



# Developing a Modern Tax Framework for Malaysia

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# Introduction

There is obviously a need to reform or modernize Malaysia's tax framework to fit the nation's requirements.

Increasingly complex business transactions, rising cross-border transactions, new ways of doing business, the current speed of change and technological developments – all of these factors are contributing to the demand for a tax framework. In particular, these factors are contributing to the demand for a tax framework that is agile and able to meet the requirements of businesses where digitalization, geopolitical and technological disruptions are the norm.

The introduction of any new taxes or a broadening of the scope of existing taxes should be preceded by a detailed study, paired with a robust consultative process with relevant stakeholders, such as regulators and industry representatives. Reforms to the tax system should be more inclusive, benefiting small and medium enterprises, which form the backbone of the economy.

So, what kind of tax framework is suitable for the future?

## 2. Necessary Features for a Tax Framework

An appropriate and advanced tax framework that would be needed for the future of the economy needs to have the following features.

### *1. Simple and easily understood*

A good tax framework, that will stand the test of time, needs to be simple and easily understood. Tax laws should not be overbearing, so that taxpayers are able to comply with the rules without being burdened by high compliance costs. Make the filing of tax returns and payment of taxes easy for taxpayers so that they can manage their tax affairs anywhere, anytime.

### *1.1. Transparent and fair*

Tax authorities should be clear about their role and objectives when formulating tax policies and preparing tax legislation. The impact of policies and legislation on industries and businesses needs to be carefully considered and measured. Modifications to the tax legislation should be done with the aim of improving the overall quality of the legislation, such as providing greater clarity and transparency on the tax treatment that impact businesses.

Authorities also need to consider the practical implications of these modifications, such as how the law will be administered consistently and how disputes can be resolved quickly, fairly and in a cost – effective manner. The imposition of penalties, for instance, needs to be carefully thought through. The severity of penalties developed should be based on the behaviour of taxpayers. A person who makes an unintentional error should not be penalized, while those who deliberately choose not to fulfill their tax obligations will need to face stiffer penalties.

In situations where there is a disagreement with the decisions or legislative interpretation of the tax authorities, taxpayers should be given fair and equitable appeal avenues. This helps to build trust and confidence in the system – that the right thing will be done – and in turn, fosters a greater willingness to ensure tax obligations are fulfilled.

### ***III. Robust and flexible***

A good tax system needs to be robust and yet flexible enough to ensure that it keeps up the pace with economic growth and global developments, while taking into account the needs of the country and its businesses. The system must consider the big picture, to promote economic efficiency and encourage behaviour that contributes to economic development. For example, tax incentives encourage the growth of certain sectors, while taxes are imposed on certain activities to discourage specific behaviours.

### ***IV. Communicative and engaging***

A factor that contributes to the success of a tax framework is that of the active engagement and communication with the taxpaying public. The behaviour and performance of the tax administration contributes significantly to the public's perception about paying taxes. An effective tax administration collects the right amount of tax at the right time, with minimal cost to the Government whilst being equitable to taxpayers. It allows the Government to deliver services and manage the country, while minimizing obstacles to businesses and economic growth.

For this to happen, continuous consultation and engagement with taxpayers is required, and understanding the real implications of tax legislation on businesses is important. An effective tax framework that is fit for the times really boils down to the basic principles of ensuring that transparent and fair laws are applied to all, at the appropriate times, in appropriate measures, for the good of the greater community.

# 3. Features of Our Tax Reform

Tax reform is essential as part of a credible and sound fiscal management framework, if Malaysia is to move forward towards becoming a highly competitive and dynamically developed nation. The proposed tax reform's central priorities are not only **on the efficiency and effectiveness** of the tax system to counter tax avoidance and evasion but to also to take into consideration the aspects of **equity and fairness**.

In general, tax reform must be built on the following features:

- a **Fairness and the lowering of the overall tax burden** to provide more incentive to work, save, invest and compete.
- b **International competitiveness** for businesses and to encourage more investments in high technology and value-added sectors, create jobs and to ultimately raise economic growth potential.
- c **Effective, simpler and less complex tax administration** so as to minimize compliance costs, reduce business costs as well as to discourage tax avoidance and evasion. The complexity of the tax system and fiscal incentives/reliefs/allowances, in terms of qualifying and reporting requirements, increases costs, especially for Small and Medium Enterprises (SMEs).
- a **Revenue adequacy and sustainability** to enable prudent spending and budget management while maintaining fiscal stability.



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## 4. Issues for Consideration

There are four pillars in achieving a fairer tax system: **incentives, certainty in law, consistency and simplicity.** Their implementation needs to be fairer and non-discriminatory between the different sectors of the economy.

An overly preferential tax treatment for one sector relative to others not only encourages rent-seeking behaviours, but also creates distortions, in terms of resource allocation, and could cause a bias in terms of investment choices among sectors or activities.

Globally, countries are stepping up to create efficient, balanced and effective tax systems. While globalization and digitalization facilitate freer capital flows, enhancing the mobility of skilled workers and deepening wider cross-border trade flows, they also increase the opportunities for tax avoidance and evasion, and hence put competitive pressures on Malaysia to design a tax policy that is time-tested in the global marketplace and investment arena.

In formulating the proposed tax policy in a globalized and complex environment, we have to take into consideration the following implications and externalities:

- a While corporate income taxes can influence the choice of investment location, a conducive business-friendly regime and regulatory environment, supported by stable macroeconomic conditions are equally important factors.
- b High tax incidence, compliance and business costs can affect the cost of producing goods and services and hence, erode relative international competitiveness.
- c Sales and other related taxes would impact tourism, e-commerce and cross-border shopping as they can influence tourists' spending on domestic goods and services as well as the hospitality sector.
- d Personal income taxes can influence the mobility of labour, increase the supply of the domestic workforce and attract talented workers in the choice of the country in which they wish to work.
- e Taxes imposed on the input and the raw materials, cascading through the production process, can dampen production and investment as well as penalize exports.
- f Excessive taxation, such as excise duties on certain sectors (e.g. cigarettes and liquor), whilst intended to discourage smoking and promote a healthy lifestyle and raise tax revenue, it encourages the consumption of illegal products and rampant smuggling activities. This results in the loss of billions of ringgit of potential Government revenue.

The tax system also needs to avoid ambiguous interpretations, exemptions and loopholes that can distort investment decisions and consumer choices. Most importantly, domestic companies and foreign multinational enterprises are attracted to a stable and predictable tax system, which is administered in an efficient and transparent manner. Based on recent global developments, data points to the need to shift away from taxing employment and business activity and towards taxing ownership and consumption.





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## 5. The Problem of Tax Revenue Base in Malaysia

The tax revenue base of Malaysia is extremely narrow. For example, the 2012/2013 Economic Report stated that 21% of registered companies (i.e. 107,043 out of 508,150 companies registered with the Inland Revenue Board) and 15% of employees were subject to income tax. With around 2.2 million individuals paying income taxes compared to a workforce of 14 million, this puts into focus the extremely narrow base from which the Government tries to extract its tax revenue. In addition, oil-related revenues generate around 30% of the total revenue of the Government.

The personal income tax base is affected by the granting of too many personal reliefs/subsidies and there is a need to collapse these into 4 or 5 broad categories. Instead, as part of political expediency, we keep increasing reliefs/subsidies. The 2013 Budget change geared to lower personal income tax rates was a populist move which took 170,000 taxpayers out of the tax net. This move

was part of a continuation of such policies implemented in the past 15 years, where taxpayers went out of the tax net for similar reasons.

As for the corporate tax rate, it will be a challenge to lower it under current economic circumstances if there is no additional tax revenue generator. Thailand had announced a move to a 20% tax rate, as has Indonesia. Even the United Kingdom had lowered its corporate tax rate to 19% in 2017, though the pandemic has now led the Government there to consider raising tax rates in order to build reserves given the huge outlay made to manage the Covid-19 pandemic. But, then again, if we look at a European nation, we have to bear in mind that there the VAT/GST systems are matured and the tax rates are generally at higher levels. As part of a strategic move to draw foreign direct investment and remain competitive, Malaysia too needs to move similarly with probably a 1% annual cut in the corporate tax rate and widening the scope of its consumption taxes.

As such, the Government does face some serious constraints and the issue of tax evasion and the under-reporting of income is also an area that needs substantial research, as the hidden and informal sectors can generate substantial tax revenue. A robust fiscal framework (over say a 5 to 10 year time frame) to outline the way forward is what we need.

Based on the *Fiscal Outlook Report (Section I: Fiscal Policy Overview)* issued by the Malaysian Ministry of Finance (MOF) in 2018, some of the key lessons from cross-country fiscal reform experiences are:

- Tax increases are more detrimental to growth than expenditure cuts.
- Reforms based on expenditure cuts are more likely to succeed and are longer lasting than reforms based on tax increases.

- Expenditure cuts should not be across the board as it affects long-term economic growth.
- Adopt gradual fiscal consolidation if there is fiscal space to do so.
- Public engagement and public support are important factors necessary for the success of reforms.
- Pragmatism in the fiscal reform commitment is needed to allow for unforeseen circumstances which require adjustments of fiscal reforms.

## 6. Possible Solutions

Based on the current situation, a suggested reform focus could logically be in the following areas:

- a. Increase in tax effort (reducing the tax gap).
  - ▶ Enhance compliance and strengthen enforcement;
  - ▶ Widen coverage to encompass the informal economic sector;
  - ▶ Reduce tax evasion;
  - ▶ Promote voluntary tax compliance.
- b. Reform the tax structure.
  - ▶ Increase the shift to indirect taxes (broaden coverage of the existing consumption taxes and increase the tax rate, as dictated by condition and need);
  - ▶ Introduce wealth, digital and capital gain-based taxes, depending on the circumstances.
- c. Streamline the tax incentive regime.
  - ▶ Institute a review on the use of incentives and their effectiveness;
  - ▶ Simplify the tax incentives legislation i.e. the Promotion of Investments Act 1986;
  - ▶ Ensure a level playing field and equal access for both domestic and foreign investors.

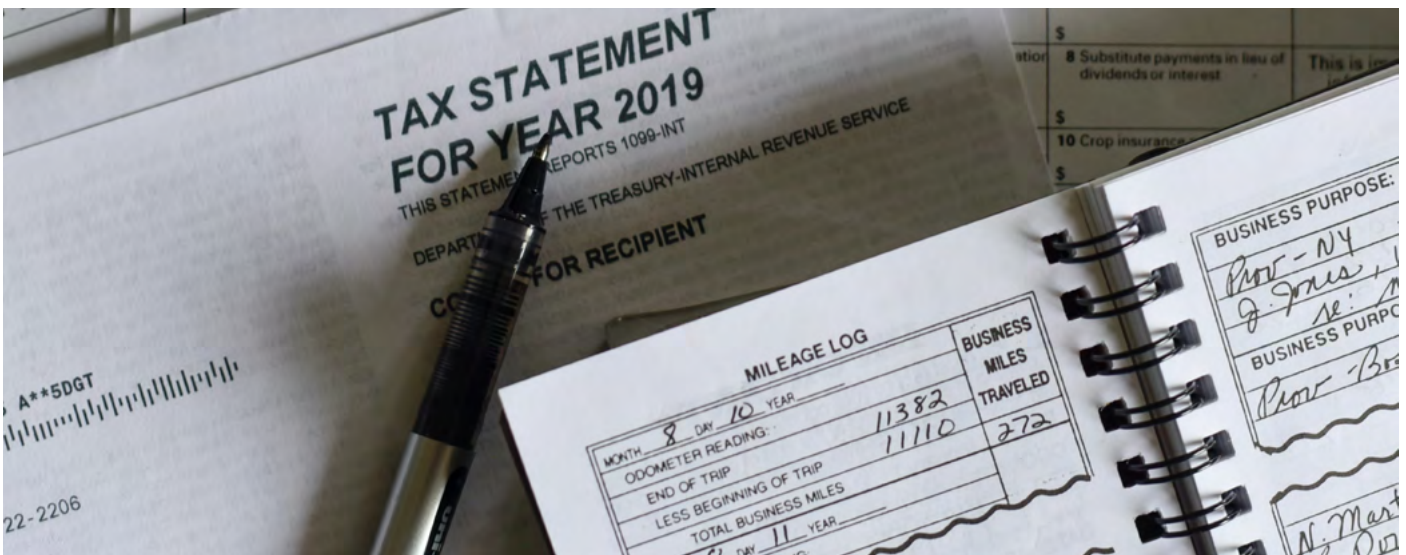


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- d. Technology deployment, database and information sharing.
- ▶ Develop integrated databases and systems with inter-agency information sharing;
  - ▶ Deploy artificial intelligence and data analytics to strengthen tax administration.

When one looks at the various types of taxes that can be imposed, these can only fall into the following three categories:

1. Income taxes.
2. Wealth taxes.

In terms of the principles of effective design of a tax, various studies and reports suggest the following principles:

- Simplicity;
- Neutrality;
- Stability;
- Flexibility.

All these will then have to be enmeshed within the objectives of imposing taxes which adhere to the following aspects:

- Funding of Government expenditure;
- Equity and Redistribution;
- Macroeconomic stabilization;
- Behavioural change;
- Growth and Competitiveness.

All these were also stated in the Mirrlees Review in the United Kingdom where the UK tax system was analyzed and the review was published by the Institute for Fiscal Studies in the form of two books, “Dimensions of Tax Design” in 2010 and “Tax by Design” in 2011.

With regard to designing an effective system, the Mirrlees Review also made the following suggestions:

- Welfare and economic efficiency: Minimize negative effects of the tax system on welfare and economic efficiency.
- Administration and compliance costs: Select a system that costs less to operate, other things being equal.
- Fairness other than in the distributional sense: Ensure fairness of procedure, avoidance of discrimination, and fairness with respect to legitimate expectations.
- Transparency: A tax system that people can understand is preferable to one that taxes by ‘stealth’.

Malaysia thus needs to:

- Introduce a strategic plan on the direction forward in respect of developing and improving the sources of tax revenue especially since oil reserves (from which petroleum income tax and royalties are generated) will dwindle in the near future.
- Review the legislative framework, **holistically**, to simplify current provisions and to remove archaic ones.
- Keep tabs on improvements in the tax legislation in the region and other parts of the world. Make proactive suggestions to reform and enhance the current structure so that we are in sync with worldwide developments.

Measures put into place to address the long-standing deficit need to move into a higher gear. Of course, the pandemic has caused the deficit to widen and that makes it imperative that steps are taken to plan for the necessary calibration needed, post-pandemic. This has been suggested by many commentators and some of the measures are listed below:

- Effective revenue and public expenditure management is needed. Controlling expenditure will be challenging in view of the various commitments that the Government has made in terms of various development projects as well as the fact that curbing the rise in operating expenditure is difficult, due to the 'locked-in' nature of these expenses. Nevertheless, Government contracts could be made more effective with clear, transparent, open tenders and clear anti-corruption parameters set across all agencies.
- Subsidy rationalization should be continued with vigour. The need to continue to focus on targeted subsidies for those with low-incomes and the poor, or unemployed, is imperative. The granting of subsidies which are not being applied in the manner intended must also be eradicated. Thus, the efficiency of public transfers has to be re-examined as transfers cannot be done without equal contribution of the recipients.
- A very robust and clear public relations policy needs to be implemented by the Government, to ensure its accountability, as the public needs to be kept informed on a timely basis. Issues will not go away but will simmer down and boil over after some time and this can be counter-productive to the nation.

Below are listed some key areas that can be considered for new policy implementation. It is to be noted that a few of the measures have already been introduced in the 2019/2020/2021 Budgets presented in Parliament.

## **A. The Underground Economy – Under-reporting/under-declaring**

- Introduce a tax file number for all.
- Monitor all data points effectively.
- Issue serially numbered receipts for all sales/services rendered by a business.
- Implement a voluntary disclosure program for a limited period of time.
- Presumptive taxation for small traders/difficult-to-tax sectors based on the sales made in a year, and avoid the need for a full set of accounts to be maintained.
- Enhanced enforcement and effectively widen investigation activities.
- Curtail the smuggling of taxable goods/under-declaration of imported values.

## **B. Reduce Tax Leakag**

- To only grant incentives to desired sectors / type of investment—focus only on pre-packaged incentives for big-ticket investments and introduce cost benefit approach/measures.
- Remove all other incentives e.g. double deductions, accelerated allowances, etc.
- Consider using the corporate tax rate as an incentive i.e. either offer a 5% rate or a 10% rate instead of total exemption.
- Tie incentives to strict key performance indicators or conditions and withdraw incentives if there is any non-compliance with the relevant conditions.

- Cut down the number of agencies involved in granting / approving tax incentives.
- Limit/restrict carry-forward of business losses, capital allowances, unutilised incentives to 5-7 years.
- Reinvestment Allowance – review/restrict scope and limit carry-forward to 5-7 years.
- Limit or remove exemptions in real property gains tax (RPGT), stamp duty and other taxes.
- Ensure that the use of discretionary powers by the Inland Revenue Board (IRB) or the Minister of Finance is subject to clear internal criteria so as to limit any possible abuse.
- Reconstitute the concept of Designated Area (DA) or Special Area (SA) (indirect taxes) so as to eliminate abuse.

### **C. Enhance/Improve Tax Administration**

- Effective data management in the tax agencies (IRB/Customs Department) and linkage with other agencies.
- Data analytics (including predictive software to measure cost/revenue impact).
- Improve the way tax audits are carried out.
- Enhance investigative capabilities.
- Review the recognition of income for income tax purposes, as it should be closely aligned to accounting standards.
- Review the deductibility of expenses for tax purposes:
  - a. Align to accounting standards;
  - b. Make it easier to determine deductibility e.g. entertainment, interest restriction, etc;
  - c. Make the law simpler / easier to compute tax liability.
- Corporate governance expenditure to be clearly designated as being tax deductible.



- Review personal income tax rates and tax reliefs and consider widening the chargeable income bands, set suitable tax rates in line with global developmental trends.
- Simplify the appeals process especially for the first stage of appeal at the Special Commissioners of Income Tax (consider appointing more Special Commissioners and do not limit these to civil servants as there are many distinguished lawyers/tax practitioners who can also serve as Special Commissioners) as well as consider Tax Courts as an alternative to the Special Commissioners.
- Make it easy for taxpayers via technology to meet their obligations as well as use the website effectively.
- Taxpayer rights to be monitored effectively.

#### **D. New Sources of Tax Revenue**

- Digital economy – online foreign suppliers/business users in the country (B to B)/ consumers in the country (B to C) to be subjected to a service tax as well as a withholding tax deduction by the users of the services or impose income tax on foreign online suppliers via a levy (as done in India) or to introduce a virtual permanent establishment (PE) concept.
- Capital gains tax – consider introducing this under the Income Tax Act and impose it first on corporations and then individuals. The tax rate could be a low flat rate which can later be amended over time to blend in with the corporate tax rate. This means that the real property gains tax will be blended in with the income tax.
- Inheritance tax/wealth tax – could be considered with a threshold of RM10 million and the tax rate could be 5%.
- Increase the stamp duty rate on real property valued more than RM5 million.

- Consider removing existing tax exemptions on specific entities and imposing a new income tax on passive income such as interest on bank deposits, etc (previously there was a 5% withholding tax by banks on interest on fixed deposits).
- Review exemptions on charities to ensure effective governance and record-keeping and consider implementing a new flat income tax rate, such as 5%, on annual surpluses to inculcate compliance. Alternatively, consider continuing with the exemption of income tax but set up a Commissioner of Charities which will serve as a regulatory body for all charitable organisations and which will assist in inculcating proper/effective record keeping among such organisations.
- Sales Tax and Service Tax – widen the list of services that are subject to tax over the next few years with appropriate exclusions for goods/services passing through multiple production chains.
- Import/ excise duty legislation – recalibrate the concept of designated areas /special areas & exemptions.
- Consider removing the de minimis exemption of import duty on small imported parcels.
- Impose levies, and duties, to protect the environment/meet other social/ economic objectives related to health, climate change, etc.
- Impose travel tax/departure levy based on ability-to-pay (as announced in the 2019 Budget).
- Ultimately, consider a Sales Tax or Service Tax based on the value-added concept just like GST/VAT so as to avoid the cascading effect which can lead to unnecessary price increases.

# 7. Tax Compliance

We also need to focus on making tax compliance a way of life and a national duty. Continuous education cannot be limited to media advertisements by the tax agencies. Some suggestions include the following:

1. We need to have a tax file number allocated to all persons, irrespective of the tax status of a person.
2. We need to widen the scope of withholding taxes to cover all payments among residents and exempting such withholding only if a tax file number is disclosed to the payer.
3. We need knowledge and access to information, through well-developed information sharing mechanisms.
4. Focus on the educational approach, so as to be able to disseminate tax information including creating and publicizing a website effectively, which includes listing all tax case law decisions, etc. as the public needs to become aware of them in the self-assessment world.
5. Collect what tax revenue is due and penalize intentional non-compliance quickly. Attempt to avoid arrears and avoid chasing for collection of tax liabilities years after these have been established.
6. Carry out tax audits and tax investigations in a professional manner. The IRB and the Customs Department officers must not look at a tax revenue target as a starting point.
7. Introduce an effective human resource policy so that technical capabilities are enhanced i.e. get the right personnel. Outsource certain aspects, for example the research into a highly technical area which may be the subject of an advanced ruling so that there is an effective understanding of the specific issue and its place within the industry.
8. Train officers of the tax authorities by getting contributions from even the private sector so that we develop staff with a broader mindset and greater business knowledge.

9. Utilize technology effectively to provide services to taxpayers, to assist staff to respond on a timely basis and to collect taxes quickly. We must use technology in a holistic manner and not in a piecemeal manner so that systems are integrated effectively.
10. Enhance and protect taxpayers' rights by improving and monitoring the Taxpayer's/ Client Charter, which must exist in all tax agencies. Perhaps, the Auditor-General's Office should monitor the effectiveness of the Charter.
11. To assist in making compliance easier, there should be a general convergence between accounting profits and taxable profits.

With an enhanced image of the IRB and the Customs Department being fair and responsible agencies, which are professional in their outlook and service delivery, the compliance levels should increase and that will enable a revision in the income tax rates. With a growing tax base, the Government should look at committing itself to a phased reduction in income tax rates to continue to enhance Malaysia's attractiveness as an investment destination and to encourage citizens to work hard.



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## 8. Small & Medium Enterprises (SMEs)

There is currently a mismatch between the tax definition for SMEs and that adopted by SME Corporation Malaysia. The former is based on the paid-up capital of the company while the latter is based on sales turnover or employee headcount. The paid-up capital of a company may not be accurately used to measure whether it is an SME. Thus, the tax definition should be aligned with that of the one adopted by the SME Corporation, allowing more SMEs to enjoy the existing reduced corporate tax rate for a SME.

A bolder move would be to prescribe a simpler set of tax rules for SMEs, which would reduce their compliance costs and administrative requirements. Another consideration is for SMEs, below a certain threshold to be taxed based on a fixed prescribed amount or a percentage of sales generated (also known as a presumptive tax). A simpler tax system would not only help accelerate the growth

# 9. Discretionary Powers

There are currently two legal provisions that empower the Finance Minister to exempt any person from paying a tax. One is by way of statutory order, which must be laid before Parliament for approval, while the other is merely an approval letter from the finance minister. In the case of the latter, there has been a suggestion to repeal this discretionary power granted to the Finance Minister on the grounds of transparency.

This suggestion certainly has some merit if we look at past media reports that have exposed the various sweetheart tax deals granted by certain European countries to reputable multinational companies in order to attract their investments. However, the potential time and uncertainty involved in going through Parliament should not be discounted as this does not bode well for companies, from a commercial perspective. Instead, more checks and balances should be incorporated into the process. A way of doing this is for all tax exemption applications to be evaluated and approved by one body, such as the National Committee on Industry (NCI), comprising representatives from various regulatory agencies, including the Ministry of Finance and the Inland Revenue Board. This would be consistent with the NCI's current role of approving tax incentive applications received by the Malaysian Investment Development Authority (MIDA).

# 10. Single Agency for Tax Incentives

It is proposed to have a single investment promotional agency to approve investments, perks and benefits for both local and foreign investors alike.

Currently, there are too many government agencies overseeing tax incentives in specific economic areas. For example, the Iskandar Regional Development Authority is tasked to oversee tax incentives offered in Iskandar Malaysia, Malaysia Digital Economy Corporation for companies in the information technology industry/ shared services centre sector, Halal Development Corporation for halal investments and so on.

It is proposed that the management of tax incentives in Malaysia be cohesively placed under the umbrella of MIDA, which would lead and administer the tax incentive framework in Malaysia.

Sub-agencies that specialize in specific sectors can be formed under MIDA and these sub-agencies can form part of the committee evaluating and approving tax incentive applications. This gives MIDA a holistic view of our tax incentives regime and enables MIDA to formulate effective policies for the country, as a whole. From the investors' perspective, having a one go-to Government agency avoids confusion and simplifies the compliance process.

# Tax Administration

One of the key thrusts of the Government has been to strengthen the nation's institutional and implementation capacity. The Government has stated its commitment to improve the efficiency and effectiveness of the public sector service delivery system, so as to provide quality service and create an enabling environment for business. It has, over the years, taken various steps to create an enabling environment for business as well as to improve service delivery. Although these initiatives have yielded commendable results in some aspects, the Government needs to step up its effort to further improve the public service delivery system, in order to enhance Malaysia's competitiveness and attractiveness to investors. The tax system is one such area to do this, and a key enabler to energizing investment activity.

An efficient tax system requires an effective tax administration structure. A well-designed tax which is poorly administered can become an instrument of injustice. In view of the importance of taxation to the funding of an economy, substantive reforms in tax administration have been undertaken in many countries. One such reform measure was the introduction of self-assessment, which places the burden of determining tax liability on the shoulders of taxpayers with the tax authority/agency carrying out random tax audits to verify the accuracy of what had been declared in the tax return form.

An income tax system is based on the willingness of citizens/persons to pay their taxes voluntarily. This requires the tax agency to adopt a philosophy of having outreach and educational programmes to promote voluntary compliance.





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The study of taxpayer compliance is an important aspect of this approach. One needs to understand the psychology of taxpayers i.e. appreciating why persons comply or fail to comply with tax laws is important. This is essential so that steps can be taken to try to reduce non-compliant behaviour amongst the populace. With self-assessment, the monitoring of compliance levels and, therefore, research into compliance should be increased. It is also important to understand the behaviour of different groups of taxpayers (based on income level, occupational groupings, ethnicity, etc) so that remedial steps and new strategies can be devised to try to overcome negative perceptions within these groups.

Studies on taxpayer behaviour do seem to suggest that services to taxpayers that facilitate the reporting, filing and paying of taxes, or that impart education or information among citizens about their obligations under the tax laws, may in many circumstances constitute a more cost-effective method of securing compliance than measures designed to counter non-compliance. This would involve providing certainty and clarifying legal ambiguities, communicating clearly, and assisting in lowering the costs of compliance to taxpayers. There is much to be gained from viewing taxpayers more as clients than would-be defaulters.

Compliance management is not simply about audits, verification and enforcement. It is also about making it as easy as possible for people to comply. A significant part of the IRB's and the Customs Department's budget should be directed at the provision of advice and assistance involving marketing and education programmes, advisory visits for new businesses, as well as seminars and responding to telephone and written enquiries.

An effective tax administration system requires establishing an environment in which citizens are induced to comply with tax laws voluntarily, while efficient tax administration requires that this task be performed at a minimal cost to the community.

An important element in the reformation of any successful administrative is simplicity. It is important to simplify procedures for taxpayers. For example, by eliminating demands for superfluous information in tax returns. Tax administration requires facilitating compliance, monitoring compliance and dealing with non-compliance. Facilitating compliance involves improving services to taxpayers by providing clear instructions, understandable forms, and assistance and information as necessary. Timeliness is crucial.

In order to continue to collect more tax revenue (which will be essential in assisting future moves to attain a balanced or a surplus budget), the need for effective enforcement implementation by the tax agencies (both the Inland Revenue Board (IRB) and Customs Department) is an important component. It is time the tax agencies are transformed into truly service-oriented entities which use information technology effectively and efficiently. Existing systems and procedures need to be redesigned and streamlined with the latest technology. There will be a need for the Government to budget for such an expenditure. We must attempt to move along this path, but it requires a holistic approach, that means that the whole agency must be wired, trained, and have a service-oriented mindset. A proper and systematic approach towards implementing technology and efficient and well-trained staff will

lead to a more effective tax agency. This will lead to the registration of more taxpayers, effective actions to recovery and thus greater tax revenue.

Additionally, there is a need for the tax authorities to be more forthcoming with the issuance of clear guidelines, on a timely basis, to ensure transparency within the tax system. Speedier and more efficient processing of tax returns and of refunds of overpaid taxes would promote greater public confidence in the system. Hence, a holistic technological transformation is absolutely essential. With the transformation, it is hoped that the tax authorities will be more proactive/responsive in issuing timely clarifications on relevant areas which will assist taxpayers in making their financial decisions.

There should be more effective use of the website of the IRB and Customs and more information should be displayed on a timely basis. Drafts of intended public rulings could be exposed to the public for a period of time so that the public has the occasion to provide feedback which can then be considered before the public ruling is finalized.

Clarity and the consistent application of the law is essential, so that businesses are not hindered. The tax system must be business-friendly rather than a bureaucratic system. To be fair, the tax agency has made some advances in terms of improving efficiency but more needs to be done.

All in all, the future trend will be the increasing reliance on tax revenue being generated by the tax authorities through effective implementation and enforcement strategies. This initiative requires capital expenditure to spur the transformation of the relevant agencies. Implemented properly, such expenditure should result in improved tax revenue collection. It must not be forgotten that technology is needed not only to collect taxes but also to educate and assist taxpayers and tax agents in meeting their obligations – a holistic solution for the benefit of all.



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## 12. Conclusion

It is timely that Malaysia announces a comprehensive fiscal reform which is widespread and wide-ranging, which puts into place a long-term plan to mould a world class tax system that will be comparable to systems used in the leading developed nations in the world. It is time to let go of the 'ad-hoc' approach of tinkering with the tax system.

The recommendations in this paper would need more detailed study/simulation and must also be introduced on a staggered basis over the next few years in line with the evolution of the economic growth and the financial management of the country.



The Center for Market Education (CME) is a boutique think-tank based in Kuala Lumpur, Malaysia.

As an academic and educational institution, CME aims to promote a more pluralistic and multidisciplinary approach to economics and to spread the knowledge of a sounder economics, grounded in the understanding of market forces.

In order to do so, CME is not only involved in academic initiatives, but it organizes seminars, webinars and tailor-made economics classes for students, journalists, business people and professionals who wish to better understand the relevance of economics for their daily lives and activities.

Economics matters and needs to be presented in a fashion in which the link with reality is clearly visible. In this sense, we look not only at theoretical economics but also at policy making, with an emphasis on the unintended consequences generated by political actions.



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