

## High Court Quashes RM78.6 Million Tax Assessments, Rejects Revenue's Ownership Test For Shipping Tax Exemption

14 October 2026

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Recently, the High Court in *AM v Ketua Pengarah Hasil Dalam Negeri* quashed tax assessments and penalties totalling over RM78.6 million issued against a Malaysian shipping company.

The High Court allowed the taxpayer's judicial review application and found, amongst others that the Revenue had applied the wrong test in assessing ownership by treating financing, management and insurance arrangements as additional conditions of ownership, and that its decision was tainted by an error of law.

The taxpayer was successfully represented by the firm's Tax, SST & Customs Partner, S. Saravana Kumar together with Senior Associate, Dharshini Sharma and Pupil, Yuna Ng.

### Background

The taxpayer for the purposes of its business has purchased 16 vessels (Subject Vessels), all of which were duly registered as Malaysian ships under the Merchant Shipping Ordinance 1952 (MSO). The taxpayer had claimed the shipping profits tax exemption under Section 54A(1)(b) of the ITA and capital allowances under Schedule 3 of the ITA in respect of the Subject Vessels for the YAs 2007 to 2023.

Following a tax audit, the Revenue issued tax assessments disallowing the tax exemptions and capital allowances claimed by the taxpayer on the basis that the taxpayer was not the true owner of the Subject Vessels.

Consequently, the taxpayer commenced judicial review proceedings in the High Court to challenge the lawfulness of the tax assessments.

## **Taxpayer's Case**

The taxpayer advanced several grounds in challenging the tax assessments:

### Legal Title And MSO Registration

The taxpayer submitted that ownership of a "Malaysian ship" under Section 54A(1)(b) of the ITA is established by registration under the MSO. The taxpayer produced various documentary evidence such as the Certificates of Registry, Memorandums of Agreement, Bills of Sale, and Ship Transcripts to establish ownership.

Relying on *Ketua Pengarah Hasil Dalam Negeri v Labuan Ferry Corporation Sdn Bhd*, the taxpayer contended that MSO registration is the decisive criterion for a vessel qualifying as a 'Malaysian ship' for the purposes of the Section 54A exemption. The taxpayer further relied on *Director General of Inland Revenue v Teo Tuan Kwee* and *CIMB-Principal Asset Management Bhd v Ketua Pengarah Hasil Dalam Negeri* for the proposition that 'owner' for tax purposes is not confined to bare legal title and encompasses beneficial ownership.

### No Extra-Statutory Rules

The taxpayer argued that Section 54A of the ITA does not import any financial or commercial tests such as source of funds, group financing arrangements or corporate control.

Relying on *Ketua Pengarah Hasil Dalam Negeri v OKA Concrete Industries Sdn Bhd* and *National Land Finance Co-operative Society Ltd v Director General of Inland Revenue*, the taxpayer submitted that taxing provisions must be construed strictly and that the Revenue is not entitled to rewrite the statute by reading in requirements that Parliament did not intend.

### Commercial Financing

The taxpayer further contended that intercompany financing provided by its foreign parent company was a standard commercial arrangement. Merely utilising intercompany loans does not negate legal or beneficial ownership.

### Judicial Review Remains Available

The taxpayer submitted that its filing of a Form Q appeal with the Special Commissioners of Income Tax (SCIT) did not extinguish its right to judicial review. Relying on the Federal Court decisions in *Ketua Pengarah Hasil Dalam Negeri v Kind Action (M) Sdn Bhd* and *Mohd Najib bin Hj Abd Razak v Government of Malaysia*, the taxpayer contended that the existence of a domestic remedy is not a complete bar to judicial review where exceptional circumstances, including illegality, are shown.

## The Revenue's Position

The Revenue resisted the judicial review application on the following grounds:

### Availability Of Alternative Remedy

The Revenue argued that judicial review was not the right avenue of appeal because the taxpayer had an alternative statutory remedy via an appeal to the SCIT under Section 99(1) of the ITA. It maintained that the issue of ownership was a mixed question of fact and law falling within the jurisdiction of the SCIT and there was a need to tender more documentary evidence and cross examine witnesses.

### Totality Of Evidence

On the substantive question of ownership, the Revenue contended that registration under the MSO alone was insufficient to satisfy the statutory wording of "owned by him" under Section 54A(1)(b) of the ITA, as reading registration as conclusive would render those statutory words superfluous. True ownership must be determined by looking at the totality of the evidential matrix, taking into account the registry, acquisition, financing, control, insurance policies and conduct of the parties.

The Revenue relied on the fact that the foreign parent company had funded the acquisitions and contended that the taxpayer was therefore not the beneficial owner of the Subject Vessels as the parent company could "control" the taxpayer.

## High Court's Decision

The High Court allowed the judicial review application and granted an order of certiorari quashing the disputed tax assessments, together with declarations that the taxpayer was the owner of the Subject Vessels and that the Revenue had no legal or factual basis to disallow the exemption and capital allowance claims.

### Availability Of Judicial Review

The court noted that while judicial review is generally not readily available where a statutory remedy exists under the ITA, this does not automatically preclude judicial review in tax cases as recognised by the Federal Court in *Mohd Najib bin Hj Abd Razak v Government of Malaysia*.

In line with the principles set out in the *Government of Malaysia v Jagdis Singh* and *Ketua Pengarah Hasil Dalam Negeri v Kind Action*, judicial review remains available where a taxpayer is able to demonstrate the presence of exceptional circumstances. Such circumstances were satisfied on the facts, given that the dispute turned on a pure question of law, namely whether the Revenue has any legal basis to disallow the taxpayer's income tax exemption under Section 54A and its capital allowance claims under Schedule 3 of the ITA on the basis that the taxpayer was not the owner of the vessels.

### The Ownership Test

The court further noted that the main issue was whether the Revenue had applied the correct test in assessing ownership and whether the financial arrangements provided a lawful basis to disregard registered documentation relating to the Subject Vessels.

In this regard, the court held that although the Revenue was entitled to examine financing, management, insurance, and corporate arrangements, it was not entitled to treat those arrangements as additional conditions of ownership or as sufficient to displace the legal effect of relevant acquisition instruments.

Accordingly, the court found that the Revenue's disallowance was tainted by an error of law and was therefore unlawful.

### Outcome

This decision reaffirms the position that the Revenue cannot introduce extra-statutory operational or financial requirements to override valid legal title and registration documents pursuant to the MSO when determining ship ownership under the ITA.

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