Policy & Profit

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Striking a balance with e-invoicing

- E-invoicing is transforming tax compliance and transparency but may stifle businesses
- A balanced enforcement approach is needed to protect innovation and jobs

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Malaysia is implementing e-invoicing, a Continuous Transaction Control model that aligns with global digital transformation trends. The government positions this as a necessary step to curb tax evasion, improve compliance, and ultimately enhance Malaysia's business competitiveness.

As a public policy practitioner, I recognise the benefits of e-invoicing – shedding light on the grey economy, streamlining tax collection and improving transparency.

But as a business owner, I can't help but worry that if not managed delicately, e-invoicing may inadvertently stifle the entrepreneurial spirit that Malaysia desperately needs to thrive.

Generational impact

To truly grasp the implications of e-invoicing, one must understand how it integrates into our tax system.

Unlike goods and services tax (GST), which primarily focuses on tax revenue collection, e-invoicing is about digitising transactions in real-time, ensuring full visibility of business income and expenses. I believe its impact would even surpass GST; it is a generational change in the making.

Malaysia's taxpayer base is composed of individuals, corporations and other entities (including cooperatives and enterprises).

In 2022, they collectively contributed RM153.5bil in tax revenue, with individuals accounting for 22%, corporations 53.5%, and others 24.5%. The main target of e-invoicing (for now) is business income tax – specifically corporations and the "others" category.

As at 2022, Malaysia had about one million registered businesses, of which 98% were micro, small and medium enterprises (MSMEs), and the rest, large corporations.

Given the revenue distribution, only a small fraction of businesses contribute the bulk of corporate tax revenue.

To compare and for context, 2.7 million individuals are contributing to the 22% or RM33.8bil in income tax.

The figures of corporations and others filing taxes could not be sourced at the time of writing.

With e-invoicing, the Inland Revenue Board (IRB) will be able to track every transaction, leaving no room for income tax evasion. The first phase of e-invoicing has already identified 66,000 businesses on eCommerce platforms that do not comply with tax obligations.

But the implications go beyond businesses. As e-invoicing data accumulates, authorities will eventually turn their focus to individuals. As of 2022, Malaysia's workforce stood at 15.1 million, yet only 4.18 million (27%) filed taxes and of that just 2.71 million qualified as taxpayers.

This means only a small percentage of working Malaysians are bearing the tax burden.

With e-invoicing, every transaction between individuals and businesses will be captured – whether it's a side hustle, a rental income, or a small home business – putting everyone under tighter scrutiny.

Ripple effect

While e-invoicing may seem like a straightforward compliance exercise, the reality is far more complex.

Business owners, particularly those in the MSME sector, are already overwhelmed with regulatory requirements, from subsidy rationalisation to increases in Employees' Insurance Scheme and Social Security Organisation contributions, potential Employees Provident Fund adjustments, and rising operational costs.

Adding real-time tax reporting into the mix could discourage small businesses from scaling or even pushing them into closing shop.

Imagine if the IRB aggressively enforces tax compliance on businesses that have long operated in the grey economy.

Fearfully, many may face bankruptcy, forcing closures that could send economic shockwaves through the system.

MSMEs in particular, employ almost half of Malaysia's workforce and if these businesses shut down, our job market will take a massive hit. Moreover, the perception of how tax enforcement is carried out matters. There is a tendency to label tax evaders as unscrupulous actors.

While some businesses certainly game the system, many are simply trying to survive in an ecosystem riddled with bureaucratic hurdles and high compliance costs. Taking an overly punitive approach without considering the economic and employment consequences could backfire on us instead.

That is not to say don't take action at all. But one must appreciate the context.

Before the introduction of the Malaya Income Tax Ordinance in 1947, Malaysia relied heavily on indirect taxes such as customs and excise duties. Income tax was a new concept then, just as e-invoicing is today.

Every major tax reform has faced resistance. People inherently dislike parting with their income, especially when they perceive inefficiencies in government spending.

E-invoicing represents the next iteration of tax collection, but its sheer reach will expose not just deliberate tax evasion but also incidental non-compliance.

Every informal side hustle, every under-the-table transaction – whether driven by necessity or convenience – will be dragged into the light.

The concern is not about preventing tax evasion but ensuring fairness and sustainability in enforcement – understanding the many families that could be impacted.

The way forward

The government must tread carefully to avoid suffocating the very ecosystem that fuels economic growth and domestic consumption. Here are key considerations for policymakers as they review the gains of data from e-invoicing:

> A flexible enforcement strategy: Distinguish between deliberate tax evasion and compliance struggles. Offer amnesty or structured repayment plans where necessary. Even in cases of deliberate evasions, prioritise options for the company that allow it to continue to operate.

> Reinvest revenue in MSMEs: Ring-fence a portion of the increased tax collected for loans, grants and incentives to ensure MSME development.

> Ensuring public trust: Transparency in government spending is crucial. If people see their taxes being used efficiently, they will be more willing to comply.

Malaysia must not sacrifice its entrepreneurial spirit in pursuit of higher tax revenue. A thriving, locally-driven business ecosystem is essential for long-term economic sustainability.

If the consequence of e-invoicing is a heavy-handed punitive enforcement approach to tax evaders, it risks deterring future entrepreneurs and pushing existing businesses into crisis.

Let us ensure the quest for compliance does not inadvertently kill the golden goose that lays the eggs of innovation, employment and growth.