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TECHNICAL

Direct Taxation

TAX CASE UPDATE

Power of the DGIR to impose penalty under S112(3) of the ITA

YUNG LUNG HOLDINGS SDN BHD v KPHDN

High Court in Sarawak at Kuching
Appeal No: KCH-14-2/12-2015

Date of Judgment: 4 May 2016
Date of Delivery of Decision: 25 April 2016

Facts and Issues:

This is the appeal against the decision of the Special Commissioners of Income Tax (SCIT) who affirmed the decision of the Director General of Inland Revenue (DGIR) to impose a penalty of RM85,212.20 against the company ("the taxpayer") for inadequate payment of tax assessed for the year of assessment (YA) 2010.

The taxpayer, Yung Lung Holdings, is a company with diverse business interests, including property development and supply of machinery parts. The penalty imposed for YA 2010 was based on 20% of the tax assessed (RM426,061). However, the taxpayer had paid an amount of RM245,000 by 7.11.2011, i.e. before the final due date for submitting the Return Form for YA 2010, which is 31.7.2011. The company's estimated tax payable submitted via Form CP204 on 10.11.2009, was RM37,000. This was revised to RM245,000 via submission of Form CP204A.

The DGIR decided to impose penalty at 20% of tax assessed, and not on the difference between the tax assessed and the amount paid in advance by the company (RM245,000). The taxpayer was dissatisfied with the imposition of the penalty on the assessment for the YA 2010 and appealed to the SCIT, who affirmed the decision of the DGIR.

The taxpayer then appealed to the High Court ("the Court"). The issues for determination are:

1. Whether the finding of the SCIT that the assessment by the DGIR under S90(3) of the Income Tax Act 1967 (ITA) is correct in facts and law. (All sections cited hereafter refer to sections in the ITA, unless otherwise stated.)
2. Whether the penalty of RM85,212.20 imposed under S112(3) for late submission is correct in law.
3. Whether the penalty of 20% of tax assessed is justified in law.

Decision:

Appeal dismissed. The grounds of decision are summarized below:

1. The following sections of the ITA are quoted as being "the relevant sections" governing the DGIR's power to assess the tax due from the taxpayer:

i. Section 112(3)

ii. Section 90(3)

iii. Section 77A(1)

2. The relevance of S77A is given emphasis as the taxpayer was late in submitting its income tax return for YA 2010. In accordance with S77A(1) the company was required to submit its tax return within 7 months after the close of the company's accounting period (1.1.2010 to 31.12.2010), i.e. by 31.7.2011, but the return was only submitted on 7.1.2012 by way of e-filing. It is stressed that S77A is specifically mentioned in both S90(3) and S112(3), and "*these 2 sections are therefore the governing provisions upon which the DGIR must exercise his power to assess the company's chargeable income as well as the penalty to be imposed for the late filing of the said return*."

3. Counsel for the taxpayer had submitted that "*the assessment of tax cannot be made under section 90(1) and (2) because the said section only applies to a taxpayer who has not filed a return*…" This argument cannot be upheld because the words – "…*has not furnished a return* ***in accordance with section 77 or 77A***…" found in S90(3) – conveys the clear meaning (in the context of this case) of compliance with the timeline prescribed by S77A on the due date for submission of the tax return. This approach to the interpretation of statute is based on the "principle of strict interpretation" which is mentioned by the Supreme Court in *National Land Finance Co-operative Society Ltd v DGIR [1994] 1 MLJ99*. Based on this principle the Court is inclined to give effect to the literal meaning of the words in the said section.

.4. Based on the same principle mentioned above, the same interpretation is accorded to S112(3) which employs the same words – "….*default in furnishing a return* ***in accordance with subsection 77(1) or 77A(1)****…*." This means that the DGIR is empowered in the context of this case, to impose the penalty for the company's failure to comply with the timeline of 7 months prescribed by S77A(1). This the DGIR is allowed to do because it is not disputed that the company was not prosecuted for the failure to comply with the timeline specified in S77A(1).

5. The company contended that the penalty was "not fair" because it had paid the sum of RM245,000 in advance. However, the Court cannot accede to the contention that the penalty should be based on the difference between the tax payable and the tax already paid because that is not what S112(3) expressly or even impliedly provides. There is no ambiguity in that section which (if there was any) must be resolved in the taxpayer's favour.

6. The company's counsel had also submitted that S112(1) is a compounding provision and not a tax assessment provision. The following submission of the taxpayer is quoted verbatim in the judgment:

> *"…..In this section [S112(3)], the respondent may require a taxpayer to pay a penalty if the respondent decides not to prosecute him in court for the offence committed under section 112(1). Section 112(3) states that "If no prosecution under subsection (1) has been instituted in respect of the offence committed, the respondent may require him to pay the penalty prescribed under section 112(3)"*

However, on examination of S112(3), the word "if" (underlined) is not found. The word actually used is "and" and the Court is of the view that the company's contention based on the (wrong) word ("if") is misleading. The said sub-section, "pure and simple", empowers the DGIR to impose penalty to a maximum of 3 times the amount of tax **when** there is no prosecution for the failure to comply with S77(1), S77A(1) and S77(3) and not "if" there was none.

7. Based on the facts recorded by the SCIT, the company was a repeat offender (the same offence was committed for 1991, 2007 and 2009, and the DGIR had "*in fact been very lenient*" towards the company in the exercise of his power under S112(3).

Based on the above reasons, the appeal was dismissed.

Members may read the full Grounds of Judgment at the Institute's website and the LHDNM website.