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# As the dust settles, what's in store for SMEs & others?

by
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**Entrepreneurship from the ground up, to SMEs and beyond, are being promoted under Budget 2019**

Malaysians were given a hint of the austere days ahead when Budget 2019 was announced. Finance Minister Lim Guan Eng revealed that the state of Malaysia's financial affairs and the call to improve the Rakyat's wellbeing would set a new path for public spending to restore the economy as an Asian Tiger.

I see positive steps in some of the key changes announced, which impact SMEs and individuals.

But to ensure long-term impact, I believe a root-and-branch reform framework is needed, one that incorporates measures that enhance operational efficiency in tax administration, curbs leakages and accounts for unreported income in the underground economy, while aiming for income tax cuts to spur economic growth.

The government recognises this, having established the Tax Reform Committee to perform a holistic review of Malaysia's tax system.

### What's to come

The measures announced in Budget 2019 and the Tax Reform Committee's ongoing comprehensive study of a new tax framework address the call for new revenue sources while promoting fiscal discipline. So what are these new revenue sources and what else can we expect?

There are three key areas currently on the Tax Reform Committee's radar.

### 1. Stepping up tax compliance

The return of the tax amnesty programme (the Special Voluntary Disclosure Programme) is an encouraging move by the tax authorities. Those who voluntarily declare any unreported income from Nov 3, 2018 to June 30, 2019, including in offshore accounts, would face fines of 10% or 15% (depending on when their disclosures are made).

Those who are in the midst of a tax audit or Inland Revenue Board (IRB) investigation will also qualify for these reduced penalty rates. The reduction in penalty rates and possible immunity from legal action will encourage tax evaders to come forward more willingly.

Meanwhile, stricter penalties (80% to 300%) after the programme ends is perhaps the clearest indication that the authorities are increasing their focus on compliance and enforcement under a self-assessment environment.

These penalties can easily be avoided if taxpayers and employers alike are more diligent and vigilant in meeting their tax obligations.

But how exactly will the authorities track and uncover any instances of law-breaking in order to reduce the tax gap?

With the implementation of the Automatic Exchange of Information (AEOI) this year, the IRB can now audit and access "money trails." This includes financial information like financial transactions, assets and other tax-related information of both individuals and companies.

As such, individuals are advised to keep complete records of their income sources, particularly those from offshore investments or sources, so that all transactions can be identified.

Technology will enhance the effectiveness of this process, through social media monitoring and big data analytics, for instance.

The IRB will also use these measures to investigate unexplained extraordinary wealth (e.g. possession of luxury goods, jewellery, handbags or property) to recover such monies, whether in the form of additional taxes, penalties or fines.

### 2. Surfacing the underground economy

Another common form of tax leakage - the underground economy – is also being addressed. Earnings in the underground economy escape taxation, keeping tax revenues lower than they otherwise would be. And this includes unreported income from legal monetary, goods and services transactions.

Its pervasiveness has increased with the rise of contingent workers who hold multiple, often concurrent, contract jobs in this digital age. This includes freelance consultants and stay-at-home mums who perform data entry, research or translation work.

Contingent workers typically lack awareness of how much taxable income they must report. They are often confused over which expenses are deductible, resulting in huge year-end tax bills and possible penalties.

That's why I believe it's crucial for the authorities to expend more resources in educating taxpayers. With better awareness and understanding, taxpayers will no longer be able to fall back on the 'I-didn't-know' excuse.

If our tax base continues to be eroded and our tax compliance is poor, the government may respond by raising tax rates, encouraging a further flight into the underground economy that worsens budget constraints.

And we don't want that, do we? Think about it. A significant amount of income earned in the underground economy could be immediately spent in the official economy, stimulating growth.

A balance is needed to encourage the growth of the underground economy, while surfacing income earned into the country's taxation system.

In response to the changing landscape, the Tax Reform Committee is taking some positive steps to address individual income tax by considering different avenues for wealth creation.

The aim is to increase and protect the country's tax base in the longer term, minimising tax arbitrage opportunities and leakages.

### 3. Improving the efficiency of tax administration

Many countries have taken steps to transform taxpayer services, offering tailored digital self-services to make tax compliance feel less like a chore.

The IRB's challenge is to do this while continuing to improve tax administration efficiency by containing administration costs and simplifying the reporting and collection mechanism.

Any tax reform framework needs to move with the times, using more sophisticated online portals and mobile self-service channels.

I recommend a review to rationalise personal reliefs and simplify tax bands, so that tax filing may be simplified, reducing the burden of record keeping and auditing documentary evidence.

Malaysia still operates under extremely stringent filing timelines, and there are ongoing concerns that the new penalty regime would be seen as harsh after the tax amnesty period lapses.

To encourage compliance, a simplification of the tax system or perhaps even a waiver of the requirement to file for most individual taxpayers needs to be considered.

Articulating the benefits of self-service filing to taxpayers is also crucial. Various tools need to be made available, from personal tax calculators and effective tax guides to online assessments that enable users to test their eligibility for exemptions/concessions.

By automating various administrative functions, taxpayers and tax authorities would be more inclined to collaborate with each other. For example, businesses should be encouraged to demonstrate sound establishment of their internal control framework relating to payroll deduction and employees' income reporting to provide assurance to the IRB.

This will help taxpayers to be in control of their compliance, reducing the likelihood of full audit reviews.

### Where do we go from here?

Budget 2019 focuses on the Rakyat's wellbeing while promoting an entrepreneurial culture to restore Malaysia's status as an Asian Tiger. Any future introduction of new taxes comes with the assurance that the Tax Reform Committee is taking a holistic view in promoting a more efficient, neutral and progressive tax system.

Such a tax system should leverage on new technology and advocate expedient tax administration while enforcing compliance to minimise tax leakages.

Although the government is adopting a cautious outlook with its pledge to create a more progressive and effective taxation system, I believe that the possibility of future tax cuts and other tax breaks should not be discounted.

Striking a balance between pursuing sustainable economic growth while promoting fiscal discipline is key.

As a start, a medium-term timeline needs to be observed in cognisance of specific benchmarks already put in place by the government to pursue economic growth.

The journey may be tough, but as they say 'growth and comfort don't co-exist.' FocusM

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## How Budget 2019 helps SMEs and others

| BUDGET 2019 MEASURES | KEY OBSERVATIONS |
|---|---|
| Tax relief to encourage savings in children's higher education<br><br>Tax relief cap for EPF and life insurance contributions raised to supplement the working population's EPF contributions. | While it was a scaled down effort for tax reliefs, social welfare protection remains on Budget 2019's agenda |
| Reduction in tax rate for SMEs to foster growth in the entrepreneurial economy | Overall gains for SMEs despite an income tax rate freeze for individuals and corporations |
| Real Property Gains Tax (RPGT) rates raised for disposals from the sixth year onwards. Changes in stamp duty | The hike aimed at widening the revenue base and curbing speculative investments |