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CHARTERED TAX INSTITUTE OF MALAYSIA (225750-T)

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TO ALL MEMBERS

TECHNICAL

Direct Taxation

TAX CASE UPDATE

Tax exemption status of a charitable institution – Application for judicial review.

SOCIETY OF LA SALLE BROTHERS v KPHDN

High Court of Malaya at Shah Alam
Civil Appeal No: 25-8-04/2015
Date of Judgment: 30 December 2016

Facts and Issues:

The Society of La Salle Brothers (the Applicant) is a charitable institution with the sole objective of ensuring that education is accessible to Malaysians of all races, religion and creed. It had obtained tax exemption status from the Controller General of Inland Revenue (CGIR) in a letter dated 26 January 1970, which stated (among other matters) that:

- The Applicant was a charitable institution and therefore not liable to income tax;
- The allowances paid by the Ministry of Education for the education services rendered by the Brothers were regarded as subsidies to the Society, of which the Brothers are beneficiaries;
- The Brothers themselves were not liable to income tax in respect of allowances paid by the Ministry.

The Applicant was notified in a letter dated 25 July 1995 from the Director General of Inland Revenue (the Respondent) to re-apply for tax exemption status following amendments to paragraph 13 of Sch. 6 of the Income Tax Act 1967 (ITA) under S.13 of the Finance Act 1988, and to submit certain documents for this purpose. However, the Applicant did not take any action in regard to this letter.

For the years of assessment 2000 (CY and PY) to 2003, the Applicant reported income from various sources for each year, among which were income which were not exempted from tax. The non-exempt sources were:

- Dividends, interest and discounts;
- Rentals, royalties and premiums; and
- Other income (Annual/membership fees, donations and sale of assets).

The Applicant was then issued with notices of assessment (NAs) dated 16 March 2015, for the years of assessment (YA) 2004, 2006 to 2007, and 2010 to 2013, for tax amounting to a total of RM41,390,396. Penalties at the rate of 20% were imposed for failure to furnish the return for the respective year by or before the deadline of 30 April of each year. Following this, the Applicant's tax agent met with the Respondent to request for the tax payable to be paid by instalments, which request was supported by a letter dated 13 April 2015.

Subsequently, the Applicant filed for judicial review on 9 April 2015 to (among others) quash the notices for the above-mentioned years of assessment "on the premise that the decision is null and void and unconstitutional."

Decision:

The Court found that the notices of assessment for the relevant years of assessment dated 16 March 2015 are valid and enforceable. Therefore the Prayer for an order of certiorari was denied.

Based on the findings of the Court, the Applicant's submission that the Respondent's decision (to issue the assessments under dispute) was ultra vires, illegal, void, unlawful and/ or in excess of authority, cannot stand.

The grounds of decision are summarized below:

1. **Submissions**

1.1 Among the contentions of the **Applicant** was that, it (being a charitable institution) enjoyed tax exemption status as stated in the letter from the CGIR dated 26 January 1970. That letter was never withdrawn. The Applicant also submitted that the amendments contained in the Finance Acts of 1986, 1988, 2000 and 2007 do not in law, have any effect on the vested right that the Applicant had acquired before the said amendments. While the law has been amended, it cannot have retrospective effect. Moreover, the NAs dated 16 March 2015 for YA 2004, 2006 and 2007 (with penalties added) are time barred. As the respondent had failed to provide any valid justification for issuing the time barred assessments, his decision to do so was unreasonable. Based on these reasons, the decision of the Respondent requiring the Applicant to pay tax for the relevant YA was ultra vires, illegal, void, unlawful and/or in access of authority.

1.2 The **Respondent** submitted that the application for judicial review was inappropriate and an abuse of the process of court as the Applicant had failed/ refused to resort to the appeal process provided under S.99 of the ITA. In this case, the Applicant had failed to show the existence of exceptional circumstances that would warrant a judicial review. It was also submitted that the tax exemption status of the Applicant cannot be deemed as being granted in perpetuity, that status is no longer enjoyed as a result of the amendments under the respective Finance Acts. Furthermore, the Applicant did not take any action to re-apply for tax exemption status subsequent to the said amendments. Following the amendments, the assessments in dispute were issued in accordance with the law. Although the NAs for YA 2004, 2006 and 2007 dated 16 March 2015 were issued outside the limitation period, it was the Respondent's belief that there were elements of fraud and/ or negligence on the part of the Applicant. The burden of proof that the assessments were excessive/ erroneous was on the Applicant.

2. **Decision of the Court**

2.1 The Court examined the provisions of Paragraph 13 of Sch. 6 of the ITA as it stood on 26 January 1970, and after amendments contained in the following Acts:

(i) Finance Act 1986
(ii) Finance Act 1988
(iii) Finance (No.2) Act 2000
(iv) Finance Act 2007

Based on its examination of the words of the relevant amendments in the Acts as well as the contents of the letter dated 26 January 1970, the Court found that –

(i) the letter dated 26 January 1970 clearly states that the Applicant is a charitable organization not liable to income tax;

(ii) by virtue of the amendments under the Finance Act 1988*, it is mandatory for the Applicant (which is a charitable organization) to apply to the DG for tax exemption, and

also for it to apply its income solely for charitable purposes or charitable objects within Malaysia, and the amount so applied in a YA must not be less than 70%;

* *CTIM's Note: The year stated in the judgment (page 13, paragraph 35) is 1998 which appears to be a typographical error.*

(iii) it was not disputed that the Respondent had notified the Applicant via its letter dated 29 July 1995 of the requirement to re-apply for tax exemption status;

(iv) based on the reading of the law as amended under the Finance (No. 2) Act 2000, the exemption granted to the Applicant ceased to have effect from YA 2003*, unless approval was granted by the DGIR under an application made for the purposes of S.44(6) of the ITA.

* *CTIM's Note: The year stated in the judgment (page 14) is 2013 but 2003 is the YA stated in the amendment in the Finance (No.2) Act 2000 (refer to page 11 of the judgment).*

Based on the above reasons, the Court found that the NAs for YA 2004, 2006 to 2007, 2010 to 2013, dated 16 March 2015 are in accordance with the ITA.

2.2 The Applicant's argument that amendments to the law cannot have retrospective effect is not applicable in this case, in the light of the fact that the DG had notified the Applicant of the need to re-apply for tax exemption status.

2.3 The Court is in agreement with the submission that the application for judicial review was inappropriate and an abuse of the process of Court. The Applicant had "bluntly refused or failed" to lodge an appeal in accordance with procedures provided for under S.99 of the ITA. It was pointed out that the process of judicial review is always at the discretion of the Court and, where other avenues or remedies are available to the Applicant, "it will only be exercised in very exceptional circumstances." In this case, the Applicant had failed to prove the existence of "exceptional circumstances" to justify the issue of an order of certiorari.

2.4 On the matter of time bar, the Court found that the assessments for YA 2004, 2006 and 2007 were beyond the time limit stipulated in S.90(1) of the ITA, but the Applicant had failed to discharge the burden of proof (which rested upon the Applicant) that there was no element of fraud, negligence or willful default on its part. Therefore the Respondent was rightfully entitled to issue the NAs for YA 2004, 2006 and 2007.

2.5 With regard to penalty imposed at the rate of 20%, the Court found that the penalty was imposed in accordance with S.112(3) of the ITA (the Applicant having failed to submit the Returns within the statutory time limit) and was satisfied that the Respondent had exercised proper discretion in imposing the penalty. Hence the Court cannot disturb the decision of the Respondent who had fully considered the relevant issues in imposing the penalty.

2.6 On the Applicant's submission that the amendments do not in law, have any effect on the vested right that the Applicant had acquired before the said amendments, the Court declared that it totally disagreed with that submission and pointed to the amendment which stated that "(the) exemption shall cease from the year of assessment 2003" (S.26 of Finance (No.2) Act 2000) unless an approval was granted under an application made for the purposes of S.44(6) of the ITA. As it was an "undisputed fact" that the Applicant did not make such an application, it cannot enjoy the exemption.

2.7 As long as the DGIR is exercising his legal powers in accordance with the provisions of the ITA, it is not for the Court to intervene.

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

The Society of La Salle Brothers has subsequently appealed to the Court of Appeal (CoA). The CoA has heard the appeal and has unanimously allowed it. The full Grounds of Judgement is available at the official website of the Office of Chief Registrar, Federal Court of Malaysia and a write-up on it will be circulated to members in a subsequent e-CTIM.