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Greetings from
Deloitte Malaysia Tax Services

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Inland Revenue Board

Takeaways:

1. Public Ruling No. 12/2017: Appeal against an Assessment and Application for Relief
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Upcoming events:

1. *Industry 4.0: Future of manufacturing*

Important deadlines:

Task	2018 Due Date	
	28 February	**1 March**
1. 2019 tax estimates for companies with March year-end		√
2. 6th month revision of tax estimates for companies with August year-end	√	
3. 9th month revision of tax estimates for companies with May year-end	√	
4. Statutory filing of 2017 tax returns for companies with July year-end	√	
5. Due date for 2018 CbCR notification for companies with February year-end	√	

Public Ruling No. 12/2017: Appeal against an Assessment and Application for Relief

On 12 January 2018, the Inland Revenue Board (IRB) uploaded on its website Public Ruling (PR) No. 12/2017 (issued on 29 December 2017) to replace PR No. 7/2015. The PR No. 12/2017 was issued mainly to provide information on the provisions that came into force on 1 January 2017:

i. Appeals and relief application against non-taxable cases under Section 97A of the Income Tax Act 1967 (the ITA); and

ii. The relief application not in respect of error or mistake under Section 131A of the ITA.

Various examples have also been provided in PR No. 12/2017.

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NMA Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri (KPHDN) (Special Commissioners of Income Tax)

Issues:

Whether the amount of RM2,879,997 incurred by the taxpayer in year of assessment (YA) 2012 which relates to the acquisition of the business of NM Corporation Berhad (NMC) was deductible in the computation of chargeable income of the taxpayer pursuant to Section 33(1) of the ITA.

Decision:

The Special Commissioners of Income Tax (SCIT) dismissed the appeal by the taxpayer on the following grounds:

1. The term loan from EON Bank taken by the taxpayer was for the purpose of acquiring the business of NMC along with NMC’s assets and liabilities, and the term loan was guaranteed by a Standby Letter of Credit (SBLC) from the DBS Bank.

   The SBLC was related to the term loan taken by the taxpayer for the acquisition of NMC's business. If the taxpayer defaulted in the repayment of loan from EON Bank, the DBS Bank would be liable for the repayment of the term loan. Put simply, the RM2,879,997 expenses claimed by the taxpayer on the SBLC (i.e., commissions for SLBC which was a loan guarantee, indulgence fee for early repayment and early repayment charges) were all related to the term loan taken by the taxpayer for the acquisition of NMC's business including its assets and liabilities.

   Hence, the direct expenses incurred for the SBLC (i.e., RM RM2,879,997 claimed by the taxpayer as a deduction) was capital in nature and was not wholly and exclusively incurred in the production of income and therefore, not claimable under Section 33(1) of the ITA.

2. Based on the oral evidence, documents and written submissions adduced by both the taxpayer and the IRB, the SCIT found that the taxpayer had failed to prove his case on the

balance of probabilities in accordance with Paragraph 13, Schedule 5 of the ITA. Thereby, the SCIT unanimously dismissed the taxpayer's appeal.

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D Bank Berhad v Ketua Pengarah Hasil Dalam Negeri (KPHDN) (Special Commissioners of Income Tax)

Issues:

1. Whether the taxpayer was entitled to claim capital allowance on the capital expenditure incurred by the taxpayer in his acquisition of S Bank Berhad (SBB) Group of Companies' databases (i.e., core deposit and credit card customers database valued at RM263,612,000 and RM153,091,000 respectively) under Schedule 3 of the ITA; and

2. Whether the imposition of penalty by the IRB on the taxpayer under Section 113(2) of the ITA for the YAs 2006 and 2007 was correct in law and, if so, whether the penalties are reasonable and warranted.

Decision:

In a majority opinion, the Special Commissioners of Income Tax (SCIT) allowed the appeal by the taxpayer on all issues with the following grounds of judgement:

Issue 1

1. The word "plant" is not defined in the ITA and consequently the SCIT has been given the wide power to ascertain the meaning of "plant" based on the facts of the case. The word "plant" ought to be given the widest possible sense and its use should not be confined. The category of "plant" ought to be more open and be allowed to grow in line with time and the SCIT must view and assess the taxpayer's trade (as a whole) in determining the meaning of "plant". As long as the asset fulfilled the functional test, where the asset forms part of the tools used in the taxpayer's trade, it is sufficient, irrespective of whether the assets were tangible or not. Intangible assets, e.g., "know-how" and processing data have had been held as "plant". Therefore, the taxpayer's databases ought to be included in the meaning of "plant" and the claim for capital allowance under Schedule 3 of the ITA must be allowed.

2. Under the principles of statutory interpretation, a court is not entitled to read words into legislation or statute. If the provision is unclear or ambiguous, then the person ought not to be taxed and if there exists ambiguity in a provision of taxing law, the benefit of doubt must be given to the taxpayer.

3. The IRB had concluded that the databases were simply in the nature of "goodwill" and referred to "goodwill" only. The SCIT found that "goodwill" is defined in the Shorter Oxford English Dictionary (6th Edition) as "the established custom or popularity of a business (a sum paid for) for privilege, granted to the purchaser by the seller of a business, of trading as the recognised successor of the seller". In the view of the SCIT the databases allegedly only contained SBB's customers' information and did not amount to merely "goodwill" as the databases did not only refer to the goodwill, reputation or popularity of the business. It is also noted that the databases and the goodwill were separately referred to and were placed

next to each other in the taxpayer's balance sheet. Therefore, it was clear that the databases were not "goodwill".

4. Further, the information and data of more than 330,000 credit card holders and depositors obtained from SBB had been used in the taxpayer's business. With the information, the taxpayer was able to earn more income and gain profit at a higher rate by selling the products and offering new loans. Hence, the SCIT found that the database was an important tool for the taxpayer to carry out its banking business and it had played a useful and functional role in the taxpayer's banking business. In the circumstances, the database had fulfilled the functional test as it had been an important tool in the taxpayer's banking business.

5. The IRB's contention on the issue of "setting" (i.e., that the databases were merely a "setting") against the taxpayer was dismissed by the SCIT as the evidence was found to be an afterthought of the IRB. The SCIT found that the issue was only raised in the IRB's written grounds (i.e., during the trial of the case) and not any time before this. Apart from this, based on Shorter Oxford English Dictionary, "settings" was defined as "a person's or thing's immediate environment or surroundings"; the taxpayer's database thereby did not fall under the meaning of "environment or surroundings".

6. The intangible assets such as law books, paintings, patterns, charts, plan and data processing could also be classified as "plant". In this case what was important was that the assets successfully fulfilled the functional test wherein their presence in various forms of tools assisted the taxpayer in the conduct of his banking business. Therefore, the IRB's contention that the presence of databases did not help the taxpayer in his banking business was dismissed by the SCIT.

7. In order to obtain capital allowance, a person has to expend an amount before he is allowed to claim for capital allowance. The taxpayer had never expended any amount to obtain his own database or one that he would own in the future. Thereby, there was no issue as to why the taxpayer did not claim capital allowance for his own database and only applied for capital allowance for databases obtained from SBB.

Issue 2

1. On receiving a relief application under Section 131(1) by the taxpayer, the IRB was required to conduct an inquiry or investigation as Section 131(2) has placed a burden and responsibility on the IRB with the words "shall inquire"; the IRB will then make a fair and reasonable decision on the taxes that have been paid by the taxpayer. In these circumstances, the IRB needs to review and reassess carefully the taxpayer's application and seek clarification from the taxpayer if necessary. The IRB's failure to do so had resulted in taxpayer being denied of his rights to claim for capital allowance under Schedule 3 of the ITA and subjected to penalty under Section 113(2) of the ITA. The IRB had also failed to notify his decision to the taxpayer's application under Section 131(1).

2. The IRB made an error in imposing a penalty on the taxpayer as the assessments for the YAs 2007 and 2008 were made after the IRB allowed the taxpayer's application under Section 131(1) and granted a relief for the YA 2006 to claim capital allowance on the capital expenditure incurred in acquiring the databases. Further, the taxpayer's tax refunds for the YA 2006 had already been made. Hence, the SCIT found that the IRB had failed to take into account all factors, specifically, the fact that the taxpayer had been given a relief under

Section 131(2) after a detailed investigation by the IRB and after the tax credit was refunded to the taxpayer for the YA 2006. Based on the IRB's decision for YA 2006, the taxpayer subsequently filed revised tax computations for the YAs 2007 and 2008. The SCIT found that the taxpayer had never intended to deceive or confuse the IRB. The SCIT therefore dismissed all the contentions put forward by the IRB on this issue.

3. The IRB had never informed or adduced any grounds or explanation to the taxpayer as to why the penalty was imposed for the YAs 2006 and 2007. The burden of proof on the imposition of penalty by the IRB under Section 113(2) of the ITA was on the IRB. However, the IRB had failed to adduce any evidence to show that the taxpayer had dishonest intention and had negligently produced the incorrect and inaccurate return forms or had produced incorrect information to the IRB. Therefore, the SCIT rejected the reasons given by the IRB for the imposition of penalty against the taxpayer. Following that, the IRB was found to have failed to prove the essence of Section 113(2) of the ITA against the taxpayer and in the circumstances, there should not have been any penalty imposed on the taxpayer.

4. The IRB had imposed the same penalty as what was contained in the "Tax Audit Framework" produced by the IRB (i.e., 45%). The SCIT found that the imposition of penalty was in contravention wherein the IRB ought to have considered all the relevant factors and the surrounding circumstances of the case before any penalty could be imposed. The IRB had failed to exercise its discretion in accordance with the facts and the circumstances of the case and merely complied with the Tax Audit Framework. Hence, the IRB was found to have acted mechanically against the taxpayer in the imposition of 45% penalty.

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