

TECHNICAL

Direct Taxation

TAX CASE UPDATE

Interest Against The Revenue

Whether the High Court may award interest against the Revenue?

Ketua Pengarah Hasil Dalam Negeri v Pelangi Sdn Bhd (2012) (Federal Court)

Facts:

The taxpayer was a property developer and in 2008, the taxpayer received compensation for the compulsory acquisition of its land. It did not subject the compensation to income tax following the decisions in *Ketua Pengarah Hasil Dalam Negeri v Penang Realty Sdn Bhd* [2006] 2 CLJ 835 and *Lower Perak Co-operative Housing Society Berhad v Ketua Pengarah Hasil Dalam Negeri* [1994] 3 CLJ 540.

The Revenue disregarded the decisions in *Penang Realty* and *Lower Perak* and relied on its Decision Impact Statement and subjected the compensation to income tax. Accordingly, the taxpayer filed a judicial review application on 17.2.2011 and was granted leave by the High Court on 8.4.2011. On 22.8.2011, the High Court held that:

- (a) The Revenue was bound by the decisions in *Penang Realty* and *Lower Perak*.
- (b) The Revenue's Decision Impact Statement had no legal effect.
- (c) The Revenue's decision to subject the compensation to income tax shall be quashed.
- (d) The Revenue was to refund the taxes unlawfully collected and retained with interest at 4% per annum to the taxpayer.

Issue:

Whether the High Court may award interest against the Revenue?

Decision:

The High Court held that the cases cited by the taxpayer illustrated clearly that the High Court was vested with discretion to impose interest payment as compensation under Section 11 of Civil Law Act 1956. According to the High Court, this position was affirmed in a number of Federal Court decisions. Interest is awarded in the nature of compensation to remedy the aggrieved party whose money has been unlawfully deprived by the other party. In the circumstances of the case, the High Court ordered the Revenue to pay interest to the taxpayer on the sum unlawfully retained by the Revenue from date of the Revenue's decision.

The High Court observed that the position of Revenue in such a situation, which was conferred with coercive power of the state, having the benefit of a massive interest free loan as fruit of an unlawful

action. Reference was made to the House of Lords' decision in *Woolwich Building Society*, where the concept of unjust enrichment or unjust benefit was considered in awarding interest to the taxpayer. The High Court commented that the House of Lords observed that it was unacceptable to deny interest to a taxpayer especially when the taxpayer had paid large sums of money to the Revenue based on invalid regulations and retained free of interest, pending a court decision.

In the present case, the Revenue had subjected the gains arising from the compensation for compulsory acquisition of land to income tax despite the decisions of the superior Courts. As the tax unlawfully retained by the Revenue was at all material times rightful money belonging to the taxpayer, the High Court ordered the Revenue to return the retained tax to the taxpayer with interest of 4% running from the date of the Revenue's decision to unlawfully retain the tax.

The decision of the High Court was unanimously affirmed by the Court of Appeal. The Revenue's application for leave to appeal to the Federal Court was unanimously dismissed by the Federal Court.

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