Implementing electronic tax filing and payments in Malaysia

Taxation is essential for sustainable economic development, and tax administration is a basic function of a successful state. Taxation also helps make a government accountable to its citizens. When governments spend taxpayers’ money, they are more accountable to make budget decisions transparent and accessible.

By 2012, 76 of the economies measured by Doing Business had implemented electronic tax filing (e-filing) and electronic payment (e-payment) systems.

By 2012, 76 of the economies measured by Doing Business had implemented electronic tax filing and payment systems. This case study examines Malaysia’s experience with modernizing manual tax filing and payment and moving to a paperless online system. Malaysia shows the opportunities that technology can provide to taxpayers and governments—as well as the challenges that may emerge during the transition.

In 2004 Malaysia’s Inland Revenue Board (IRB) launched e-filing and e-payment for income taxes. IRB encountered several implementation challenges, key among them the public’s initial reluctance to use the new system. So IRB increased its promotion efforts, upgraded the system and hired staff to show taxpayers how to use it.

The number of individuals and companies using e-filing jumped from 5% of active taxpayers in 2006 to 37% in 2012.

The time that businesses need to comply with Malaysia’s tax regulations fell from 190 hours in 2004 to 133 in 2012 as measured by Doing Business.

Tax systems in developing economies, like those in more developed ones, face both new challenges and new possibilities as a result of technological change. Malaysia’s ongoing reform of its electronic tax filing and payment system shows how and under what conditions technology can benefit both tax authorities and taxpayers.

E-filing systems increase the quality and quantity of information available to tax officers, enabling them to complete transactions faster and more accurately. Returns filed electronically have much lower error rates than paper returns and substantially cut the need to impose penalties and other punitive measures to foster compliance. The more efficient handling provided by electronic returns allows tax officers to issue assessments and refunds more quickly, and taxpayers know right away if their returns have been accepted by the tax authorities.

E-filing lowers the cost of handling returns—allowing administrative resources to be reallocated to other tasks such as auditing, customer services and tracking non-compliance.

The benefits of e-filing and e-payment systems extend to other electronic processes in the tax authority. E-filing and e-payment allow for better, safer data storage that can be used to implement a risk management system for auditing and enforcement. Automation helps establish a good system for tracking case files, which is essential for effective auditing.
and increases the speed and quality of data provided to auditors. In addition, e-filing systems are usually complemented by software that standardizes and facilitates processes for taxpayers, making compliance easier.

Finally, well-designed electronic systems can lower corruption by reducing face-to-face interactions. To ensure that taxes are collected efficiently and reduce opportunities for corruption, a generally accepted principle is that tax authorities should not handle money directly. Ideally, tax officials should have little direct contact with taxpayers and so less discretion in deciding how to treat them.

E-filing is also easy, flexible and convenient for taxpayers. E-filing makes it possible to file returns from a taxpayer’s home, library, financial institution, workplace, tax professional’s business or even stores and shopping malls. With an integrated e-filing and e-payment system, taxes can be filed and paid online from any place.

GLOBAL EXPERIENCES WITH AND LESSONS FROM ELECTRONIC FILING

Singapore was one of the first economies to adopt electronic systems in its public administration. In 1992 the Inland Revenue Department was replaced by the Inland Revenue Authority of Singapore, which developed an integrated, computerized tax administration system.

The authority’s first step was shifting from a hard-copy filing system to paperless imaging. Going electronic made administrative processes more efficient by freeing staff from unproductive paper shuffling, enabling better taxpayer service. The time needed to issue assessments dropped from 12–18 months to 3–5 between 1992 and 2000. This change allowed staff to work more on auditing and investigation. Automated standard taxation procedures also made the system less dependent on the subjective expertise of individual tax officers, reducing the potential for corruption. Return processing, auditing and payment functions were separated, and officials’ attitudes toward taxpayers improved.

Chile’s Internal Revenue Service was the country’s first public agency to adopt online technology—well before most other public services. Electronic methods were intended to facilitate tax compliance and decrease direct interaction with taxpayers. Chile is one of the few economies that have managed to approach nearly 100% use of electronic systems. Online tax returns were submitted for the first time in 1998.

Chile faced several barriers at the outset of e-filing. Taxpayers had limited Internet access, and tax preparers were reluctant to use the new system because they were unfamiliar with the technology and saw it as a threat to their profession. In addition, the revenue service’s information technology system could not handle the huge congestion of tax returns, especially in the few days just before the deadline. So Chile continuously upgraded its electronic system and offered prefilled electronic forms to simplify the process for taxpayers. The tax authority also introduced ambitious initiatives to overcome connectivity shortages by creating a public-private network of more than 880 e-filing centers, providing more than 30,000 connectivity points. In addition, it made arrangements with internet cafes so that taxpayers could use their equipment for free and trained operators at access points. It even developed a mobile training and awareness unit that traveled to different parts of the country to help people file taxes online.

The use of technology to foster tax compliance by the United States Internal Revenue Service (IRS) shows that more developed economies also face challenges in increasing the use of e-filing. The IRS introduced e-filing of federal tax returns in 1986. Though this system predated Singapore’s, it was initially less comprehensive. In fact, even though the number of electronic returns filed increased over time, the potential savings from that increase were partly offset by the ongoing use of paper filings for complex returns. But by 2012 the IRS achieved 80% e-filing of major returns.

Initially, e-filing was not entirely paperless. Until 1999 electronic filers still had to submit signed paper documents. The IRS realized that when taxpayers switched to e-filing, the time savings partly offset the costs of processing the still-large volume of signed paper documents. In 1999 the IRS introduced an electronic option to replace signed paper documents. In addition to lowering processing costs, e-filing has cut the time required to get refunds—making more taxpayers willing to file returns electronically.

MALAYSIA’S EXPERIENCE

Seeking the benefits of electronic tax systems and reflecting the government’s vision of leveraging online technology, Malaysia’s Inland Revenue Board (IRB) launched its electronic system for taxes in 2004. IRB aimed to increase revenue collection by improving taxpayer services. The goal was to cut time and cost and to allow taxpayers to comply with tax obligations more easily, enabling IRB to maintain a good reputation with taxpayers even as it widened its tax base.

With the new system, taxpayers can complete forms and provide needed payment details online instead of sending them by mail or taking them to a tax office. The online system was developed by IRB’s information technology department. IRB implemented a roaming public key infrastructure system that gives users secure access to sensitive information from any location without having to carry digital identification. The electronic system integrated tax filing and payment on one server—a major advantage over manual procedures.

For every tax filing or payment, taxpayers have to log in, select and complete the appropriate forms, sign and submit them digitally. An acknowledgment is received immediately. The e-filing system automatically calculates the necessary payment details. It also limits deductions that taxpayers are entitled to based on deduction rules—enabling taxpayers to avoid mistakes that would result in penalties.

In addition, prefilled online tax returns have been available since 2006, starting with taxpayers basic information and later extended to include their incomes and reliefs. In 2012 IRB enhanced its e-filing system by introducing smartphone filing.
for individual taxpayers. That same year, it introduced organizational e-filing for company managing directors to enable companies to use their digital certificates to file returns electronically. Previously, directors had to use their personal certificates.

In addition, IRB introduced automatic refunds. Due to the big number of refund cases and to expedite refunds, refunds were directly credited to taxpayers’ accounts through electronic fund transfers—reducing the number of unclaimed checks.

**IMPLEMENTATION CHALLENGES**

IRB encountered several challenges implementing e-filing and e-payment, key among them is the public’s readiness to use it. When the system was introduced in 2004, both Malaysian and non-Malaysian citizens could choose to file their tax returns manually or electronically. The private sector was not involved in the development of the project. Its feedback was sought later.

Two years into the project, few Malaysians were using e-filing. Though taxpayers and tax preparers recognized its benefits, the number of taxpayers using the e-filing system remained far below expectations, with individuals and firms using e-filing accounting for just 5% of the taxpayer population in 2006. There may be many reasons for this initial lack of enthusiasm. When tax systems change, taxpayers and tax authorities take time and incur costs adapting to and adopting them.

The low use of the electronic system was mainly due to the initial reluctance of Malaysian taxpayers to abandon paper-based processes. Studies were conducted to analyze taxpayers’ intentions to file electronically and their willingness to do so. Uncertainty about the security and privacy of information transmitted online was one of the reasons for low use of e-filing. The new system also created anxiety for users uncomfortable with the technology. Returns had to be completed online; users could not complete soft copies of their returns offline and upload them to IRB.

**A CHANGE IN STRATEGY**

Because of the low initial participation in the electronic system, in 2008 IRB expanded its promotion efforts, sponsoring seminars, talks and television advertisements and distributing flyers and pamphlets. IRB also set up booths at conventions and held roadshows to promote the electronic system and raise public awareness, using the slogan “as easy as 1, 2, 3.” IRB also realized the importance of involving the private sector and asked professional bodies such as tax preparers and accountants to share ideas on how to enhance the online system. IRB also gathered feedback from taxpayers through its customer care centers and branches.

At first some taxpayers and tax preparers reported that the server was slow and often failed. Authorities responded with several upgrades to make it accessible with different browsers. IRB also installed computers in its offices so that taxpayers could file electronically, and hired workers to train taxpayers on how to use the system. And it launched a program to help taxpayers during the peak filing season. Special counters with extended operating hours at all branches were made available for the public to submit their returns through e-filing.

A tax authority gains the most benefits from e-filing when it achieves 100% use of the online system for filing and paying taxes. Accordingly, IRB provided incentives and services to encourage e-filing. For example, IRB offers a grace period of 15 days from its official deadline if returns are filed electronically. In addition, if a tax return is submitted late, the IRB penalty is 5% less if the return was submitted electronically. The charter for IRB clients was redrawn to include a pledge to refund any excess taxes within 30 working days from the date of receipt if the returns were filed electronically.

IRB continues to encourage taxpayers to file online. Among its latest initiatives, it is offering to do presentations at companies with at least 200 employees who use the service. The use of the online system has picked up dramatically: by 2012, 37% of active taxpayers filed electronically.

**POSITIVE OUTCOMES**

Malaysia’s efforts are showing results. Between 2006 and 2011 the share of individuals and companies filing electronically increased from 5% to 34% (figure 7.1). Over the same period, tax collections increased from 14.5% of GDP to 15.3%. Further analysis would be needed to fully understand the link between e-filing and revenues.

IRB’s ongoing efforts to improve its electronic tax system have lowered the administrative burden of complying with corporate tax obligations as measured by Doing Business. In 2006 it took 24 fewer
CONCLUSION

Electronic systems for filing and paying taxes, if implemented well and used by most taxpayers, benefit both tax authorities and taxpayers. Malaysia’s experience has shown the opportunities that technology can provide as well as the challenges that may emerge as the users are phasing in the change over time.

FIGURE 7.2  Malaysia’s electronic filing system has eased compliance with tax obligations for businesses

Source: Doing Business database.

hours to file taxes than in 2005 (figure 7.2). By 2007 far more small and medium-size companies were filing electronically, further reducing time to comply with corporate income and labor taxes obligations from 166 hours in 2006 to 145 in 2007. In 2010 tax preparers deployed new software linked to IRB’s e-filing system. In addition, IRB improved its e-filing system and introduced online filing of tax estimates. These improvements cut compliance time to 133 hours a year.

NOTES

This case study was written by Joanna Nasr.
12. Malaysia Inland Revenue Board data.
13. IRB data. This is the percentage of taxpayers who used e-filing but did not necessarily pay taxes electronically.
15. Malaysia Inland Revenue Board website.
For corporate taxpayers, the due date is 7 months from the closing of account. If a company’s accounting period ends with the calendar year (which is usually the case), the deadline for manual submission is the end of July, with an additional 15 days if filings are submitted electronically.
16. Malaysia Inland Revenue Board data.
17. World Bank, World Development Indicators database.