RDS
ROSLI DAHLAN SARAVANA PARTNERSHIP
ADVOCATES & SOLICITORS

Legal Insight

FEBRUARY 2021
Vol.2/Q1/21

CONTENT:

JUDICIAL REVIEW IN CUSTOMS DISPUTES:

MBM v Ketua Pengarah Kastam Diraja Malaysia

by Amira Rafie

Pursuant to the Rules of Court 2012, the decisions of the Director General of Customs ("**DGC**"), a public authority that carries out a public function in raising bills of demand against taxpayers, are amenable to judicial review. On the other hand, Section 143(5) of the Customs Act 1967 ("**CA 1967**") provides that all taxpayers aggrieved by the decision of the DGC must appeal to the Customs Appeal Tribunal to have its case heard.

In light of the latter statutory appeal procedure, it is no surprise that applications for leave for judicial review faces strong opposition in the courtroom. However, it is crucial to understand why in many instances judicial review is preferred. In a customs case, once a bill of demand is issued, the taxes and/or duties must be paid within the stipulated timeframe regardless of whether the taxpayer appeals against the decision or not. This inevitably results in taxpayers having to pay large sums despite the assessment being raised arbitrarily as well as having to wait for years

KDN: PP 19637/12/2020 (035236)

Printed by: **Percetakan Jiwabaru Sdn Bhd** | No. 2, Jalan P/8, Kawasan Miel Fasa 2, 43650 Bandar Baru Bangi, Selangor **(KDN: PQ1780/427)**

before finally having their money refunded. Application for judicial review at the High Court allows taxpayer to make a concurrent application for a stay of any further proceedings and/or enforcement of the bill of demand until the High Court decides on the matter.

This inevitably results in taxpayers having to pay large sums despite the assessment being raised arbitrarily as well as having to wait for years before finally having their money refunded.

The Supreme Court in ***Majlis Perbandaran Pulau Pinang v Syarikat Bekerjasama-Sama Serbaguna Sungai Gelugor Dengan Tanggungan*** **[1999] 3 CLJ 65** had expressed:

"In deciding on the choice of remedy in such a situation the court should take into account certain matters; to wit:

> *Whether the alternative statutory remedy will resolve the question at issue fully and directly; whether the statutory procedure would be quicker, or slower, than procedure by way of judicial review; whether the matter depends on some particular or technical knowledge which is more readily available to the alternative appellate body; these are amongst the matters which a court should take into account when deciding whether to grant relief by way of judicial review when an alternative remedy is available. ...*
>
> *Where there is an alternative remedy, judicial review will only be granted in exceptional circumstances."*

In the recent case of **MBM v Ketua Pengarah Kastam Diraja Malaysia ("MBM case")**, the High Court granted leave to the taxpayer to initiate a judicial review against the DGC.

Facts

The taxpayer is the general distributor for a European car in Malaysia. The dispute is in relation to the hybrid model of a car .In 2015, the Minister of Finance ("**MOF**") had granted, amongst others, a full import duty exemption for completely knocked-down (CKD) units for certain models of vehicles to be assembled locally. Further, in 2017, the MOF approved

the taxpayer's application for a special incentive package subject to the conditions stated in the approval letter.

In 2018, the DGC conducted a post import audit on the taxpayer and subsequently issued a preliminary audit finding in relation to the hybrid model. The DGC disregarded the taxpayer's numerous attempts at explaining that the hybrid model had been approved for a full tax exemption pursuant to the letters from the MOF in 2015 and 2017.

The issue for determination in this case is merely a question of law which is whether the DGC has any legal basis and authority to disallow the taxpayer's claim for tax exemption granted to the taxpayer by the MOF in the absence of a withdrawal of the tax exemption by the MOF.

In July 2020, the taxpayer was issued with two bills of demand by the DGC for the audit period January to December 2017 pursuant to the CA 1967 and the Goods and Services Tax Act 2014 ("**GST Act 2014**") imposing additional duties amounting to RM 8.7 million.

The taxpayer maintains that it had adhered to and complied with all the conditions stated in both approval letters and being aggrieved by the assessment from the Customs, filed an application for leave for judicial review at the High Court. On 24.9.2020, the High Court heard both the taxpayer's application for leave and the objections from the Attorney General's Chambers on behalf of the DGC. On 19.10.2020, the High Court granted the taxpayer, leave to initiate judicial review proceedings against the DGC.

The issue for determination in this case is merely a question of law which is whether the DGC has any legal basis and authority to disallow the taxpayer's claim for tax exemption granted to the taxpayer by the MOF in the absence of a withdrawal of the tax exemption by the MOF.

Alternative Remedy Is Not A Bar To Judicial Review

The general position is as enumerated by the Supreme Court in the case of Government of Malaysia & Anor v Jagdis Singh [1987] 2 MLJ 185 which recognised that even where there is an alternative remedy for the

aggrieved person, judicial review is available in the following exceptional circumstances:

(i) Clear lack of jurisdiction; or
(ii) Blatant failure to perform statutory duty; or
(iii) A serious breach of the principles of natural justice.

Such principle is consistent with more recent decisions of the Federal Court in ***Bintulu Lumber v Ketua Pengarah Hasil Dalam Negeri*** **[FC No. [01(f)-28-10/2019(Q)]** and ***Ketua Pengarah Hasil Dalam Negeri v Alcatel-Lucent (M) Sdn Bhd & Anor [2017]*** **2 CLJ 1**. In both these cases, although it was found that judicial review were not a suitable remedy for the taxpayers based on particular facts of the case, the Federal Court was careful not to shut the door on judicial review in tax cases where there are exceptional circumstances.

It was established by the Federal Court in the *Majlis* Perbandaran Pulau Pinang case that an error of law amounts to a lack of jurisdiction and Certiorari (an order to quash the decision of the public authority) will lie to correct it:

> *"In our view, therefore, unless there are special circumstances governing a particular case, notwithstanding a privative clause, of the "not to be challenged, etc," kind, judicial review will lie to impeach all errors of law made by an administrative body or tribunal and, we would add, of inferior courts. In the words of Lord Denning in Pearlman v Harrow School (ibid) at p.70, "No Court or tribunal has any jurisdiction to make an error of law on which the decision in a case depends.* ***If it makes such an error it goes outside its jurisdiction and certiorari will lie to correct it****."*

Similarly, this was expressed in the Court of Appeal case of ***Syarikat Kenderaan Melayu Kelantan Bhd v Transport Workers Union*** **[1995] 2 CLJ 748**.

Furthermore, Section 141N of the CA 1967 makes it clear that a taxpayer has the option of either appealing to the Customs Appeal Tribunal or to commence proceedings at the High Court. The provision reads as follows:

"(1) *Where an appeal is lodged with the Tribunal and the appeal is within the jurisdiction of the Tribunal, the issues in dispute in such appeal, whether as shown in the initial appeal or as emerging in the course of the hearing, shall not be the subject of proceedings between the same parties in any court unless-*

(a) ***the proceedings before the court were commenced before the appeal was lodged with the Tribunal****; or*

(b) the appeal before the Tribunal is withdrawn, abandoned or struck out.

(2) *Where paragraph (1)(a) applies, the issues in dispute in the appeal to which those proceedings relate, whether as shown in the initial appeal or as emerging in the course of the hearing, shall not be the subject of proceedings between the same parties before the Tribunal unless the appeal before the court is withdrawn, abandoned or struck out."*

If Parliament had intended for an appeal to be made only to the Tribunal, it would have been expressly stated, as Parliament does not act in vain. Thus, the legislative intention behind Section 141N of the CA 1967 is clear in providing two options for redress to the taxpayer.

Judicial Review Is The Only Remedy

In relation to bills of demand raised under the GST Act 2014, as was the issue in the MBM case, the taxpayer does not have the right to appeal to the GST Appeal Tribunal because the GST Act 2014 has been repealed by Section 3 of the Goods and Services Tax (Repeal) Act 2018 ("**GST Repeal Act 2018**") which was gazetted on 28.8.2018 and came into effect on 1.9.2018. The repeal of the GST Act 2014 has a bearing on the present case as the GST Appeal Tribunal established under Section 125 of the GST Act 2014 has also since been abolished.

Not only that, the taxpayer does not have the right to appeal to the Customs Appeal Tribunal after the amendment to Section 141M of the CA 1967. With effect from 1.9.2018, Section 141M of the CA has been amended

by Section 10 of the Customs (Amendment) Act 2018 to state that the jurisdiction of the Custom Appeal Tribunal to hear appeals in relation to GST is stated under Section 5 of the GST Repeal Act 2018. Section 5(1) of the GST Repeal Act 2018, only allows the Customs Appeal Tribunal to decide on a review application under Section 124(1) of the GST Act, as if the GST Act had not been repealed, if the application is made before 1.9.2018. In the MBM case, the Customs Decision was made after the GST Act has been repealed. Thus, the taxpayer could no longer file a review application under Section 124(1) of the GST Act.

Based on the above, it is plain to see that the taxpayer in this case is not accorded with any recourse or remedy under Section 5 of the GST Repeal Act. Therefore, the only way for the taxpayer to seek relief is to file a judicial review application.

Exceptional Circumstances

At the hearing of the MBM case, it was submitted that the DGC had committed an error of law and exceeded its jurisdiction in raising the bills of demand. Firstly, the DGC had failed to comply with the decision of the Court in ***Ketua Pengarah Hasil Dalam Negeri v Latex Manufacturing Sdn Bhd* [2017] 7 MLJ 379** which states that where there is no cancellation of a tax incentive by the relevant authorities provided under the law, the taxpayer ought to be allowed to continue enjoying the tax incentive granted to it. Further, it was also decided that there must be a strict adherence to the procedures provided under the law for a withdrawal of tax incentive and the tax authority is not the rightful authority to withdraw such incentives.

Secondly, in ***Syarikat Pendidikan Staffield Bhd v Ketua Pengarah Hasil Dalam Negeri* [2011] 5 CLJ 916** has held that once the taxpayer had satisfied all the conditions, the Inland Revenue Board must give effect to the said exemption. The Inland Revenue Board is not allowed to disregard such exemption arbitrarily or to impose additional conditions on the grant of the exemption. Drawing parallels to the MBM case, the taxpayer had complied with all the conditions imposed by the MOF and had not been informed of any contravention or breach of the same.

There is also an issue of breach of natural justice whereby the taxpayer has a legitimate expectation that the DGC will adhere to the import duty exemption and the special incentive package granted by the MOF. The taxpayer took the view that the DGC's actions, constituted a denial of the taxpayer's legitimate expectations arising from the approval granted by the MOF.

The Court of Appeal in ***Hotel Sentral (JB) Sdn Bhd v Pengarah Tanah dan Galian Negeri Johor, Malaysia & Ors*** **[2017] 6 CLJ 161** held that legitimate expectation as a concept, is now a term of art capable of being enforced in law and it is incumbent upon the court to protect the interests of parties whose expectations have been created by the very conduct of public decision-making bodies when such expectations faces an onslaught by virtue of changes and / or reversals in decisions that had been acted upon by such parties. Further, there are authorities from other jurisdictions which have held that where a public body exercising a statutory function had induced a legitimate expectation of a substantive benefit through a promise, the subsequent denial of that benefit could be so unfair, it would amount to an abuse of power. This was explained in great detail in the English Court of Appeal case of ***Regina v North and East Devon Health Authority, ex parte Coughlan*** **[2001] QB 213.**

The granting of leave for judicial review in tax cases is in line with settled law that every exercise of statutory power cannot be arbitrary.

In essence, by failing to adhere to and apply the settled legal principles and the decision of our Courts above, the DGC has clearly committed an error of law amounting to a clear lack of jurisdiction, which warrants the grant of leave for judicial review in this case.

Conclusion

The granting of leave for judicial review in tax cases is in line with settled law that every exercise of statutory power cannot be arbitrary. Notably, the Federal Court in ***Indira Gandhi a/p Mutho v Pengarah Jabatan Agama Islam Perak and others*** **[2018] 3 CLJ 145** had highlighted that:

"At the outset, it is axiomatic that any exercise of legal power, including discretionary power, is subject to legal limits.

Thus it is clear to us that the boundaries of the exercise of powers conferred by legislation is solely for the determination by the courts. If an exercise of power under a statute exceeds the four corners of that statute, it would be ultra vires and a court of law must be able to hold it as such..."

In any case, with regard to this decision and the recent tax cases, this serves as a reminder that judicial review remains a viable course to challenge the decision of the public authority tax collection offices, be it the DGC or the Inland Revenue Board.

Amira Rafie | *Pupil-in-Chambers*
Tax, SST & Customs
amirarafie@rdslawpartners.com

SECURING A STAY ORDER IN TAX DISPUTES:

AN ANALYSIS OF THE HHD CASE

by S Saravana Kumar

The COVID-19 pandemic has affected many businesses in Malaysia in multiple ways which includes financial impacts. The restriction in economic and social activities has largely affected the manner in which taxpayers conduct their businesses. This is compounded even further with the sluggish global economy, resulting in poorer consumer demand. These factors combined with many more, left taxpayers in a position with a tight cashflow.

In this judicial review proceeding, the taxpayer, who is a property developer, applied for an order to stay all further proceedings and effect in relation to the disputed tax assessments raised by the Inland Revenue Board ("**IRB**") pending the disposal of the judicial review proceedings.

Facts

The taxpayer entered into the agreements with the Johor State Government whereby the taxpayer has agreed to sell a stipulated number of its property units to Bumiputera purchasers at a discount. In the event where the taxpayer is unable to sell the Bumiputera property units, the units will be made available to non-Bumiputera purchasers provided that the conditions in the agreements are complied with. Pursuant to the agreements, the taxpayer applied to the Johor State Government to release the Bumiputera units to the non-Bumiputera buyers. In response, the taxpayer was asked to make contributions to the Johor State Government in order to obtain the release. The taxpayer deducted the contributions made to the Johor State Government as a deductible expense under Section 33(1) of the Income Tax Act 1967.

In March 2020, subsequent to a tax audit, the IRB issued its tax audit

findings letter to the taxpayer. Among others, the IRB alleged that the contributions are not allowed for tax deduction as it is capital in nature. The taxpayer responded with detailed explanations stating reasons on why the contributions are deductible by emphasizing on the nexus between the contributions and production of income. In June 2020, the IRB maintained its position and raised tax assessments for the years of assessment 2015, 2016, 2017 and 2018 for nearly RM 9 million.

In fact, in ***Kerajaan Malaysia v Margaret Au Nyat Fah* [2008] 3 CLJ 424**, the High Court took the view that some of the IRB's powers to take civil action against taxpayers, appear to be amongst the harshest amongst all civil laws and that some of the measures taken to collect taxes may be seen to be oppressive.

On 27.8.2020, the High Court heard the taxpayer's leave application for judicial review and also the objections from the Attorney General's Chambers and the IRB. Being satisfied that there were exceptional circumstances in the present matter, the High Court granted the taxpayer leave to commence judicial review proceedings against the IRB. Consequently, the taxpayer sought for a stay order against the payment of the disputed taxes. The taxpayer submitted that the High Court had the jurisdiction to grant a stay order even in a tax matter.

Jurisdiction To Grant Stay In Tax Matters

The first question to be determined is whether a stay of further proceedings should be granted until the full and final determination of the judicial review application pursuant to the court's inherent jurisdiction. In ***Government of Malaysia v Jasanusa Sdn Bhd* [1995] 2 MLJ 105,** the Supreme Court clearly stated that:

> *"With respect, in our view,* ***neither s. 103 (I) nor s. 106 (3), bars a Court,*** *in appropriate circumstances,* ***from exercising its inherent powers of granting a stay, even in a tax case.*** *(See Supreme Court decision in Chong Woo Yit v. Government of Malaysia [1989] 1 MLJ 473 at p. 475 Col. 2, last para, per Gunn Chit Tuan CJ)."*

In ***Kerajaan Malaysia v Ekran Bhd* [2006] 5 CLJ 92**, the High Court held that:

"...It is *not disputed that the power to grant stay of proceedings or execution pending appeal is a discretionary exercise of power premised on s. 73 of the Courts of Judicature Act* 1964".

In fact, in ***Kerajaan Malaysia v Margaret Au Nyat Fah* [2008] 3 CLJ 424,** the High Court took the view that some of the IRB's powers to take civil action against taxpayers, appear to be amongst the harshest amongst all civil laws and that some of the measures taken to collect taxes may be seen to be oppressive. Accordingly, the court would not be restricted from granting a stay if the facts warrant it:

"Section 106(3) of the ITA 1967 states: "In any proceedings under this section the court shall not entertain any plea that the amount of tax sought to be recovered is excessive, incorrectly assessed, under appeal or incorrectly increased under s. 103(4), (5) or (5A)." This section, to some extent in my view, is in breach of natural justice and violates the spirit of the Federal Constitution. A judgment obtained on an erroneous assessment which the defendant cannot honour may lead him to be made a bankrupt and/or to financial ruin. ***AMONG ALL CIVIL LAWS, THIS APPEARS TO BE THE HARSHEST and SOME OF THE MEASURES TAKEN TO COLLECT TAXES*** *as on the facts of this case* ***ARE PRIMA FACIE SEEN TO BE OPPRESSIVE.*** *For example, in this case, the administratrix was deprived from travelling overseas when the tax due and owing was not personal to her.* ***WHEN THERE IS AN ABUSE SUCH AS THIS, THE COURT MUST READILY ACT TO PROVIDE THE REMEDY TO THE VICTIM.*** *In this instance, the court is obliged to grant the judgment, as per the law. However,* ***THE COURT IS NOT RESTRICTED FROM GRANTING A STAY*** *of the judgment, if the facts of the case warrant so."*

It is trite law that the High Court has the power to grant such a stay against public authorities such as the IRB

Preserving Status Quo

It is trite law that the High Court has the power to grant such a stay against public authorities such as the IRB as held in ***Islamic Financial Services Board v Marlin Fairol Mohd Faroque & Anor* [2010] 8 CLJ 173.** A judicial review stay is not the same as stay of execution after judgment in judicial

proceedings. It should be given a wide interpretation so as to enhance the effectiveness of the judicial review jurisdiction. This means preserving the status quo by suspending the Decision under challenge pending the determination of the judicial review application, which as a result, will not deny the taxpayer the full benefit of a successful challenge.

In the HHD case, the taxpayer urged the High Court to preserve the status quo of the taxpayer prior to the IRB's decision to raise the disputed tax assessments. The taxpayer's argument was that the implementation of the Decision will result in a large and burdensome amount of taxes that are wrongfully and unfairly imposed on the taxpayer. As the amount of the disputed tax is rather high, this will result in a financial crisis and cash flow problems for the taxpayer.

It must be noted that the courts have recognised that the categories of 'special circumstances' are 'infinite' and will 'grow with time' depending on the facts of each case.

Special Circumstances As Test for Stay

The paramount consideration for the courts in allowing or refusing a stay, is whether or not special circumstances exists as held in ***Kosma Palm Oil Mill Sdn Bhd & Ors v Koperasi Serbausha Makmur Bhd*** **[2003] 4 CLJ 1.** It must be noted that the courts have recognised that the categories of 'special circumstances' are 'infinite' and will 'grow with time' depending on the facts of each case. It was observed in ***The Government of Malaysia v Datuk Haji Kadir Mohamad Mastan and another case*** **[1993] 4 CLJ 98**:

> *"I respectfully agree with those views of the learned V.C. George J. An attempt was made to define special circumstances by Raja Azlan Shah J. (as His Majesty then was) in the case of Leong Poh Shee V. Ng Kat Chong [1965] 1 LNS 90 , viz:*
>
> Special circumstances, as the phrase implies, must be spec*ial under the circumstances as distinguished from ordinary circumstances. It must be something exceptional in character, something that exceeds or excels in some way that which is usual or common.*
>
> *The definition only serves to emphasise the fact that* ***there are myriad***

circumstances that could constitute special circumstances with each case depending on its own facts. *I am of the opinion that the* ***list of factors constituting special circumstances is infinite and could grow with time.*** *Any attempt to limit the list or close a category would be to impose a fetter on the exercise of the discretion of the Court whether to grant or stay an execution; making the discretion less of a discretion. This is surely not what discretion is all about.* ***AS LONG AS ONE DOES NOT STRAY BEYOND THE PERIMETER SET BY THE JUDICIAL PRINCIPLES, THE DISCRETION CAN BE EXERCISED.***"

The High Court has also provided further guidance on the type of special circumstances that could warrant the granting of a stay in the following cases:

(a) ***Jaya Harta Realty Sdn Bhd v Koperasi Kemajuan Pekerja-Pekerja Ladang Bhd*** **[2000] 6 MLJ 493:**

"What factors would constitute as special circumstances may vary according to the circumstances of each particular case. Three essential ingredients constituting special circumstances has been propounded as follows: (i) where the ***balance of convenience*** *is in favour of the applicant; (ii) where it is apparent that* ***unless a stay is granted an appeal will be rendered nugatory****; and (iii) that the* ***applicant has an arguable appeal****".*

(b) ***Mohamad Mustafa v Kandasami (No 2)*** **[1979] 2 MLJ 126:**
"One of the determining factors that call for consideration is ***whether by not making an order for stay of execution it would make the appeal if successful, nugatory in that it would deprive an appellant of the results of the appeal****. How pertinent that factor would be may vary according to the circumstances of each particular case."*

In essence, the High Court had succinctly laid down 4 factors that ought to be considered in an application for a stay of proceedings:

(i) Whether the applicant can show special circumstances – an order for stay will be granted if an applicant can demonstrate special

circumstances when his or her appeal to the Court of Appeal will be rendered academic if the proceedings in the High Court are not stayed;

(ii) The balance of convenience (now popularly known as balance of justice) – namely a comparison of the existence, nature and extent of prejudice which may be suffered by the parties if proceedings are stayed or otherwise;

(iii) If an application to stay proceedings is an abuse of court process, such an application will be refused; and

(iv) Whether there is an explained delay in applying for a stay of proceedings.

Stay In Tax Matters

In the authors' view, the exercise of the discretion to grant a stay order would be well within the perimeter set by the judicial principles highlighted above as various special circumstances exist:

a) Balance of convenience favours the granting of the Stay;

b) The history as a law-abiding, responsible corporate taxpayer;

c) Harshness of the threat of civil action should the Stay be refused; and

d) The IRB's failure to exercise its powers accordingly.

In ***Jasanusa*** *(supra)*, the Supreme Court had then reminded that:

"...Matters of this nature involve, inter alia, balancing the need of the Government to realise the taxes and **THE NEED OF THE TAXPAYER TO BE PROTECTED AGAINST ARBITRARY OR INCORRECT ASSESSMENTS...** The Court should also bear in mind **THE POSSIBILITY OF ARBITRARY OR INCORRECT ASSESSMENTS, BROUGHT ABOUT**

BY FALLIBLE OFFICERS WHO HAVE TO FULFILL THE COLLECTION OF A CERTAIN PUBLICLY DECLARED TARGETED AMOUNT OF TAXES and whose assessments, as a result, **may be influenced by the target to be achieved rather than the correctness of the assessment**."

Matters of this nature involve, inter alia, balancing the need of the Government to realise the taxes and THE NEED OF THE TAXPAYER TO BE PROTECTED AGAINST ARBITRARY OR INCORRECT ASSESSMENTS...

Conclusion

In the HHD case, upon hearing the parties, the High Court granted a stay order to the taxpayer until the determination of its judicial review application. For the authors, consideration of public interest as a whole and the comparative effects of the granting and refusal of a stay, plays a key role to arrive at the conclusion that the balance of convenience is heavily in the favour of the granting of stay for the taxpayer. The granting of a stay as sought for by the taxpayer would ensure that the status quo presently prevails to be preserved and would also be in line with our courts' constitutional role as the 'bulwark' against 'unlawful action' as reaffirmed by the Federal Court in ***Indira Gandhi a/p Mutho v Pengarah Jabatan Agama Islam Perak and others*** **[2018] 1 MLJ 545.**

S Saravana Kumar
Partner & Head of Tax, SST & Customs
Tax, SST & Customs
sara@rdslawpartners.com

SF SDN BHD CASE:

INSIGHTS INTO GST EXEMPTION FOR LAND USED FOR AGRICULTURAL PURPOSES

by Ng Kar Ngai

Recently, the High Court in **SF Sdn Bhd v Menteri Kewangan & Anor** allowed the application for judicial review by SF Sdn Bhd to quash the decision of the Minister of Finance ("**Minister**"). The decision was made by the Director General of Customs ("**Director General**") on the Minister's behalf. The Director General had erroneously determined that parts of the land that are intended to be used for commercial development by SF Sdn Bhd should be subjected to goods and services tax ("**GST**").

Facts

SF Sdn Bhd is an established property development and investment holding company. In December 2016, SF Sdn Bhd had entered into a sale and purchase agreement to purchase five adjoining parcels of freehold land ("**the Land**"). The Land was being used for oil palm plantations and was zoned as agricultural land.

In March 2017, SF Sdn Bhd made a rezoning application to convert the zoning of the Land from agricultural to mixed development. Although SF Sdn Bhd's rezoning application had been acknowledged, the rezoning application was subject to the fulfilment of certain conditions, including payment of the rezoning premium. The legal titles of the Land were transferred to SF Sdn Bhd in September 2017. At the material time, the Land had not been rezoned from agricultural to mixed development as SF Sdn Bhd had appealed on the conditions imposed. Further, the rezoning premium payable had not been made known to SF Sdn Bhd.

The vendor of the Land subsequently issued a letter to the Director General to seek a written confirmation that no GST is chargeable for the supply of the Land. In response, the Director General held that while the

sale of the Land, which was estate land used for oil palm plantations was an exempt supply, if it is found that the Land is intended to be used for commercial purposes, the Land or parts of the Land used for commercial purposes is subject to GST. On this basis, the vendor had informed SF Sdn Bhd that the sale of the Land is subject to GST.

Consequently, SF Sdn Bhd made an application pursuant to paragraph 2(2) of the Goods and Services Tax (Exempt Supply) Order 2014 ("**Exempt Supply Order**") to the Minister. However, the Minister referred SF Sdn Bhd's application to the Director General and requested the Director General to provide a response on behalf of the Minister. As a result, the Director General maintained that GST should be imposed on parts of the Land intended to be used for commercial purposes. Being aggrieved by the decision, SF Sdn Bhd applied for judicial review to set aside the said decision.

The Law

During the GST regime, a sale of land was a supply of goods under Paragraph 2(1)(b) of the First Schedule of the Goods and Services Tax Act 2014 ("**GST Act**"). However, not every supply of land was taxable. In particular, Section 18(2) of the GST Act empowered the Minister to prescribe, by way of Gazette, any supply of goods or services as an exempt supply. Pursuant to Section 18(2) of the GST Act, the Minister made the Exempt Supply Order.

Under Item 1(1) of the First Schedule of the Exempt Supply Order, a land qualifies to be exempted from GST if the land is a land used (First Limb), or intended to be used and to the extent of it being used (Second Limb), or intended to be used (Third Limb), for residential, agricultural or general use purposes.

Under Item 1(1) of the First Schedule of the Exempt Supply Order, any land used or intended to be used to the extent of it being used or intended to be used for residential or agricultural purposes, or general use is an exempt supply.

In the event there is a dispute as to whether a supply falls within the ambit of the Exempt Supply Order, Paragraph 2(2) of the Exempt Supply Order provides that such question shall be decided by the Minister whose decision shall be final.

Based on the wording of the First Limb, a supply of land would qualify as an exempt supply if the land was used for agricultural purposes.

The High Court's Decision

The High Court in allowing SF Sdn Bhd's application for judicial review and quashing the said decision, accepted the following arguments:

(i) Issue 1 – GST treatment of the Land

(a) Under Item 1(1) of the First Schedule of the Exempt Supply Order, a land qualifies to be exempted from GST if the land is a land used (First Limb), or intended to be used and to the extent of it being used (Second Limb), or intended to be used (Third Limb), for residential, agricultural or general use purposes;

(b) By employing the word "or", it is clear that a supply of land qualifies as an exempt supply if either one of the above three limbs is fulfilled. In other words, if a land falls under any one of the limbs specified, such land would be an exempt supply;

(c) The phrase "any land used" is drafted in the past tense which made it an express condition that the land in question must have been put into use, in the past or at the time of supply, for residential, agricultural or general use purposes in order for such land to qualify as an exempt supply;

(d) Based on the wording of the First Limb, a supply of land would qualify as an exempt supply if the land was used for agricultural purposes. The Land in the present matter was estate land used for oil palm plantations. On the premise that the existing usage of the Land was for agricultural purposes, the Land would be land used for agricultural purposes and thus qualifies as an exempt supply under the First Limb;

(e) The above interpretation is consistent with the strict approach in interpreting taxing statutes as held in various cases such as ***National Land Finance Co-operative Society Ltd v Director General of Inland Revenue [1993] 4 CLJ 339, Nike Sales Malaysia Sdn Bhd v Jabatan Kastam Diraja Malaysia & Ors (2013)*** **MSTC 30-060,** ***Levi Strauss (Malaysia) Sdn Bhd v Ketua Pengarah Kastam, Malaysia (2011)*** **MSTC 30-021** and ***Tobacco Importers and Manufacturers Sdn Bhd v Ketua Pengarah Kastam, Jabatan Kastam Diraja Malaysia*** **[2017] 1 LNS 1738;**

(f) By claiming that the Land is taxable based on SF Sdn Bhd's future intention to develop the Land for mixed development, the Minister and Director General are essentially invoking the Second Limb and the Third Limb to impose tax on a subject that is already an exempt supply; and

(g) The Minister and Director General are not allowed to arbitrarily disregard the effect of the First Limb. Such interpretation is illegal and wrong in law as it defeats the intention of Parliament in empowering the Minister to gazette the Exempt Supply Order, which is to exempt a taxable supply and not to impose tax on a subject.

The Minister and Director General are not allowed to arbitrarily disregard the effect of the First Limb. Such interpretation is illegal and wrong in law as it defeats the intention of Parliament in empowering the Minister to gazette the Exempt Supply Order, which is to exempt a taxable supply and not to impose tax on a subject.

(ii) Issue 2 – Delegation of decision-making power

(a) It is trite law that a discretionary power must be exercised personally unless there is an express provision empowering the delegation of the decision-making power. This principle is reflected in the Federal Court case of Ang Ming Lee & Ors v Menteri Kesejahteraan Bandar, Perumahan dan Kerajaan Tempatan & Anor and other appeals [2020] 1 MLJ 281;

(b) The wording of Paragraph 2(2) of the Exempt Supply Order is clear and unambiguous. The power or authority to decide on whether any supply of goods or services is an exempt supply is vested exclusively in the Minister whose decision shall be final. The Minister is not empowered to delegate such authority to the Director General;

(c) Section 18(2) of the GST Act only empowers the Minister to determine any supply of goods and services to be an exempt supply and this intention is reflected in Paragraph 2(2) of the Exempt Supply Order. In such circumstances, it is clear that trust is being placed upon the Minister to exercise that power personally; and

(d) Even if assuming that such delegation is legally permitted, the Minister is in breach of the first principle of natural justice, i.e. no man shall be judge in his own cause (nemo judex in causa sua) by delegating the decision-making power back to the Director General who made the initial decision against which SF Sdn Bhd was appealing.

Conclusion

This recent decision dealt with a novel point of law in a GST case as to whether a supply of land used for agricultural purposes qualifies as an exempt supply under Item 1(1) of the First Schedule of the Exempt Supply Order.

In making its decision, the High Court expressed the view that it is essential to identify the status of the land at the time of supply. In the present matter, the time of supply is at the time when the Land is transferred or disposed of. At the material time, the Land was being used for oil palm plantations and was zoned as agricultural land. Accordingly, the Land is an exempt supply.

This decision further demonstrates that once a supply is already an exempt supply, the Minister and Director General are not allowed to arbitrarily disregard the exemption and look to a taxpayer's future intention to impose tax on a subject that is already an exempt supply. Such an interpretation of Item 1(1) of the First Schedule of the Exempt Supply Order is not only arbitrary, but it also raises a further question as to when this intention should be determined.

Additionally, this case also serves as a reminder that a public authority has no jurisdiction to commit an error of law or act in a manner that is procedurally improper or in breach of the principles of natural justice. Such an error or procedural impropriety would render the decision susceptible to judicial review.

Ng Kar Ngai | *Associate*
Tax, SST & Customs
karngai@rdslawpartners.com

INSIGHTS INTO EXCEPTIONAL INPUT TAX CREDIT

by Nur Amira Ahmad Azhar

During the GST ("**Goods and Services Tax**") regime, a business registered under the Malaysian GST is required to charge GST on its output of taxable supply of goods and services made to its customers. The business can then claim input tax incurred in the course of its business. Input tax is defined as the GST incurred on any purchase or acquisition of goods and services by a taxable person for making a taxable supply in the course or furtherance of business[1]. Under the GST, businesses are entitled to claim input tax credit when the business is a GST registered business or when the business incurs the GST.

Many businesses incur GST expenses prior to the effective date of their GST registration, to be used in the course or furtherance of business. Can a business claim the GST amount spent before he it was registered under the GST Act?

JEP Sdn Bhd v Ketua Pengarah Kastam, Jabatan Kastam Diraja

Recently, the High Court in **JEP Sdn Bhd v Menteri Kewangan & Anor** allowed the application for judicial review by JEP Sdn Bhd ("**JEP**") to quash the decision of the Director General of Customs ("**DG**"). The DG had erroneously disallowed JEP's claim for input tax credit on the basis that JEP did not make any taxable supply whilst being a registered person.

Facts

JEP is in the business of constructing, commissioning, operating and maintaining a Coal Fired Power Plant. In late 2014, JEP applied to be registered under the Goods and Services Act 2014 ("**GST Act**"). In the late 2017, the JEP made an Exceptional Input Tax Credit Claim under

1 *GST Guide for Input Tax Credit*

Regulation 46(1) of the Goods and Services Regulations 2014 ("**GST Regulations**") amounting to RM45 million. The Director General ("**DG**") apportioned the claim and allowed only RM2,232.21 of the Exceptional Input Tax Credit Claim ("**Exceptional ITC Claim**"). The remaining (i.e. the Disallowed ITC) was rejected by the DG. The Disallowed ITC is the input tax paid by JEP for the construction of the Power Plant. The reason for rejecting JEP's claims were as follows:

The GST legislation provides an exception to the general rule by allowing a taxable person to claim GST incurred on business expenses prior to their effective date of GST registration.

(i) The Disallowed ITC is not eligible to be credited as JEP has not made any taxable supply from the Power Plant when it was registered under the GST Act; and

(ii) The input tax incurred for the furniture and equipment for the continuance of the JEP's business is approved with the following calculation:

Input tax x (Period in which a person becomes registered under the GST Act ÷ Useful life items)

Exception To The General Rule – The Law

The GST legislation provides an exception to the general rule by allowing a taxable person to claim GST incurred on business expenses prior to their effective date of GST registration. Regulation 46(1) of the Goods and Services Regulations 2014 ("**GST Regulations**") enables businesses to claim input tax incurred by them prior to their registration under the GST Act. The requirements for an exceptional input tax claim are as follows:

(a) The claim must be paid prior to a business' registration under the GST Act;

(b) The claim was paid for the furtherance of business which was carried on by the at the time of payment; and

(c) The claim must be made in the first GST return.

The High Court's Decision

The High Court in allowing JEP's application for judicial review and quashing the said decision, accepted the following arguments:

Argument 1 - Contravention with the object and spirit of the GST Act

(a) The Explanatory Statement to the GST Bill 2014 has made it clear that GST is never intended to be a cost to business:
"... The GST is a broad-based consumption tax based on a value-added concept ... Payment of tax is made in stages with by the intermediaries in the production and distribution process. The tax itself is not a cost to the intermediaries and does not appear as an expense item in their financial statements.

GST covers all sectors of the industry and is a tax on final consumption of goods and services. It is collected through a credit system where GST incurred on inputs is offset against GST charged on outputs."

(b) It is trite law that an authority is not allowed to make decisions which go against the object objective and spirit of the legislations as held by the Federal Court in Palm Oil Research and Development Board Malaysia & Anor v Premium Vegetable Oils Sdn Bhd & Another Appeal [2005] 3 MLJ 97.

(c) In The Ordinary Co Sdn Bhd v Lembaga Rayuan Negeri Selangor & Anor [2014] 7 MLJ 705 and Syarikat Pendidikan Staffield Bhd v Ketua Pengarah Hasil Dalam Negeri [2011] 5 CLJ 916, the High Court held that the courts in reviewing a decision made by the authority must consider the intent of the Parliament in enacting the legislations and give effect to the same. Any decision which contravenes the intent of the Parliament ought to be quashed as it tantamount to an error of law.

(d) One of the key mechanisms of the GST concept is that businesses may recover the GST incurred on costs and business expenses from the Government (in the form of input tax credit) to ensure that GST is chargeable only on the value added by a business activity. It is in the

same spirit that the Parliament enacted Regulation 46(1) of the GST Regulations to enable businesses to claim for input tax incurred by them prior to their registration under the GST Act.

Argument 2 - No Requirement of Taxable Supply

(a) The requirements for an exceptional input tax credit claim are set out in Regulation 46(1) of the GST Regulations and have been duly complied with:

(i) The Exceptional ITC Claim was paid prior to JEP's registration under the GST Act on 1.8.2016;

(ii) The Exceptional ITC Claim was paid for the purposes of the JEP's business which was carried on by the JEP at the time of payment; and

(iii) JEP's claim for the Exceptional ITC Claim was made in its first GST return on 28.12.2018.

(b) Sections 38 and 39 of the GST Act are irrelevant for the purposes of ascertaining an exceptional input tax credit claim. The correct provision to be referred is Regulation 46(1) of the GST Regulations which is a stand-alone provision. This is because:

(i) The wordings used in Regulation 46(1) of the GST Regulations do not require JEP to make a taxable supply before making the Exceptional ITC Claim.

(ii) It is also clear from the express wordings in Regulation 46(1) of the GST Regulations that the Parliament did not intend to confer any discretion on the Respondent to impose additional requirement when considering an exceptional input tax credit claim.

Argument 3 – The DG's Formula Not Prescribed By Law

(a) The DG is not entitled in law to apply a formula that is not prescribed in

Regulation 46(1) of the GST Regulations in considering an Exceptional ITC Claim. The alleged formula, the DG only allowed JEP's claim for the input tax paid for the furniture and equipment purchased for the continuance of the JEP's business.

(b) In absence of any legal basis, such inconsistency in the DG's Decision would render it liable to be quashed by the Court. As held by the Court of Appeal in ***Ang Sue Khoon v Majlis Bandaraya Pulau Pinang* [2015] MLJU 1866**, an inconsistent decision by an authority may be regarded as unreasonable to the extent of "Wednesbury unreasonableness".

Argument 4 - JEP's Legitimate Expectation

(a) It is trite law that a decision by a public authority may be quashed on the ground that it is in violation of a legitimate expectation as held by the Federal Court in ***Majlis Perbandaran Pulau Pinang and Ketua Pengarah Hasil Dalam Negeri v Latex Manufacturing Sdn Bhd* [2017] 7 MLJ 379** .

This recent decision by the High Court is significant and inviting, since GST has been abolished many are not aware that they may still claim refunds due to them during the GST regime.

(b) The DG's decision is in violation of the JEP's legitimate expectation as it contravenes the DG's express wordings and practices set out in the DG's Guide:

(i) Paragraphs 56 to 59 of the DG's Guide provide that a taxpayer may claim the input tax credit on assets paid before the business is registered under the GST Act provided that the assets are capitalised according to the accounting standard applicable in Malaysia; and

(ii) JEP had capitalised the relevant assets in relation to the Power Plant in which the Disallowed ITC was paid in accordance with the accounting standard.

Conclusion

It must be highlighted that the High Court in delivering the judgment held

that the fact that exceptional input tax credit is labelled as an exceptional one calls for the Court to allow input tax credit claim that has exceptional circumstances - for the businesses to be able to claim GST incurred before being a registered GST person.

This recent decision by the High Court is significant and inviting, since GST has been abolished many are not aware that they may still claim refunds due to them during the GST regime. Despite the Ministry of Finance announcing that the Customs is committed to expedite GST refunds, the Customs remain slow and hesitant to refund taxpayers.

This case further demonstrates that public authority cannot act arbitrarily by committing an error of law or acting beyond its legislative authority by not giving effect to a prescribed law.

Nur Amira binti Ahmad Azhar | *Associate*
Tax, SST & Customs
amira@rdslawpartners.com

IS A CAR PARK A "PLANT"?

AN ANALYSIS OF THE PP CLINIC CASE

by Brandon Chee Ken Wei

The taxpayer's principal activity is in the business of providing healthcare and medical services. On 11.12.2014, the Malaysian Investment Development Authority ("**MIDA**") granted the taxpayer an income tax exemption by way of 100% Investment Tax Allowance pursuant to the Income Tax (Exemption) (No.12) Order 2006 [P.U.(A) 113/2006] ("**Exemption Order 2006**") equivalent to qualifying capital expenditure incurred on the projects for the expansion, modernisation or refurbishments of a private healthcare facility within a 5-year period commencing from 7.4.2010 to 6.4.2015. The said exemption shall adopt the Income Tax (Exemption) Order 2012 [P.U.(A) 22/2012] ("**Exemption Order 2012**"), save for paragraphs 3 and 4(3)(b). In 2012, the taxpayer constructed an extension to its existing hospital building and subsequently made claims for Investment Tax Allowance ("**ITA**") of RM91,421,922 and Industrial Building Allowance ("**IBA**") of RM77,154,982.

In April 2016, subsequent to a tax audit, the Inland Revenue Board ("**IRB**") issued its tax audit findings letter to the taxpayer. Among others, the IRB alleged that the ITA claim on the hospital building expenditures of RM3,267,832 incurred outside the incentive period is not allowed. In addition, the ITA and IBA claims for building expenditures incurred in the year of assessment ("**YA**") of 2012 that are attributable to the car parks are not allowed. The taxpayer responded with detailed explanation stating that the car parks are part of the building as a "qualified project" and industrial building for the purposes of the taxpayer's ITA and IBA claims as the car parks were not specifically excluded from the Gazette Order and the constructed car parks are part and parcel of the new building an integral to the private healthcare facility business of the taxpayer. In July 2016, the IRB maintained its position and issued Notices

of Non-Chargeability to the taxpayer for the years of assessment 2012, 2013 and 2014.

The taxpayer subsequently filed its notices of appeal (i.e. Form Q) to the Special Commissioners of Income Tax ("**SCIT**"). The issues deliberated by the SCIT were, inter alia, whether the capital expenditure incurred by the taxpayer to construct an integrated multi-storey carpark as part of the Gleneagles Penang Hospital is eligible for:

(a) ITA claim pursuant to the Exemption Order 2006 and Exemption Order 2012; and/or

(b) IBA claim pursuant to Paragraph 37A Schedule 3 of the Income Tax Act 1967?

Taxpayer's Contention

Investment Tax Allowance

The taxpayer contended that it had fulfilled all the conditions under the Exemption Order 2006 and was entitled to claim for ITA for the multi-storey car park. Nonetheless, in light of the enforcement of Exemption Order 2012, the taxpayer took note and adopted the following paragraph:

> ***"Exemption***
>
> 4. (1) The Minister exempt a qualifying company in the basis period for a year of assessment from the payment of income tax in respect of statutory income derived from a ***qualifying project*** which is equivalent to the amount of allowance as determined in subparagraph (2).
>
> (2) The amount of allowance referred to in subparagraph (1) shall be one hundred per cent of the ***qualifying capital expenditure*** incurred in the basis period for a year of assessment within a period of five years."

The key terms stated in the above paragraph are **qualifying expenditure** and **qualifying project**. In this regard, Paragraph 2 of the Exemption Order

2012 provides that qualifying capital expenditure means capital expenditure incurred by a qualifying company on an asset used in Malaysia solely for the purpose of qualifying project in relation to a building, the cost of purchasing or constructing new building of an approved standard and that building has been licensed with the Ministry of Health, and registered with the Malaysian Healthcare Travel Council. Paragraph 2 even goes further to include "*expansion, modernisation or refurbishment*".

Based on the above, it is clear that in order to claim ITA on the capital expenditure incurred on the new hospital building, the taxpayer need only satisfy the following:

If Parliament had intended for car parks to be disqualified from the ITA claim under the Exemption Order 2012, it would have been specifically provided in the said provision

(a) the new building is of an approved standard which has been licensed by the Ministry of Health and registered with the Malaysian Healthcare Travel Council;

(b) the claim does not include capital expenditure incurred for the construction of living accommodation; and

(c) the project undertaken is for the expansion, modernisation or refurbishment of an existing private healthcare facility business.

In fact, it was undisputed by the IRB that capital expenditure of the entire hospital building has been allowed except the multi-storey car park. Thus, the only question left for consideration is whether the multi-storey car park is specifically disqualified under the Exemption Order 2012.

In this regard, paragraph 2 of the Exemption Order 2012 in defining "qualifying capital expenditure" has specifically disqualified capital expenditure incurred for living accommodation only, and not for car parks. If Parliament had intended for car parks to be disqualified from the ITA claim under the Exemption Order 2012, it would have been specifically provided in the said provision as held in ***Ketua Pengarah Hasil Dalam Negeri v Success Electronics & Transformer Manufacturer Sdn Bhd* (2012) MSTC 30-039.**

Industrial Building Allowance

The taxpayer argued that the hospital building is an industrial building and the capital expenditure incurred should be allowed for an IBA claim. The only part of the hospital building in dispute is the multi-storey car park.

The taxpayer submitted that the multi-storey car park which are integrated to the hospital building is clearly part of the hospital building, and thus qualifies for capital expenditure. The taxpayer relies on the principles laid down by the High Court in ***Lavender Confectionary & Bakery Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* (2018) MSTC 30-170**, which referred to the case of ***Director General of Inland Revenue v C. Company of Malaysia Bhd* [1980] MTJ 67**, whereby one has to give due consideration to the entirety test and functionality test in determining the nature of the capital expenditure incurred by the taxpayer.

In the *C. Company* case (supra), the learned Special Commissioners applied the "entirety test" in determining the nature of the capital expenditure incurred by the taxpayers. The SCIT held that the road system which links up the factory was integrated with the industrial buildings in the factory complex. It was something necessarily used in connection with the building and without the road system, the factory would not be able to function adequately.

The "*functionality test*", as laid down by the High Court in *Success Electronics*, require the incentives claimed to be determined whether it is necessary and integral to the taxpayer's activity in determining the meaning word 'factory', or in this case the hospital building.

In applying both the "*entirety test*" and "*functionality test*" to the current case at hand, there is no doubt that the construction of the multi-storey car park was integral to the expansion of the taxpayer's existing hospital business in constructing the new hospital building and the multi-storey car park was used in the course of the taxpayer's business. In the event the taxpayer refused to offer additional car parks for its patients, it would heavily reduce the number of patients visiting the taxpayer's hospital services because of the lack or insufficient car park facility.

Lastly, the taxpayer contended that paragraph 66 of Schedule 3 of the ITA 1967 is not applicable in this present matter as this paragraph would only be applicable if there exist parts of a building that is not so used as an industrial building is more than 10% of the building. The multi-storey car park is indeed utilised as an industrial building, which is necessary, integral and forms part and parcel of the hospital building.

The IRB's arguments

In brief, the IRB contends that despite the taxpayer is in the healthcare services and had the relevant interest on the expansion of its hospital building, the expenses incurred and claimed for the multi-storey car park by the taxpayer does not fulfil the requirements of the Exemption Order 2006 and the Exemption Order 2012, and also paragraph 66 of Schedule 3 of the ITA 1967.

The IRB alleged that the taxpayer's claim for ITA and IBA was correctly rejected as the taxpayer had failed to claim for its exemption of income tax on capital expenditure within the period of five (5) years by virtue of Exemption Order 2006, and the Exemption Order 2012 did not supersede nor revoked Exemption Order 2006. Hence, the Exemption Order 2006 was still applicable to the taxpayer.

The IRB further relied on the ground that the taxpayer failed to look at the Exemption Order 2012 as a whole as the multi-storey car park attached to the taxpayer's hospital building is not the main business of the taxpayer.

It was argued by the IRB that the multi-storey car park is not so used as the taxpayer's business is conducted in the main hospital building. The multi-storey car park merely constitutes an extension of the hospital building which is not so used in the taxpayer's healthcare business. Furthermore, as the total surface area of the multi-storey car park constitutes 36.07% of the total build-up area of the hospital building (i.e. more than 10%), the IRB submitted that Paragraph 66 Schedule 3 of the Income Tax Act 1967 is thereby applicable and relevant to the current case at hand.

The SCIT's Decision

Upon hearing the witnesses and submissions of both parties, the SCIT had unanimously allowed the taxpayer's appeal and held that the multi-storey car park in this appeal is part of the hospital built by the taxpayer and is mainly used for the taxpayer's business. Hence, the ITA and IBA claims made by the taxpayer is allowed under the Income Tax Act 1967.

The SCIT looked at the hospital and the multi-storey carpark as a whole, as one body; and function as one building in the same industry. The multi-storey carpark is part of one industrial building, which is the taxpayer's hospital building.

The learned panel of the SCIT looked at the hospital and the multi-storey carpark as a whole, as one body; and function as one building in the same industry. The multi-storey carpark is part of one industrial building, which is the taxpayer's hospital building. There is no doubt that car parks are commonplace in every development, commercial or residential area.

In deliberating whether the multi-storey car park has been used as an industrial building, the learned panel of the SCIT adopted and put to use the "entirety test" and "functionality test". There is no doubt that every part within the hospital has different functions, but they are integral in reaching the main ultimate goal in the industry. In the judgment, the learned panel of the SCIT had even referred to the human body as an example, "We have different parts and have different functions, hand and leg and etc. They all are for one goal. If we lose on leg, our body still can function but not in full and perfect manner and the outcome is the same. The same applies to the hospital and the multi-storey carpark."

On another note, the learned panel of the SCIT took note that the taxpayer had generated rental income in operating the multi-storey car park and such income was subsequently brought to tax by the IRB.

Based on the above, the learned panel of the SCIT had set aside the Notices of Assessment issued by the IRB against the taxpayer for the YAs 2012, 2013, 2014 and 2017.

Conclusion

This decision is similar to another recent case in which the taxpayer successfully argued that multi-storey car parks are considered as a "plant" in the case of ***Ketua Pengarah Hasil Dalam Negeri v Tropiland Sdn Bhd* (2012)**. Taxpayers must take note that when claiming for capital allowance, two questions need to be addressed, First, whether the "plant" or asset is an apparatus; and second, whether the usage or "plant" or asset is integral to the taxpayer's business.

If the asset is an apparatus used in the course of business, and from which the taxpayer generates income, then it should ordinarily qualify as a plant.

Therefore. one must consider the totality of facts and evidence in respect of the functions of an asset in the business. If the asset is the apparatus used in the course of business, and from which the taxpayer generates income, then it should ordinarily qualify as a plant. However, businesses must ensure that these facts are properly documented contemporaneously.

Brandon Chee Ken Wei | *Associate*
Tax, SST & Customs
brandon@rdslawpartners.com

DEDUCTIBILITY OF BUMIPUTERA DISCOUNT PAYMENTS:

AN ANALYSIS OF THE ST CASE

by Nur Hanina binti Mohd Azham

The taxpayer, a property developer, was dissatisfied with the decision of the Special Commissioner of Income Tax ("**SCIT**") in disallowing the taxpayer's appeal to deduct the Bumiputera Discount Payment under Section 33(1) of the Income Tax Act 1967 ("**ITA**"). On 22.9.2020, the High Court ruled in favour of the taxpayer and found that the Bumiputera Discount Payment was in fact deductible under Section 33(1).

Background Facts

The taxpayer's principal activity is the business of property development in Selangor. The taxpayer entered into an agreement with the State Government of Selangor and amongst others, agreed to allocate a percentage of Bumiputera Quota on the shop lot units they wish to build. Despite numerous attempts made to sell the shop lots, the taxpayer was unable to sell the Bumiputera Lots. According to the Agreement with the State Government, if the taxpayer fulfils all the conditions stipulated, the taxpayer can make a contribution to the State Government for the release of the Bumiputera Quota ("**Bumiputera Discount Payment**"). The taxpayer made the contribution and sought for the expenses to be deducted. The Inland Revenue Board ("**IRB**") disallowed the deduction on the grounds that it was capital and penal in nature.

Being aggrieved by the IRB's decision, the taxpayer filed an appeal to the SCIT to challenge the legality of the said decision. During the hearing in April 2018, the IRB focused on the point that the Bumiputera Discount Payment was penal in nature, hence, not incurred wholly and exclusively in the production of income.

The SCIT agreed with the submission of the IRB and held that the taxpayer has breached the State Government's Circular by selling the Bumiputera shop

lots to non-Bumiputera. Having breached the Circular the SCIT further held that the Bumiputera Discount payment was penal in nature and hence, not incurred wholly and exclusively in the production of income and not a deductible expense. Consequently, the taxpayer filed its appeal at the High Court.

The Bumiputera Discount Payment fulfils Section 33(1) of the ITA on the grounds that the Bumiputera Discount Payment is an expense of the taxpayer, it is an expense incurred in the course of the taxpayer's business

Deductibility Of Bumiputera Discount Payment

The primary issue to be determined by the High Court is whether the taxpayer is entitled to claim deduction for the Bumiputera Discount Payment under Section 33(1).

For the purposes of deductibility, so long as a taxpayer fulfils the requirements stipulated in Sections 33(1) and 39(1) of the ITA, the Bumiputera Discount Payment incurred by the taxpayer should be allowed as a deduction. As a general rule, expenditure incurred in the course of business is deductible if it falls under Section 33(1), which is commonly referred to as the "basket provision". This was stipulated in the Court of Appeal's case of ***Aspac Lubricants Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* [2007] 5 CLJ 353**.

The case of ***Margaret Luping & Ors v Ketua Pengarah Hasil Dalam Negeri* [2000] 3 CLJ 409)** held that in order to obtain a deduction under Section 33(1), the following elements must be satisfied:

(a) Outgoings and expenses;
(b) Wholly and exclusively;
(c) Incurred during that period;
(d) In the production of income; and
(e) Not prohibited under Section 39(1) of the ITA.

In this case, the Bumiputera Discount Payment fulfils Section 33(1) of the ITA on the grounds that the Bumiputera Discount Payment is an expense of the taxpayer, it is an expense incurred in the course of the taxpayer's business and the shop office units were the taxpayer's stock in trade and the taxpayer received income from the sale of the shop office units.

The High Court examined whether the Bumiputera Discount Payment was incurred "in the production of income". In ***Director General of Inland Revenue v Kulim Rubber Plantations Ltd*** **[1981] 1 MLJ 214**, the Federal Court examined the phrase as for the purpose of enabling a person to carry on and earn profits in the trade. In this regard, it is evident that the Bumiputera Discount Payment is closely connected to the taxpayer's business based on the following:

I. The taxpayer is in the business of property development. The taxpayer derives his income from the sale of properties;

II. The Bumiputera Discount Payment is clearly a necessary incident for the taxpayer to generate its business income. Under the 2007 Circular, developers who are given release from the Bumiputera quota would need to make a payback of the Bumiputera Discount Payment to the State Government before the transfer of title;

III. The Bumiputera Discount Payment, which is a contribution to the Government for each unit released, or "sumbangan kepada Kerajaan Negeri", is necessary and integral to the taxpayer's business;

IV. The shop office units were the taxpayer's stock in trade and the taxpayer received income from the sale of these units; and

V. The profits made by the taxpayer from the sale of these shop units were brought to income tax by the taxpayer.

Further, the nature of the payment made is not penalty. The taxpayer did not infringe or breach any statutory laws. Pursuant to the Agreement entered with the State Government, the taxpayer was given the option to contribute to the State Government in return for the release of the Bumiputera Lots provided all the conditions were satisfied. However, the SCIT made an erroneous finding that the Bumiputera Discount Payment is not deductible simply because the expense is penal in nature.

The SCIT had clearly failed to recognise that there is no basis for the IRB to aver that the 10% Bumiputera Discount Payment is to penalise taxpayers for the breach of the Bumiputera quota release mechanism. If breaches of the Bumiputera quota release mechanism are already accounted for by the 5% charge, it begs the question as to how the 10% Bumiputera Discount

Payment can also be regarded as to penalise the taxpayer for failure to comply with the express conditions given.

In fact, regardless of whether the taxpayer complies with the Bumiputera quota release mechanism, the taxpayer would have to make the 10% Bumiputera Discount Payment to the authorities if a Bumiputera-allocated unit is sold to a non-Bumiputera. This has been acknowledged by the SCIT. Hence, there was no basis for the IRB to aver that the 10% Bumiputera Discount Payment is penalty for non-compliance with the mechanism.

Be that as it may, the taxpayer submitted that an expense that is penal in nature is still deductible. Section 39(1) of the ITA does not disallow such deduction. Based on the Commonwealth cases cited by the taxpayer, payments in nature of a violation of policy are deductible so long as it complies with Section 33(1) of the ITA. It was observed in ***British Colombia Ltd v Her Majesty The Queen* [1999] 3 SCR 804** whereby the taxpayer was a registered egg producer who decided to produce over-quota due to local market conditions. The Supreme Court of Canada in deciding for the taxpayer held that the levy was incurred as part of the taxpayer's day-to-day operations and the decision to produce over-quota was a business decision made in order to release income.

In a similar case, ***Prima Nova Harta Development Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* (Rayuan No: WA-14-7-12/2019)**, it was held by the High Court that the cash contribution to obtain the release of the Bumiputera lots quota is a deductible expense under Section 33(1) ITA. The High Court further held that by selling the bumiputera lots to non-bumiputeras, it directly generates the taxpayer's income. However, to be able to do so, the taxpayer needs to return the bumiputera discount to the State Government. In such case, the expenses or payments made by the taxpayer are "wholly and exclusively" borne for the purpose of generating income as well as being closely related to the business of the taxpayer and thus, such expenses should be made deductible under Section 33(1) ITA.

Wrong Reliance On The 2011 Circular

In deciding that the Bumiputera Discount Payment was not deductible under Section 33(1), the SCIT had erroneously relied on the 2011 Circular and held that the 2011 Circular completes the 2007 Circular by providing a detailed

Bumiputera quota release mechanism. There is no basis for the 2011 Circular to be read in tandem or in addition to the 2007 Circular since the 2011 Circular is intended to provide for an entirely different mechanism, which is the self-regulatory mechanism.

IRB cannot arbitrarily disallow an expense as a deduction if it is not prescribed under the law.

Further, the 2007 Circular is the only Circular to be referred and not the 2011 Circular as the deduction was made in respect of Year of Assessment 2011 for the financial year ended 30.6.2011 whereas the 2011 Circular only came into effect on 7.9.2011.

In fact, both the taxpayer and the IRB agreed that the applicable circular is the 2007 Circular. Based on the clear opinion of the Privy Council in the case of ***Chua Lip Kong v Director-General of Inland Revenue* [1982] CLJ (Rep) 1**, the Courts are not entitled to go behind this statement which has been agreed by both parties. It was not merely part of the evidence before them which they were either to accept or reject as they thought fit. In this respect, both parties had accepted that the circular applicable to the taxpayer is the 2007 Circular.

Conclusion

In this case, upon hearing the parties, the High Court allowed the taxpayer's appeal. This recent decision is encouraging as it recognises the position that Bumiputera Discount Payments incurred by property developers are indeed in the ordinary course of business and hence, tax deductible. It also shows that the IRB cannot arbitrarily disallow an expense as a deduction if it is not prescribed under the law.

Nur Hanina binti Mohd Azham | *Pupil-in-chambers*
Tax, SST & Customs
nurhanina@rdslawpartners.com

For further information, please contact us:

Datuk D.P. Naban
Senior Partner
+603 6209 5405
naban@rdslawpartners.com

Rosli Dahlan
Partner | Head of Dispute Resolution
+603 6209 5420
rosli@rdslawpartners.com

Ooi Bee Hong
Partner | Head of Corporate and Real Estate Transactions
+603 6209 5401
beehong@rdslawpartners.com

S. Saravana Kumar
Partner | Head of Tax, SST & Customs
+603 6209 5404
sara@rdslawpartners.com

Ong Eu Jin
Partner | Head of Capital Markets and M&A
+603 6209 5488
eujin@rdslawpartners.com

Tan Gek Im
Partner
+604 370 1122
gekim@rdslawpartners.com

Chia Loong Thye
Partner
+604 370 1122
ltchia@rdslawpartners.com

Rosli Dahlan Saravana Partnership is a full-service commercial firm focusing on the following practice areas:

- **Appellate Advocacy**
  DP Naban
  naban@rdslawpartners.com
  Rosli Dahlan
  rosli@rdslawpartners.com

- **Banking & Finance (Conventional and Islamic)**
  Ong Eu Jin
  eujin@rdslawpartners.com
  Tan Gek Im
  gekim@rdslawpartners.com

- **Capital Markets (Debt & Equity)**
  Ong Eu Jin
  eujin@rdslawpartners.com

- **Civil & Commercial Disputes**
  DP Naban
  naban@rdslawpartners.com
  Rosli Dahlan
  rosli@rdslawpartners.com

- **Competition Law**
  Ooi Bee Hong
  beehong@rdslawpartners.com
  Annabel Kok Keng Yen
  annabel@rdslawpartners.com

- **Construction and Arbitration**
  DP Naban
  naban@rdslawpartners.com
  Rosli Dahlan
  rosli@rdslawpartners.com

- **Corporate and Commercial**
  Ooi Bee Hong
  beehong@rdslawpartners.com
  Tan Gek Im
  gekim@rdslawpartners.com

- **Corporate Fraud**
  DP Naban
  naban@rdslawpartners.com
  Rosli Dahlan
  rosli@rdslawpartners.com
  Yeow Wei Jien
  weijien@rdslawpartners.com

- **Employment & Industrial Relations**
  DP Naban
  naban@rdslawpartners.com
  Rosli Dahlan
  rosli@rdslawpartners.com
  Louis Liaw Vern Xien
  louis@rdslawpartners.com

- **Energy, Infrastructure & Projects**
  DP Naban
  naban@rdslawpartners.com
  Rosli Dahlan
  rosli@rdslawpartners.com
  Kenny Lam Kian Yip
  kenny@rdslawpartners.com

- **Fintech**
  Ooi Bee Hong
  beehong@rdslawpartners.com
  Annabel Kok Keng Yen
  annabel@rdslawpartners.com

- **Government & Regulatory Compliance**
  Rosli Dahlan
  rosli@rdslawpartners.com
  Ooi Bee Hong
  beehong@rdslawpartners.com

- **Intellectual Property**
  DP Naban
  naban@rdslawpartners.com
  Kenny Lam Kian Yip
  kenny@rdslawpartners.com

- **Medical Negligence**
  DP Naban
  naban@rdslawpartners.com
  Hayden Tan Chee Khoon
  hayden@rdslawpartners.com

- **Mergers & Acquisitions**
  Ooi Bee Hong
  beehong@rdslawpartners.com
  Ong Eu Jin
  eujin@rdslawpartners.com

- **Personal Data Protection**
  Ooi Bee Hong
  beehong@rdslawpartners.com
  Annabel Kok Keng Yen
  annabel@rdslawpartners.com

- **Real Estate Transactions**
  Ooi Bee Hong
  beehong@rdslawpartners.com
  Ong Eu Jin
  eujin@rdslawpartners.com
  Tan Gek Im
  gekim@rdslawpartners.com
  Chia Loong Thye
  ltchia@rdslawpartners.com
  Annabel Kok Keng Yen
  annabel@rdslawpartners.com

- **Shipping & Maritime**
  DP Naban
  naban@rdslawpartners.com

- **Tax Incentives**
  S. Saravana Kumar
  sara@rdslawpartners.com

- **Tax, SST & Customs**
  DP Naban
  naban@rdslawpartners.com
  S. Saravana Kumar
  sara@rdslawpartners.com

- **Trade Facilitation**
  S. Saravana Kumar
  sara@rdslawpartners.com

- **Wills and Estate Administrations**
  Tan Gek Im
  gekim@rdslawpartners.com

RDS
ADVOCATES & SOLICITORS

Level 16, Menara 1 Dutamas, Solaris Dutamas
No. 1 Jalan Dutamas 1, 50480 Kuala Lumpur, Malaysia
Tel: +603 6209 5400
Fax: +603 6209 5498

21st Floor, Menara Northam,
No. 55, Jalan Sultan Ahmad Shah,
10050 Penang, Malaysia
Tel: 04-370 1122
Fax: 04-370 5678