows British Tax law to be comprehensive and systematic.

In Malaysia tax law is modified when there is a requirement and the change is piecemeal, for example the banning and later the subsidy of Unleaded Fuel in 1991 were in response to the Haze of 1991. Two major environmental polices were introduced in 2002 in the form of the National Policy of the Environment and 2009 in the form of the National Green Policy The National Policy of the Environment is *set to harmonise economic development goals with environmental imperatives* and deals with issues such as the stewardship of the environment, conservation of nature and diversity, continuous improvement in the quality of the environment, and sustainability. Issues from the finance point of view were hardly touched. The National Green Policy deals with using green technology as a way to accelerate the Malaysian economy and to promote sustainability.

[8] Malaysia signed on 12 March 1999. The protocol is ratified by Malaysia on 4 September 2002.

Both policies dwell on how to achieve sustainability from a science point of view rather that from a finance point of view – including the mode of taxation.

At this juncture in order for Malaysia to have a more comprehensive environmental policy including a tax policy, tax laws needed to be reviewed from a macro level rather than a need to do basis. The areas that need review include

- Companies Tax Law
- Individual tax Law – including employment tax law
- Local Government Laws
- Custom Duties

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