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TECHNICAL

Direct Taxation

TAX CASE UPDATE

Claim of Reinvestment Allowance on capital expenditure on Non-Promoted Products by a company with a Pioneer Certificate

OPTO SENSORS SDN. BHD. v KPHDN

High Court of Malaya at Kuala Lumpur
Civil Appeal No: R1-14-01-2010
Date of Judgment: 8 October 2010

Facts and Issues:

This is an appeal by the appellant (the Taxpayer) against the decision of the Special Commissioners of Income Tax (SCIT) who had dismissed the Taxpayer's appeal against additional assessments raised by the respondent (DGIR) for the years of assessment (YA) 1998, 1999, and 2000(Current Year).

The issues for determination was summarized in the following statement by the SCIT:

> "*whether the Appellant is entitled to claim RA on capital expenditures incurred in respect of non-promoted products of the company, notwithstanding the Appellant had been granted pioneer status under PIA for its promoted products*."

The facts found by the SCIT include the following:

- The Taxpayer was incorporated in Malaysia in 1994 with the principle activities of manufacturing opto electronic products, printed circuit assemblies, computer peripherals and other related products, and servicing of x-ray machines for baggage inspection system.
- The Taxpayer was granted a manufacturing licence for the products shown below. In January 1995 the Taxpayer applied to the Malaysian Industrial Development Authority (MIDA) for pioneer status (PS) of these products, and was granted PS for some of the products (Promoted Products), as indicated below:

Products granted Manufacturing Licence	
Promoted Products (PP)	*Non-Promoted Products (NPP)*
X-ray scanners/systems, Pulse Oximeters	Optical Mice, Optical Sensors, Musical interface devices

- MIDA issued a pioneer certificate (PC) dated 15.6.1996 to the Taxpayer for the PP. Production day of the PS was fixed on 1.8.1996.
- The Taxpayer continued to manufacture the NPP, even though they were not granted PS.
- For the years of assessment under appeal, the Taxpayer reported profits for both the PP and

the NPP.

- The Taxpayer claimed reinvestment allowance (RA) of 60% on the capital expenditure incurred on the NPP for YA 1998, 1999 and 2000(CY). RA was initially granted by the DGIR but in 2004, the RA claims were disallowed on the basis that the Taxpayer is not entitled to RA as it has been granted PS under the Promotion of Investments Act 1986 (PIA).
- The DGIR then raised additional assessments for YA 1998, 1999 and 2000(CY).

The Taxpayer appealed against the above assessments to the SCIT, who dismissed the appeal. The SCIT decided, *inter alia* that the Taxpayer, being a pioneer company, is prohibited by Para. 7(a)(ii) Sch. 7A of the Income Tax Act 1967 (ITA) from claiming RA under Para. 1 of Sch. 7A. The taxpayer cannot enjoy incentives under the PIA simultaneously with RA under Sch. 7A of the ITA. (All sections cited hereafter are from the ITA unless otherwise stated.)

The Taxpayer then appealed to the High Court (the Court). The issue is whether the SCIT is correct in its interpretation of Para. 7(a)(ii) and its finding that the Taxpayer, having been granted a PC under the PIA, comes within the provisions of that paragraph and is therefore excluded from claiming RA.

Decision:

Appeal dismissed. The grounds of decision are summarized below:

1. **Submissions**

1.1 The following are arguments submitted for the Taxpayer:

- It is submitted that wordings of Para. 7(a) of Sch. 7A allows the Taxpayer to claim RA on the NPP because that paragraph only precludes RA from being extended to PP.
- Support for the above submission is based on the High Court case of *Syarikat Kion Hoong Cooking Oil Mills Sdn Bhd v KPHDN* (Tax Appeal No. 14-01-2005-1). In that case, the respondent had submitted that Para. 7(a)(ii) is an exclusion clause based on the status of the company and not on the status of the products it manufactures. However, the learned Judge (in that case) held that on a proper interpretation of Para. 7(a)(ii), that paragraph must be read as a whole in the context in which it appears. "(T)he company" that is excluded from enjoyment of RA is described not merely as the company which has been granted a PC, but as the company which has been granted a PC "in respect of a promoted activity or promoted product." If it is interpreted in the way proposed by the respondent (in that case), –
  - it will result in the words "in respect of a promoted activity or promoted product" being ignored and not being given effect to;
  - it will lead to the consequence of companies that are engaged in the manufacture of both PP and NPP being prejudiced or disadvantaged because of its enterprise.

  The court ought not to adopt an interpretation that produces injustice or absurdity.

  It was held that Para. 7(a)(ii) seeks to prohibit or exclude a company with a PC or product from claiming for both RA and tax rebate in respect of **the same product or activity.** The court found that the appellant had fulfilled all the conditions under Para. 7(a)(ii).

1.2 It was submitted for the DGIR that the learned judge in *Kion Hoong* had erred in applying the purposive approach of interpretation, and reference was made to the legislative history of Para. 7 which can be found in the judgment of the *Kion Hoong* case.

2. **Decision of the Court**

2.1 The Court agreed with DGIR's submission that where the words of a statute are clear, then the court must give effect to it. (*Sri Bangunan Sdn Bhd v Majlis Perbandaran Pulau Pinang & Anor* [2007] 5 CLJ 673)

2.2 Para. 7(a)(ii) refers to a company that has been granted PC under the PIA. It is appropriate to refer to the following provisions of the PIA:

- S2 of PIA where "pioneer certificate" is defined as "a pioneer certificate given under section 7 or any such certificate as amended."
- S7(3) of PIA Subparagraphs (a), (b), and (c) of this section should be read conjunctively. A PC under this section certifies that a company is a "pioneer company" at whose "pioneer factory" a "promoted activity" is carried out or a "promoted product" is produced.
- S2 of PIA defines a "pioneer company" as "*a company certified by a PC to be* ***a pioneer company in relation to a promoted activity or promoted product*** *in respect of which the tax relief period has not ended or has not ceased*."

2.3 The PC issued to the Taxpayer states that it is deemed to be a pioneer company which "*by necessary implication means that the Appellant* (Taxpayer) *carries out a promoted activity or produces a promoted product*" (an essential requirement for the issuance of a PC under S7(3) of PIA.)

2.4 Viewed against the provisions of S7(3) of PIA, the Court is of the view that it is apparent that Para. 7(a) of Sch. 7A merely repeats and reiterates the position under S7(3) of PIA that a PC is granted to a pioneer company in relation to a promoted activity or PP. The emphasis of Para. 7(a) of Sch. 7A is on the grant of a PC, which necessarily indicates that the company carries out a promoted activity or produces a PP (pursuant to S7(3) of PIA).

2.5 The Court agreed with the DGIR's submission that for the purpose of Para. 7(a) of Sch. 7A, the status of the company is relevant as opposed to the issue of promoted activity or PP.

The Court decided that on the clear and unambiguous words of Para. 7(a) of Sch. 7A, the SCIT had not erred in its decision.

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