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TECHNICAL

Direct Taxation

TAX CASE UPDATE

Application for Judicial Review – Taxation of income of a doctor who incorporates a company to carry on business as a medical practitioner

1. DATO' DR. SINGARAVELOO A/L MUTHUSAMY

2. SINGA & HOE SDN BHD (NO. 587356-U)

v CEO / DIRECTOR GENERAL INLAND REVENUE BOARD OF MALAYSIA

High Court of Malaya At Kuala Lumpur
Application for Judicial Review No: WA-25-237-12/2016
Date of Judgment: 23 November 2018

Facts and Issues:

This is an application for judicial review to quash the decision of the DGIR ("Decision") which was conveyed in a letter dated 9/9/2016 addressed to the General Secretary of the Malaysian Medical Association (MMA), ruling amongst others, that the income received by the 2nd Applicant should be taxed as income under S4(a) of the Income Tax Act, 1967 (ITA) as income of an individual and not company income. The grounds of the application are an error of law, that the decision was arbitrary and a breach of legitimate expectation.

(All sections cited hereinafter refer to sections in the ITA unless otherwise stated.)

The salient facts are as follows: -

The 1st Applicant, a registered specialist medical practitioner (the "Doctor"), had incorporated the 2nd Applicant, (the "Company") to carry on business as medical practitioners and to provide medical services to patients in and/or outside hospitals. The Doctor had signed a "Resident Consultant Agreement" (RCA) dated 1/7/2002, with Johore Specialist Hospital Sdn Bhd (JSHSD) which owns and operates the Johore Specialist Hospital ("Hospital"), to provide medical consultancy services as a Resident Consultant Physician at the Hospital.

The Respondent had initiated tax audits on several medical practitioners who practice under circumstances similar to the Doctor in this case, and the MMA had meetings with the Respondent to discuss the issue of the tax treatment of income of such doctors. In response to MMA's inquiries, the DGIR issued a letter dated 9/9/2016 by which the MMA was informed that : -

- based on the agreements signed between the specialist doctors and private specialist

hospitals, income received from these hospitals will be taxed under S4(a) as income of an individual and not as income of a company;

- the above treatment is in line with the practice adopted by the DGIR based on the provisions of the ITA, specifically, under powers granted under sections 140, 91 and 65 of the ITA. From the facts of such cases, it is clear that the agreements between the abovementioned parties are contracts for services;
- under provisions of the ITA, the DGIR has power to disregard the income of specialist doctors received through private limited companies, and to raise assessments on such income as income of the individual specialist doctors.

The Applicants then commenced proceedings for Judicial Review as their case fell squarely within that Decision. However, on 14/11/2016, the Doctor had entered into a Service Agreement with the Company, under which the Company, as Employer, agreed to engage the Doctor, as Employee, to provide medical consultancy services as a physician to the Hospital.

Decision:

The application is dismissed. The Court is of the opinion that the Decision of the DGIR is legal as it is premised on the construction of the RCA. The ITA empowers the DGIR to raise any assessment or additional assessment, and the DGIR is not estopped from adopting a different form of assessing tax.

The grounds of decision are summarized below: -

The findings of the Court are set out under the following 4 issues raised by the Applicants –

i. The decision amounts to an error of law (based on erroneous and invalid grounds);

ii. Arbitrary and unfair treatment of the Applicants;

iii. Breach of the Applicants' legitimate expectations;

iv. Retrospective punishment of the Applicants is in breach of Article 7(1) of the Federal Constitution.

Issue (i) – Error of law

1. The case calls for an interpretation of the RCA entered into between the Doctor and JSHSD in order to ascertain the true intention of the parties to the agreement (citing *Berjaya Times Square Sdn Bhd v M-Concept Sdn Bhd [2010] 1 MLJ 597*.) After examining the terms of the agreement, the Court found as follows: -

   - The Hospital offered the Doctor to conduct his professional practice at the Hospital in consideration for fees payable by the Doctor to the Hospital;
   - As for medical services rendered by the Doctor at the Hospital, JSHSD will pay all the money so received by the Doctor from his patients;
   - The Doctor had signed the said Agreement in his personal capacity (the Court agreed with the DGIR's stand on this matter.)

   Therefore, when the agreement for services was clearly made between the Doctor and

JSHDH, then all monies and payments from the patients under the RCA rightly belonged to the Doctor. Consequentially, all taxes derived from the income of the practice at the Hospital is taxable as the Doctor's (individual) income, and not the company's income.

2. The Court did not agree with the Applicant's contention that the Doctor (even though he signed the RCA with JSHSD) was acting for the company at all material times, and made the following observations –

   - The Service Agreement between the Company and the Doctor on 14/11/2016 is not of relevant consideration as the DGIR's letter was dated 9/9/2016.
   - With regard to payments of professional fees by JSHSD to the Company, the Court was of the opinion that the said payments were only an arrangement agreed to between the parties, but they cannot detract from the fact that the Doctor had entered into the RCA with JSHSD in his personal capacity. The payments were for professional services rendered by the Doctor at the Hospital, and how they were transmitted is up to the parties' arrangements, but does not change the character of the payments.
   - Citing the case of *Controller of Inland Revenue v Lim Foo Yong Sdn Bhd [1982] CLJ (Rep) 76*, the Court was of the considered opinion that the DGIR had complied with the principle of construction established in that case, by giving the RCA its ordinary meaning, which is that the agreement is a contract for service between the Doctor and JSHSD, whereby the Doctor pays for rental of his clinic at the Hospital and receives payments from his patients in consideration of his professional services.

3. In any case, the Court notes that the DGIR is empowered by S140 to disregard certain transactions (case cited - *Syarikat Ibraco-Peremba Sdn Bhd v KPHDN [2017] 2MLJ 120*), in this case, the monies being paid to the Company and not to the Doctor, and reiterates the finding that the DGIR has applied the correct principles in the construction of the RCA when he finds that, based on the agreement and the ITA, it is the Doctor and not the Company, who is chargeable to tax in respect of monies received from the Doctor's patients.

Issue (ii) – Arbitrary and unfair treatment of the Applicants

1. The Decision cannot be said to be arbitrarily made as it was made after discussions with MMS and based on DGIR's construction of the Applicants own documents.
2. With regard to the claim that other categories of professionals are given a different treatment, the Court has not been presented with any documents to show whether their contracts are the same as the Applicants'.

Issue (iii) – Breach of the Applicants' legitimate expectations

1. The Applicant's submission of legitimate expectations was premised on an audit conducted by the DGIR in 2013. However, that audit was not on the tax treatment as practiced by the Applicants, but was on the issue of certain expenses claimed by the Applicant (petrol, parking and toll fees, filing fees etc.).
2. Furthermore, the DGIR is empowered under S91(1) to raise any assessment or additional assessment if he is of the opinion that no tax or insufficient tax (assessment) has been made,

"*and this will include departing from the existing practice and adopting a different form of assessment*."

"*Estoppel cannot be invoked against the Director General of Income Tax when he is put to notice that an incorrect assessment has been made…..The Director General cannot raise an estoppel against himself from discharging his statutory duty to raise a correct assessment under the appropriate law ….*"

Teruntum Theatre Sdn Bhd v KPHDN [2006] 4MLJ 685

Issue (vi) – Breach of Article 7(1) of the Federal Constitution.

1. This is a non-issue as the cases are very clear that the DGIR can adopt a different form of assessing tax.

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

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