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Definition Of Plant For Capital Allowance: The Effect Of Paragraph 70A

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Taxpayers may claim capital allowance on the capital expenditure incurred for plant and machinery. Previously, there was no specific definition for the term plant under the Income Tax Act 1967 (ITA). Taxpayers were guided by the legal principles established in case law.

Recently, Section 28(a) of the Finance Act 2020 introduced a new paragraph 70A into Schedule 3 of the ITA, which reads as follows:

> *"In this Schedule, "plant" means an apparatus used by a person for carrying on his business but does not include a building, an intangible asset, or any asset used and that functions as a place within which a business is carried on."*

This alert examines the legal position of what constitutes as a plant for capital allowance purposes by analysing the approach taken by the courts in the past and the new paragraph 70A.

Before The Introduction Of Paragraph 70A

Traditionally, tax practitioners and tax officers look to the courts for guidance on the definition of plant. In the celebrated case of *Yarmouth v France*[1], the English court defined plant as the following:

> "*in its ordinary sense, it includes whatever apparatus is used by a business man for carrying on his business – not his stock in trade which he buys or makes for sale, but all goods and chattels, fixed or moveable, live or dead, which he keeps for permanent employment in his business".*

This definition has been long applied in Malaysia and this is evident from leading cases on capital allowance claim such as

[1] (1887) 19 QBD 647

REIMAGINING TAX SOLUTIONS

Ketua Pengarah Hasil Dalam Negeri v Tropiland Sdn Bhd[2] and *Infra Quest Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri*[3]. Our Senior Partner, Datuk D.P. Naban and Tax, SST & Customs Partner, S. Saravana Kumar successfully represented the taxpayers in *Tropiland* and *Infra Quest*.

In *Tropiland*, the taxpayer claimed capital allowance for the expenses incurred for the construction of a multi-storey carpark. The Court of Appeal ruled that the multi-storey carpark was a qualifying plant and largely adopted the approach taken in the case of *Yarmouth*. The Court considered a plethora of tests to determine if a subject matter is a qualifying plant such as the "premise" test, "business use" test and the "functional" test.

Furthermore, *Tropiland* provided several illuminating principles to aid in the court's assessment of whether a subject matter is a qualifying plant. The Court held that the categories of what constitute plant and machinery are not closed. It is apparent that the phrase is to be interpreted widely and holistically. The Court acknowledged that it must give due consideration to the particular industry concerned and take the specific circumstances of the individual taxpayer's own business into account when determining whether an apparatus is a qualifying plant. It is crucial to look at the taxpayer's business in its entirety instead of taking particular facts in isolation and consider whether the taxpayer could generate income without the apparatus.

Meanwhile, in *Infra Quest*, the High Court held that telecommunication towers were plant and commented that:

> *"This court is of the considered opinion that in distinguishing between the functional use and the setting, it must be noted that in some cases, buildings and structures have been held to be plant in their entirety as the courts considered the structures as performing an integral function with the machinery and plant contained within it."*

[2] (2013) MSTC 30-054
[3] [2016] MLJU 624

In allowing the taxpayer's appeal, the court held that the Special Commissioners of Income Tax had erred in its decision in failing to take into account of the Inland Revenue Board's lack of consideration of the entire business operations of the taxpayer in a holistic manner, particularly on the functions, specific circumstances and purposes of the purpose-built towers. Without the telecommunication towers, the business of the taxpayer could not function or be conducted. The High Court's decision was subsequently affirmed by the Court of Appeal.

Paragraph 70A Of Schedule 3

Whilst it is apparent that some part of paragraph 70A was drafted based on the wordings from *Yarmouth*, paragraph 70A significantly narrowed the scope of plant. The wordings of paragraph 70A now expressly excludes *buildings*, *intangible assets,* and *places where the business is carried out* from the definition of plant. These exclusions are contrary to the position previously held by our courts.

1. The Exclusion Of Building

The Court of Appeal in *Tropiland* previously opined that the multi-storey carpark cannot be discounted from the definition of plant simply because it is a large structure that can be characterised as a building. The exclusion of building as a plant does not only contradict the judgment in *Tropiland* but it also contradicts the definition of building in Section 2 of the ITA, which is defined as:

> *"any structure erected on land (that is not plant or machinery)"*

It is clear from the wording in Section 2 that building is not precluded from being a plant simply because it is a large structure. On the other hand, the new paragraph70A is trying to restrict the meaning of plant. While this may be a cause of concern, some solace can be found in the Supreme Court case of *National Land Finance Co-Operative Society Ltd v Director General of Inland Revenue*[4] which held that where the meaning of the statute is unclear and/or ambiguous, the ambiguity must be interpreted in favour of the subject.

[4] [1993] 4 CLJ 339

2. Exclusion Of Intangible Assets

In *Ketua Pengarah Hasil Dalam Negeri v CIMB Bank Berhad*[5], it was decided that core deposits and customers' credit card databases (Databases) were qualifying plants. Despite the subject matter's virtual and intangible characteristics, the Court found that the Databases were important apparatus for the taxpayer's banking business with due considerations to the principles in *Yarmouth.*

Despite *CIMB Bank* case having previously decided that databases were capable of being considered as qualifying plant, this is no longer the position as the new paragraph 70A expressly excludes intangible assets. The exclusion of intangible asset seems to contradict the recent tax incentives such as the Income Tax (Accelerated Capital Allowance) Information and Communication Technology Equipment) Rules 2018 and Income Tax (Capital Allowance) (Development Cost For Customised Computer Software) Rules 2019. These rules allow for accelerated capital allowance for investments in relation to information communication technology. The exclusion of intangible assets as plant via paragraph 70A surely makes these Rules redundant.

Commentary

It is now difficult to envisage whether cases such as *Tropiland*, *Infra Quest* and *CIMB Bank* would have been decided in a similar fashion today if they were to be decided in light of paragraph 70A of Schedule 3. The case of *Tropiland* is exemplary in illustrating the advantage of having a broad definition of plant and the Court of Appeal clearly acknowledges the need to interpret the phrase holistically for decision to be made with commercial sense. It is now uncertain as to how the courts would interpret these new set of provisions as the *prima facie* interpretation of the paragraph 70A seems to sit indifferently from the approach previously taken by the courts in the preceding cases.

It is apparent that the legal setting has now shifted towards a narrower definition of plant. The introduction and implementation of paragraph 70A did not effectively define the

[5] (2019) MSTC 30-301

definition of plant; instead, it imposes a more restrictive meaning to the concept.

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