Drivers and Impacts of Shadow Economy:
The Malaysian Experience
Mohd Shahfizan Md Salleh (IRBM)

12th November 2019
Introduction
Drivers of Shadow Economy
Impacts of Shadow Economy
Conclusion
Introduction

Shadow economy eating into tax revenue

It accounts for 21% of GDP, says Guan Eng

BY RAJVINDER SINGH
newsdesk@thesundaily.com

KUALA LUMPUR: There is a huge shortfall in the country’s tax revenue thanks to the shadow economy that now accounts for an estimated 21% of the gross domestic product. Finance Minister Lim Guan Eng said this loss was most obvious on the streets of Kuala Lumpur where foreigners, instead of locals, were the ones who were conducting all the business.

“They may have a deal with a local to use his business licence and they are not paying taxes. If we can ensure that they pay taxes, it will be a big boost to the national coffers,” Lim said after opening the National Taxation Seminar 2019 organised by the Inland Revenue Board (IRB) yesterday.

He said the IRB would be asked to intensify its enforcement activities. “This may help broaden our tax base if these people can be included in our taxation system,” Lim added.

He said that while such business activities were not allowed under the law, those involved should pay taxes, too.

For instance, he said, those who gained from the 1Malaysia Development Bhd scandal had a duty to pay taxes, and it was up to the court to decide what they did was right or wrong.

“We aim to collect taxes from those involved in the shadow economy. If we can find ways to ensure this group is taxed, it will be an important base for the government because the tax revenue will go up,” he said.

Lim said the introduction of the Tax Identification Number for those above 18 in 2021 was one way of tackling this issue but whether there was a need for a new law depended on recommendations from the IRB.

On whether any minister fell under the taxable income bracket of 30%, Lim said all of them had declared their income. “If they fail to do so, they can be charged under existing laws,” he said.

He added ministers were not allowed to engage in business.

Shadow Economy estimated at USD72.76 billion (21%) of Malaysian GDP
Drivers of Shadow Economy

- Tax Burden and Tax Policy
- Enforcement
- Corruption
- Cash Economy and the Organised Crimes
Tax Burden and Tax Policy

An increase in the illicit share of the cigarette market coincided with increased excise tax rates

The volume of excise-evading cigarettes has increased, but total consumption has not fallen

Cigarette consumption in Malaysia by source, 2013-2018

Source: Nielsen; Oxford Economics
Enforcement

Bank Negara raids eight illegal money services business firms in KL

Immigration Dept busts human trafficking syndicate in KL

Customs, police seize millions of Eramin 5 pills worth RM60m in Port Klang raid

Malaysia authorities seal off 3 illegal factories in Pasir Gudang

Immigration nabs 130 illegal immigrants in raids in Kajang, Puchong

Cops continue war on illegal gambling, 14,759 arrested since January
Corruption

Datuk among 16 custom officers nabbed in MACC’s widening probe on unpaid excise duties

NATION
Saturday, 20 Sep 2014
12:00 AM MYT
By M. KUMAR

RM114.5 mil seizure in Sabah corruption case biggest in MACC history

KOTA KINABALU: The seizure of RM114.5 million in a case of abuse of power involving infrastructure projects valued at RM3.3 billion associated with two civil servants in Sabah is the biggest in the history of the Malaysian Anti-Corruption Commission, it was stated here today.

MACC deputy chief commissioner (operations) Datuk Azan Baki said the seizure was made following the arrests of the civil servants - a director and a deputy director of a government agency - yesterday.

MACC freezess 375 accounts worth over RM560mil with links to illegal logging in Sarawak

NATION
Tuesday, 12 May 2015
7:25 PM MYT
By SHARON LING

Bank accounts of RM560mil frozen by MACC
Cash Economy and the Organised Crimes
Impacts of Shadow Economy

- Widening Tax Gap
- Distortion in Country GDP
- Disruption of Formal Economy
- Negative Impact to Society
Widening Tax Gap
Distortion in Country GDP

**SHADOW ECONOMY AS A % OF GDP**

- Zimbabwe: 67%
- Thailand: 43%
- Malaysia: 26%
- Hong Kong: 12%
- China: 12%
- Singapore: 9%
- New Zealand: 9%
- United Kingdom: 8%
- Australia: 8%
- US: 7%
- Switzerland: 7%

Source: Shadow Economies Around the World: What Did We Learn Over the Last 20 Years by Leandro Medina and Friedrich Schneider, International Monetary Fund working paper, 2018, via theglobaleconomy.com
Disruption of Formal Economy
Negative Impact to Society

Second largest tobacco firm in Malaysia may cut 40% of workers

LOGGING still rampant in Gua Musang

KUALA LUMPUR: While the heavy rainfall in Kelantan between Dec 22 and 24, 2014 was enough to inundate the state, other factors such as logging is said to have aggravated the situation further.

The expanse of land that have been cleared is evident when viewed from land, water or above.

The writers upon arriving in Gua Musang and Kuala Krai witnessed timber lorries on the public road at all hours, putting the lives of motorists in danger.
Conclusion

It is vital that tax administrators understand the drivers and appreciate the impacts of shadow economy in order to formulate better and effective strategies, policies and plans.

In the domain of cops and robbers, an interdiction serves to structure a black market and a shadow economy.

William Irwin Thompson