

Assessing The Challenges Of Digitalizing Tax Administration In Malaysia: A Conceptual Analysis

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Abstract—This paper explores the challenges and implications of digitalization in taxation, focusing on the case of Malaysia. This article applies a systematic approach to literature review which examines how digital transformation has impacted tax administration, from the introduction of e-filing and online payments to the broader shifts in policy design and implementation. Despite the potential benefits such as increased efficiency and revenue collection, Malaysia faces several hurdles in fully embracing digitalization. These include issues with communication, tax agent acceptance, the transformation of tax administration itself, tax system awareness and education, and the evolving landscape for businesses and society. The paper emphasizes the need for strategic planning, capacity building, stakeholder involvement, and effective change management to successfully navigate the digitalization of tax administration. Overall, it underscores the importance of addressing these challenges to fully realize the potential of digitalization in enhancing tax compliance and government revenue. Malaysia must prioritize strategy, stakeholder engagement, capacity building, and robust change management to achieve success in digital tax administration.

Keywords: Digitalization; Tax Administration and Challenges

1. INTRODUCTION

Today, as digitalization is embedded in almost everything that we do, taxation policy and tax administrative practice are being transformed to embrace digital transformation. This also means that in policy making, considerations need to be taken on how these changes will impact the implementation and execution of tax policies. (EY, 2022). Digitalization makes life easier for authorities by easing the administrative burden. Digitalization of tax administration places emphasis on collecting data and determining tax liabilities, which will result in a more secure collection and control of tax revenues. Digitalization in taxation has brought changes to how tax policy is designed and administered worldwide thus leading to the need to update legislation to adopt technology in the system. According to Ihnatišinová (2021), digitalization of tax administration communication means the creation of paperless communication between the tax subject and the tax administration. Thus, digitalization benefits the taxpayers in reducing the compliance costs. This can create a virtuous cycle by providing governments with greater revenue to invest in further productivity-enhancing reforms. Brown the Global Head of Tax Technology & Innovation KPMG in the U.S. mention in his article that digitalization has been changing all aspects of taxation for some time – from tax collections and compliance down to the tax base itself.

In Malaysia, e-filing and online tax payments were introduced to allow efficient tax submissions and payments through mobile and web-based applications. The E-Filing system's implementation substantially enhances taxpayer compliance, with socialization taxation and internet comprehension serving as moderating factors (Arsita & Tripriyono, 2022). In 2004 Malaysia's Inland Revenue Board (IRB) spearheaded an initiative to implement a system for filing and paying taxes that would promote electronic, paperless transactions. E-filing in Malaysia benefits taxpayers, as it reduces paper usage, costs, and storage space (Nada & Choiriyah, 2022).

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. According to Ladewi et al (2022), taxpayer compliance and tax collection both influence tax revenue, as do the self-assessment system.

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. According to Yegon et al (2023), online tax registration, filing, and payment have a positive and significant effect on tax compliance among small and medium enterprises in Kericho County, Kenya. Online tax system implementation through digitization of tax administration has potential benefits but requires improvement in tax service infrastructure and socialization of tax digitalization for user sustainability (Asista & Setyowati, 2022).

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. 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. Most respondents stated that e-filing can be accepted as an online and real-time tax reporting system, and it is deemed useful to assist taxpayers in their tax reporting (Meiryani et al, 2022). During the year 2012, IRB enhanced its e-filing system by introducing smartphone filing for individual taxpayers and introduced digital certificates for company managing directors to file returns electronically. Information quality and system quality positively affect the use of e-filing systems, which in turn positively affects taxpayer compliance (Pramanita & Rasmini, 2020).

While there is no denying that these initiatives have made tax compliance easier for both taxpayers and the Inland Revenue Board (IRB), there are still a number of possible issues that could result from this digital transformation.

2. RESEARCH METHODS

2.1 Literature Review

Digitalisation has changed the way we navigate the economy with the transition to Industry 4.0. The increasing digitization of many industries, such as manufacturing, services, and commerce, has had an inevitable impact on tax policies and practices in Malaysia. Digital transformation of tax administration is crucial for ensuring fiscal stability, tax security, and a more transparent and fairer digital tax environment. As for example digitalization of the tax system in Ukraine requires utilizing modern information technologies to improve taxpayer-state financial control body interaction and enhance data integrity (Tsiutsiak et al, 2023). While, digitalization of small business tax administration is in development and requires additional efforts for distribution, with potential for a new experimental taxation regime based on occupational income tax and improved electronic document security (Boboshko, 2019).

In addition, according to Anisimova (2021), improving digital tax services in Russia requires developing design, quality monitoring, and incorporating behavioral economics tools, while involving taxpayers early in the development process. While, advanced digital technologies in tax administration have raised the level of tax administration and changed the approach of tax authorities to control and analytical work, benefiting both taxpayers and tax authorities (Mikhaleva & Vochozka, 2020).

As in Malaysia which implementing a digital tax effective January 1, 2020 to ensure both international and local businesses in the digital sector pay their fair share of tax (Kuek, 2020). Economic factors and user acceptance significantly influence user awareness in the implementation of digital service tax in Malaysia (Ismial et al, 2023). Meanwhile, the government and taxpayers should work together with tax agents to engage in digital transformation. (Saraju & Hamid, 2021).

Expanding electronic services, granting equal access to digital technologies, and advancing personnel training are strategies for effective tax administration in the face of challenges and threats (Medynska & Noginova, 2022). Challenges in digitalizing tax administration include determining the place of taxation, increasing the number of transactions using cryptocurrencies and blockchain technologies, and ensuring reliable protection of personal data and security of electronic payments (Ivanovska, 2023). In the same time, digital transformation of tax administration involves integrating digital infrastructure, taxation processes, information interaction, and incorporating technologies like Blockchain, smart contracts, Big Data, AI, and IoT (Nazarov et al, 2022). Key challenges of digitalization of the tax system include ensuring flexibility, continuous improvement, and addressing aspects like universality, accessibility, compatibility, data security, and reliability (Tsiutsiak, 2023).

2.2 Methodology

This is a conceptual paper based on qualified research that attempts to define and provide clarity about the complexity of digitalizing tax administration in Malaysia. A systematic literature review is a great way to get to know some background information about the digitization of tax administration. A systematic literature review provides a comprehensive overview of literature related to a theme, theory, or method, synthesizing prior studies to strengthen the foundation of knowledge. (Paul & Criado, 2020). The review has included the examination of academic sources (articles/reviews, reports and policy documents) published in an English language that was available on databases as Google Scholar, JSTOR, Scopus. Studies were the focused on the challenges of digital tax administration

3. RESULTS AND DISCUSSION

The implementation of e-filing and e-payment systems by the Inland Revenue Board (IRB) in Malaysia encountered several challenges, despite efforts to transition taxpayers to digital platforms. Upon its introduction in 2004, both Malaysian and non-Malaysian citizens were provided with the option to file their tax returns manually or electronically. However, two years into the initiative, there was a notable lack of uptake among Malaysian taxpayers, with only a small percentage opting for e-filing. Despite recognition of the benefits of electronic tax filing by both taxpayers and tax preparers, the utilization of the e-filing system remained significantly below expectations, with e-filing users comprising merely 5% of the taxpayer population by 2006 (Tantra et al., 2023).

Similarly, experiences in other jurisdictions, such as South Africa, underscore the challenges associated with low adoption rates of e-filing systems. In South Africa, taxpayers continued to favor manual submissions despite the availability of e-filing options, indicating a discrepancy between the anticipated benefits of digitalization and actual user behavior (Mashabela et al., 2020).

Various factors contribute to the challenges encountered in the digitalization of tax administration both nationwide and specifically in Malaysia. These include, but are not limited to, issues related to information technology readiness, ease of use, perceived benefits, user satisfaction, as well as concerns regarding security and privacy. Understanding and addressing these multifaceted challenges are imperative for fostering greater acceptance and utilization of digital tax administration platforms in Malaysia and beyond.

3.1 Digitalization of Tax Administration Communication under the Effect of Global Megatrends of the Digital Age

An article written by Ihnatišinová (2021), summarized that, the transformation to new digital technologies in communication in the tax administration is investing in modern technologies and the development of digital skills of tax administration employees in one of the challenges. Society must adapt to the changes associated with digitalization; it must have the right skills to keep up with the global trends of the digital age. Great and rapid development is taking place in the field of digital technologies and innovation. As in Malaysia itself, the regulators must fill the technology gap in order to make the tax administrations digitalization is at the success. To make it success, the government should overcome the followings issues:

1. Internet openness and innovation - addressing the economic and social benefits of internet openness and policies that support its development.
2. Work and skills in the digital economy - to benefit from new, constantly evolving labour markets and new jobs in the digital age, increasing the qualifications and digital skills of the workforce. Greater use of digital technologies increases the demand for new skills.
3. Global connectivity - reaping the economic and social benefits of the development of the Internet of Things and providing the framework for tomorrow's Internet of Things. There are many opportunities to improve networks and services through the convergence of different communication technologies.
4. Confidence in the digital economy - enabling greater cooperation to protect consumers and manage their privacy and security risks. Consumer confidence is a key element in supporting the growth of the digital economy. The risk of digital security and privacy needs to be managed for economic and social prosperity.

3.2 Tax Agents' Acceptance of the Digitalisation of Tax Administration in Malaysia

Saruju and Hamid (2021) discuss the digitalisation has changed the way people navigate the economy with the transition to Industry 4.0. The government and taxpayers should work together with tax agents to engage in digital transformation. Tax agents' readiness to embrace digitalisation of tax administration in Malaysia is influenced by factors such as government incentives, tax compliance, and tax collection (Saruju & Hamid, 2021). According to Vuković (2018), digitalisation represents both challenges and opportunities for tax administration, which go beyond the simple changing of a communication channel with tax administrators or the transformation of existing services from paper to digital. To tax agents, technology intervention will have an impact on their roles in the taxation system. Hence, tax authority readiness for digitalization depends on improvements in implementing regulations and human resources competency about the digital economy (Firmansah & Rahayu, 2020).

Plainly, digital technology will ensure tax returns are pre-populated by automatically exporting data from accounting software. The tax agent's readiness to accept of the digitalisation in tax administration is a challenge. The tax agents must familiarise themselves with the new technology used in the taxation system. The consideration of tax agents' readiness is important when delivering the best services to their clients. Digitalisation can enhance their workflow and may contribute to assisting and supporting their clients' tax compliance. According to Diller et al (2020) tax consultants scoring high on extraversion and openness to experience and low on neuroticism exhibit a higher level of digitization.

3.3 Towards the Digitalization of Tax Administration

The next challenges as concluded by Vuković (2018), is the digital transformation of tax administration itself is one of the biggest challenges in the tax profession. There is no ready recipe for the digitization of tax administration and for Malaysia. There are only experiences that are often not fully applicable in each country. Digitalization of tax administration entails five elements: technologies, people, managing of tax risks, financial resources, and communication. Although technology seems to be a primary element, one should not ignore the fact that the human factor is very significant in the digitized administration. Digitalization of tax administration is possible in several ways for example through educating tax officials, recruitment, determination of their regular or special status (tax technologist) and, ultimately, performance measurement and the compensation and reward system. Digital tools can enhance tax administration processes, reducing arrears, increasing tax payment collection, and increasing state budget revenue (Ripol & Gomeleva, 2021).

3.4 Tax System Awareness and education in Malaysia

A Study on Self-Assessment Tax System Awareness in Malaysia by Fatt and Kin 2011 indicate that in the era of Self-Assessment System (SAS), it is imperative for all individuals (taxpayers and future taxpayers) to be formally exposed to tax education, so as to enable them to understand the mechanism of SAS and to equip them with some

basic tax knowledge. On 1 January 2005, in order to promote voluntary tax compliance, the IRB has implemented the self-assessment tax system (the SAS) on individual taxpayers. Under the SAS, individual who has income accruing in or derived from Malaysia are required to disclose taxable income honestly, compute tax payable correctly, file tax return form and pay tax on a timely manner. As SAS is going digital, not every single people who entitle to pay for the taxes understand how to use the system and included the petty traders. It was reported that since the implementation of SAS, the Malaysian tax defaulters has increased by almost 10 times within two years' time, from 25,160 in 2003 to 239,666 in 2005. This is situation giving the IRB such a challenges in collecting the revenues. Veerinderjeet and Renuka (2002) and Chow (2004) opined that the implementation of SAS in Malaysia poses enormous challenges on individual taxpayers. Fundamentally, the success of the SAS relies heavily on the full cooperation of taxpayers. To be tax compliant, taxpayers need to be tax literate. However, in the Malaysian education system, only accounting and some business management students are exposed to taxation at tertiary levels. Many young Malaysians (the future taxpayers) are not formally exposed to taxation in schools. More than 90% of Malaysians believe early and formal tax education in secondary schools will improve their understanding of the taxation system and their responsibility towards taxes (Othman et al, 2020). Introducing tax education at tertiary level institutions can improve tax compliance in Malaysia by increasing citizen tax knowledge (Amin et al, 2022). One of the surveys also found that, ordinary people for example the hawkers surveyed did not have a good knowledge about the mechanism of SAS, and they were apprehensive of tax audit. The plausible explanation was due to lack of formal tax education in primary, secondary and tertiary levels in Malaysia (Choong et al, 2009). What make it worst is the Malaysian tax laws are inherently voluminous and complex; and the constant changes make it difficult even for tax officers, tax academics, tax practitioners to keep abreast of the latest development, let alone the ordinary people.

4. CONCLUSION

Digitalization has significantly altered the landscape of taxation worldwide, necessitating updates to legislation to accommodate technological advancements. Despite Malaysia's progress in adopting digitalization in tax administration, the nation remains in a sustainable phase, facing numerous challenges that threaten the longevity of these initiatives. Policymakers must recognize both the opportunities and challenges posed by technology and devise strategies to ensure the successful implementation of digital tax administration. A crucial step toward achieving digitalization success is the formulation of a technology strategy and roadmap by policymakers. This involves assessing the current technology landscape and devising a plan for the next 2-5 years to guide resource allocation toward strategic initiatives. Additionally, tax authorities must proactively build capacity to support future digitalized operations, including the recruitment of data scientists to analyze tax data effectively. Stakeholder involvement is paramount in digitalization initiatives; early engagement is necessary to garner support and understanding. By involving stakeholders from the outset, tax authorities can incorporate their perspectives and requirements, facilitating smoother implementation and user acceptance. Furthermore, effective change management is essential, as transformation initiatives impact a wide range of taxpayers. Internal change management processes and public support are vital components of successful digitalization efforts. However, while this discussion provides valuable insights, it also has notable limitations. First, it tends to be nationally oriented and does not consider the varying levels of digitalization across regions or sectors. This gap may obscure the specific challenges faced by smaller businesses and rural areas, potentially hindering the success of digital tax initiatives. Understanding these local-level challenges is crucial for creating a holistic and inclusive strategy that can respond more effectively to diverse needs. Secondly, there is a lack of empirical evidence or case studies to support the theoretical frameworks presented in the literature, which raises questions about their practical relevance. Although the theoretical approach is useful for illustrating strategies under ideal conditions, without data on real-world implementation, we cannot fully grasp how these initiatives function. To substantiate insights and bolster recommendations, empirical evidence is essential. Therefore, future research should focus on conducting in-depth exploratory case studies across different regions or sectors within Malaysia. Such analyses would provide a detailed understanding of the unique opportunities and limitations encountered in digitalizing tax administration, leading to more targeted and effective strategies. Additionally, research should seek to capture the perspectives of various stakeholders involved in digital tax administration efforts. Understanding how taxpayers, tax authorities, and technology providers experience the transition will help identify potential obstacles and facilitators, which can be addressed through improved change management strategies. This approach will yield a more comprehensive picture of the digital transformation within Malaysia's tax system. In summary, achieving success in the digitalization of tax administration requires careful planning, capacity building, stakeholder involvement, and effective change management. By adopting a strategic approach and addressing these key factors, policy makers can navigate the challenges of digital transformation and reap the benefits of a modernized tax system.

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