CHAPTER 1

INTRODUCTION

1.1 Introduction

This chapter outlines the entire thesis. The first section of this chapter, which is Section 1.1, discusses the background of the study. Section 1.2 will explain the problem statement, and Section 1.3 will highlight the research questions and objectives. It will be followed by the scope of the study and the research methodology, described in Sections 1.4 and 1.5, respectively. Section 1.6 will discuss the study's contributions to the tax rebate literature, zakat institutions, and the Inland Revenue Board of Malaysia (IRBM). Finally, Section 1.7 will present the organisation of the study.

1.2 Background of the Study

Zakat and taxation are two crucial elements in Islam because both are associated with obligation and compulsion (al-Qardawi, 1973). Zakat is imposed on Muslims only, but taxes are imposed on all taxpayers, whether Muslims or non-Muslims. Zakat is mandatory to all Muslims as its obligatory nature is ordained in al-Quran and hadith.

Zakat is one of the most important elements in establishing social justice. According to Al-Qardawi 1973, zakat is essential as a social welfare levy imposed to members of the Islamic society who are wealthier than the others. Those with a certain level of accumulated wealth (*nisab* & *haul*) are obligated to pay zakat to purify themselves from the sins of greed. Allah has commanded the zakat obligation to humans as His servants through Prophet Muhammad (PBUH) to remove poverty from society.

Zakat is one of the recommended sources to help the poor while improving socioeconomic growth, especially in Islamic countries. The word “zakat” is mentioned 30 times in al-Quran (Md. Shariff et al., 2011), and paying zakat is one of the five pillars of Islam as stated by the Prophet (PBUH) in a hadith narrated by al-Bukhari:

> *"Islam is made up of five pillars: testifying that there is no God but Allah and Muhammad is the Messenger of Allah, five daily prayers, pay a zakat, fasting in Ramadan and perform Hajj”*

Meanwhile, tax is a valuable source of revenue which can be used effectively by governments for public purposes. Government needs to raise revenue, and one of the most effective means is through the imposition and collection of taxes. Nowadays, tax revenues have become a major contributor to the development of a nation for the benefit of its people. Taxation has also been used as a tool for promoting growth and development in many countries (Shaharuddin et al., 2012).

Based on this premise, zakat and tax are two crucial sources of income for Islamic countries worldwide. There are three categories of Islamic countries consisting of 57 member states with 47 countries being Muslim majority countries. These three categories can be divided into under-developed, developing, and developed countries (Muhammad et al., 2016).

For developing countries like Malaysia and Indonesia, their total tax collections in 2017 were RM 123.233 billion (IRBM, 2017) and RM 285.33 billion (Ministry of Finance of the Republic of Indonesia, 2017), respectively. Meanwhile, the total zakat collection for Malaysia was RM2.45 billion in 2014 (JAWHAR, 2017), while Indonesia collected zakat totalling RM 1.11 billion in 2015 (Outlook Zakat Indonesia, 2017).

Muslims are obligated to pay two types of taxes every year, namely, modern taxation and Islamic taxation (zakat). N. Samad et al. (2011) found that how the obligation is fulfilled differs between zakat and tax systems. In the taxation system, an individual will be considered as not complying with the tax law if he/she fails to pay tax through a formal institution. However, in the zakat system, an individual who does not pay zakat through a zakat institution does not necessarily fail to fulfil his/her obligations, as the obligations can be met by making payments directly to *asnaf* (beneficiaries).

Specifically, Muslims in Malaysia who fulfill the requirements needs to make two compulsory payments from their income, which are called income tax and zakat. Malaysia is one of the countries where zakat contributions are voluntarily paid to zakat institutions. N. Samad et al., (2016) stated that Muslims in Malaysia have a choice whether to pay zakat or not to the zakat institutions. However, although payment is voluntary, they still have to pay zakat because it is one of their religious duties of a Muslim.

Concerning the two compulsory payments of tax and zakat, the Malaysian tax system provides zakat rebate for individual Muslims who need to pay both tax and zakat. The rebate allows Muslims to avoid paying two overlapping compulsory payments each year. The zakat rebate will be deducted from an individual's total income tax in a year of assessment. This rebate will reduce the amount of total tax payable by Muslim taxpayers every year. In some cases, the rebate amount is large enough to reduce the income tax to RM0. Hence, this rebate minimises Muslims' obligation in paying both zakat and tax.

According to the Income Tax Act 1967, two types of rebates are applicable to a resident individual. First is the rebate for self and wife under Sec 6A (2) of the Income Tax Act (ITA), and second is the rebate for zakat *al-mal*, zakat *fitr*, or other Islamic religious dues as stated in Sec 6A (3) of the ITA:

> *"A rebate shall be granted for a year of assessment for any zakat, fitrah or any other Islamic religious dues payment of which is obligatory, and which are paid in the basis year for that year of assessment to, and evidenced by a receipt issued by, an appropriate religious authority established under any written law."*

This study will focus on the second type of rebate provided for resident Muslim taxpayers if they pay zakat on their income. As such, the main aim of this study is to examine the factors that influence resident Muslim taxpayers' intention to claim zakat payment as a tax rebate. This study will discuss further how this rebate system affects the intention of resident Muslims taxpayers to claim zakat payment as a tax rebate.

1.3 Problem Statement

Muslims are responsible for paying zakat and tax, which is considered as two obligations that needs to be complied (Akbar & Saimkayadibi, 2012). Regarding this, Malaysia is one of the few Islamic countries that integrate zakat in its tax system. The Inland Revenue Board of Malaysia (IRBM) implemented the zakat rebate into the tax system in the year 2001 for individual taxpayers to reduce two obligations of Muslim individual taxpayers in complying with both responsibilities (IRBM, 2014). Zakat rebate can be claimed by each resident Muslim individual taxpayer in Malaysia.

Nevertheless, there is still a lack of details provided by the IRBM after more than 17 years of the implementation of the zakat rebate. Also, there is no statistics or details on the percentages of Muslim taxpayers who have claimed the rebate as well as non-compliance issues such as claiming the rebate without providing the original receipt of zakat payment. The lack of data and research affects the effectiveness of the integration of zakat and tax, thus making it difficult to assess the extent that this system affects the intention and behaviour of Muslim taxpayers in claiming zakat as a tax rebate.

Bakar and Rashid (2010) examined the factors influencing Muslims' behaviour towards zakat on income among academicians from three faculties at the International Islamic University Malaysia (IIUM). In the study, three variables, which are sociality, religiosity, and economic motivations, were examined as factors that influence Muslims' behaviour to pay zakat on income. The study also included knowledge on tax rebate as the external factor. However, the results of the study revealed that tax rebate is not a prime factor for paying zakat on income. Therefore, it indicates that the taxpayers do not rely on the tax rebate system provided by the government in paying zakat on income.

On a similar note, Al-Mamun and Haque (2015) examined the factors influencing Muslim consumers' perception of the zakat rebate in Malaysia. In the study, a total of six factors were used, which include knowledge about zakat, knowledge about tax, halal–haram aspects, legal consciousness, religious consciousness, and perception of tax through the zakat system. The findings of the study showed that all the factors positively influence Muslim consumers' perception of the zakat rebate system. However, it is worth noting that the perception of Muslim consumers does not completely determine their intention and behaviour towards this system. A possible explanation of this scenario might be that perception is considered more of an opinion of the respondents who may not have any experience in using the system.

Recognising this gap, the present study attempts to examine the factors that might influence the compliance of Muslim taxpayers to claim zakat payment as a tax rebate. To explain how this compliance affects the intention of Muslim taxpayers towards the system, the study uses the Theory of Planned Behaviour (TPB), which was proposed by Ajzen (1991). Attitude, subjective norm, and perceived behavioural control are included as the factors affecting the compliance of Muslim taxpayers. Knowledge is added as another variable in this study.

1.4 Research Questions and Research Objectives

This study aims to examine the variables that influence the intention of taxpayers in claiming zakat payment as a tax rebate. The variables in the TPB, which are attitude, subjective norm, and perceived behavioural control, are used to examine taxpayers' intention and behaviour with knowledge as an additional variable. The knowledge variable is added to assess the level of Muslim taxpayers' knowledge about the tax rebate system in Malaysia.

Besides, the study attempts to identify which factor among the four variables has the most influence on taxpayers' intention to claim zakat as a tax rebate. Also, the study assesses whether the TPB variables and knowledge can determine taxpayers' intention to claim zakat as a tax rebate.

Research questions:

1. Does attitude influence taxpayers' intention to claim zakat payment as a tax rebate?
2. Does subjective norm influence taxpayers' intention to claim zakat payment as a tax rebate?
3. Does perceived behavioural control influence taxpayers' intention to claim zakat payment as a tax rebate?
4. Does knowledge influence taxpayers' intention to claim zakat payment as a tax rebate?

Research objectives:

1. To examine the relationship between the taxpayers' attitude and their intention to claim zakat payment as a tax rebate.
2. To examine the relationship between the taxpayers' subjective norm and their intention to claim zakat payment as a tax rebate.
3. To examine the relationship between the taxpayers' perceived behavioural control and their intention to claim zakat payment as a tax rebate.
4. To examine the relationship between the taxpayers' knowledge and their intention to claim zakat payment as a tax rebate.

1.5 Scope of the Study

This study aims to examine the variables influencing Muslim taxpayers' intention to claim zakat payment as a tax rebate. The focus of this study is individual Muslim taxpayers who have no business income. The variables involved are attitude, subjective norm, perceived behavioural control, and knowledge.

1.6 Research Methodology

This study adopted the quantitative research methodology using questionnaires that were distributed and e-mailed to individual Muslim taxpayers in Selangor. A non-probability sampling technique, namely simple purposive sampling, was used to select the sample. This sampling technique allowed the researcher to obtain a high degree of representativeness in the sample. The collected data were analysed and interpreted using the Statistical Package for Social Sciences (SPSS).

The study also used multiple regression analysis to explore the relationships among the independent and dependent variables. Multiple regression analysis is carried out when a study requires further examination to expand the value of a variable (dependent variable) based on the value of two or more other variables (independent variables).

1.7 Thesis Contributions

The importance of the study can be articulated as the contribution to the tax rebate literature, zakat institutions, and the Inland Revenue Board of Malaysia (IRBM).

1.7.1 Tax Rebate Literature

This research is an early study in Malaysia on taxpayers' intention to claim zakat as a tax rebate. It is important to study the intention of taxpayers, as it provides insights on the variables that influence the taxpayers to claim zakat payment as a tax rebate. Consequently, this study contributes to the scarce zakat-taxation literature.

The results of this study use the conclusion of TPB by Ajzen and Fishbein (1991), which mentioned that attitude, subjective norms, and perceived behavioural control significantly affect the intention of the people. This study also makes a significant contribution to expanding the TPB by providing new information from the additional variable tested by the researcher. The level of knowledge of Muslim taxpayers will be discussed at the end of this study. The addition of this variable presents an important contribution to the tax rebate literature, and the findings can be used as a reference for future studies.

1.7.2 The Inland Revenue Board of Malaysia (IRBM) and Zakat Institutions

Besides contributing to the literature, it is hoped that the findings of this study will be useful to the tax and zakat practice by contributing the IRBM with a better understanding of taxpayers' intention in claiming zakat payment as a tax rebate. This study discusses the factors of taxpayers' intention in using the zakat rebate system implemented by the government.

This study is also essential in helping the zakat institutions in Selangor to gain a better understanding of the intention of taxpayers to claim zakat as a tax rebate. At the end of this study, the researcher will discuss some suggestions for improving the factors that influence the intention of individual Muslim taxpayers to claim zakat as a tax rebate.

It is hoped that the IRBM and zakat institutions will adopt these recommendations to encourage individual Muslim taxpayers to make tax and zakat payments on income. It is also hoped that the IRBM will prioritise on these recommendations to inculcate positive intentions among Muslim taxpayers towards the rebate system that has been provided for them.

1.8 Organisation of the Study

This research is structured into six chapters.

Chapter 1 presented the introduction, which outlines the background of the study, problem statement, research questions and objectives, scope and limitations of the study, and the research methodology. The thesis contributions to the tax-zakat literature, IRBM, and zakat institutions were also discussed.

Chapter 2 will discuss the overview of Malaysian tax and zakat administration, which outlines the tax administration and zakat system in Malaysia. Furthermore, the researcher will discuss tax and zakat from the perspective of *fiqh*. The study will also discuss the integration of tax and zakat in the tax system. This chapter aims to provide insights using an illustration of the zakat rebate calculation on individual income tax.

Chapter 3 will review the literature on zakat and tax compliance. This chapter will also elaborate on the Theory of Reasoned Action (TRA) and the Theory of Planned Behaviour (TPB). In addition, this chapter will explain the factors that influence the intention of people towards tax and zakat compliance. Theoretical and conceptual frameworks will also be depicted in this chapter.

Moving on, Chapter 4 will explain the research methodology, which contains the research design. This chapter will also discuss the sampling design, data collection method, and data analysis for the quantitative approach. Next, Chapter 5 will present the results drawn from the data that were analysed using a quantitative approach.

Finally, Chapter 6 will further discuss the findings presented in Chapter 5. This chapter will also elaborate on the contributions and practicality of the implications of the present study. It will also highlight the research limitations and offer some suggestions for future research. This chapter will then summarise and conclude the thesis.