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PREMIER TAX EVENT OF THE YEAR

NATIONAL TAX CONFERENCE 2015

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NATIONAL TAX CONFERENCE 2015

TAX CASES UPDATE

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OVERVIEW

- Employment Income - Perquisite
- Business Income – Withdrawal of stock
- Basis period – Advance payment
- Deduction
- Capital Allowance
- Reinvestment Allowance
- Real Property Gains Tax

CASE #1

EMPLOYMENT INCOME - PERQUISITE

MAXIS COMMUNICATIONS BERHAD v. KPHDN

ISSUE

Whether a payment received by an employee (who holds unvested option) from his employer (in return for the employee giving up his contractual rights in the unvested options) is liable to be tax under the Income Tax Act 1967 (ITA 1967).

CASE #1

CASE - MAXIS COMMUNICATIONS SDN BHD

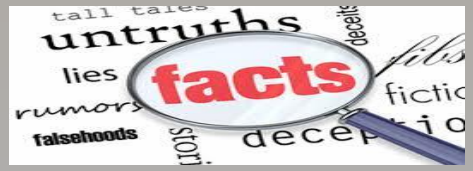
FACTS OF THE CASE

Eligible employees were granted options to subscribe for shares in Maxis through ESOS.

An eligible employee can exercise the option up to ten years from the date of the first grant.

In May 2007, Binariang made a conditional take over to acquire all voting shares in Maxis for a cash consideration.

By reason of the take over the holders of the unvested option were entitled to a payment of Equivalent Cash Consideration (ECC).



CASE #1

CASE - MAXIS COMMUNICATIONS SDN BHD

Under the ECC, employee receive alternative consideration in substitution or cancellation of all outstanding unvested shares.

Cash payment will be paid according to original vesting schedule applicable to the outstanding options.

FACTS OF THE CASE

Revenue took the position that ECC is a perquisite to the employee and taxable under Section 13(a) ITA and not as share based income.

Maxis contended ECC should be tax as share based income and taxable under section 25(1A) and 32(1A) ITA.

CASE #1

CASE - MAXIS COMMUNICATIONS SDN BHD

THE LAW

- Section 13(1)(a) of the ITA 1967
- Section 25(1A) of the ITA 1967
- Section 32(1A) of the ITA 1967

CASE #1

CASE - MAXIS COMMUNICATIONS SDN BHD

DECISION

FEDERAL COURT

It was held that ECC is taxable as a perquisite. However, Sections 25 and 32 of the ITA 1967 are not applicable as the payment to the employee was no longer under ESOS.

CASE #1

CASE - MAXIS COMMUNICATIONS SDN BHD

GROUNDS OF DECISION

- Payment under ECC is not based on ESOS. The scheme had been cancelled pursuant to a conditional take over.
- ECC being a cash payment is an employment income under Section 13 of the ITA 1967. ECC constitutes a perquisite under the section.
- The option is only vested on the employees when they exercise their rights on or after the anniversary date.
- There was no ambiguity as regards to the interpretation of the words in Section 25 and 32 of the ITA 1967.
- Based on the explanatory statements, it is clear that Section 25 and 32 of the ITA 1967 do not apply to benefit by way of cash payment.

CASE #2

BUSINESS INCOME : WITHDRAWAL OF STOCK

KPHDN V. MERCEDES-BENZ MALAYSIA SDN BHD

ISSUE

Whether the cars sold in the secondary sales channel are stock in trade withdrawn for the Appellant's own use as envisaged under Section 24(2) of the ITA 1967?

CASE #2

CASE - MERCEDES-BENZ MALAYSIA SDN BHD

FACTS OF THE CASE

The Taxpayer is a franchise holder and wholesaler of Mercedes-Benz vehicles in Malaysia. It sells both brand new and used cars.

The Used Cars are at all times available for sale to the public and is priced lower than the brand new cars.

The used cars are sold vide the secondary sales channel. The used cars are sourced by registering new stocks under the Taxpayer's name.

The cars were used as a demo or test drive car. It was also used as a promotional car for international or local event.

CASE #2

CASE - MERCEDES-BENZ MALAYSIA SDN BHD

THE LAW

- Section 24 of the ITA 1967
- Gloucester Railway Carriage and Wagon Co. Ltd v The CIR[1930] 12 TC
- W.Nevill & Co. Ltd v F.C of T [1937] 56 CLR 290
- Section 35(2) of the ITA 1967

CASE #2

CASE - MERCEDES-BENZ MALAYSIA SDN BHD

DECISION:

COURT OF APPEAL

The High Court decision was upheld. The cars sold in the secondary sales channel were not withdrawal of stock for its own use.

CASE #2

CASE - MERCEDES-BENZ MALAYSIA SDN BHD

HIGH COURT- GROUNDS OF DECISION

NOTE : No written judgment issued by the Court of Appeal.

The vehicles continue as the tax payer stock in trade despite registration and upon sales in the secondary sales channel.

It is required by law to register the new vehicles under the Taxpayer's name.

The Taxpayer's business has to be looked as a whole set of operation directed towards producing income.

Thus, the Taxpayer is entitled to deduct the written down value of its Used Car stock under Section 35(2) of the ITA 1967.

CASE #3

BASIS PERIOD - ADVANCE PAYMENT

KPHDN v. CLEAR WATER SANCTUARY GOLF MANAGEMENT BHD

ISSUE

Whether the amount of deferred licenses fees (advance payment) received by the Taxpayer pursuant to License Agreement and Rules and Regulation of the Taxpayer is correctly brought to tax under Section 24 of the ITA 1967 in the year the amount is received.

CASE #3

CASE – CLEAR WATER SANCTUARY GOLF MANAGEMENT BHD.

FACTS OF THE CASE

Taxpayer is an operator of a golf Club. Membership is available through grant of a contractual license under a License Agreement.

Under the agreement members are required to pay an advance payment equivalent to the total annual license fee payable for the term of the license.

Annual license fee is payable each year and collected upfront as a security.

In the accounts of the Taxpayer, the advance payment was recognized as liability and not income.

CASE #3

CASE – CLEAR WATER SANCTUARY GOLF MANAGEMENT BHD.

THE LAW

- Section 3 of the ITA 1967
- Section 23 of the ITA1967
- Section 24 of the ITA 1967

CASE #3

CASE – CLEAR WATER SANCTUARY GOLF MANAGEMENT BHD.

DECISION

COURT OF APPEAL

The High Court decision was upheld. It was wrong to tax the advance payment in the year it was received.

CASE #3

CASE – CLEAR WATER SANCTUARY GOLF MANAGEMENT BHD.

GROUNDS OF DECISION

- The annual license fee is payable annually in advance on the due dates during the term of the license.
- The payment is paid for future services which has not been rendered yet.
- The beneficial ownership of the advance payment is still with the member and if the member decides to cancel he may ask for refund.
- SCIT failed to appreciate the characteristic of the advance payment and ignored the contractual agreement or bargain between the parties.
- There is no debt owing under Section 24 of the ITA 1967 unless service is rendered. There is no conflict between the Act and the accounting treatment.

CASE #4

DEDUCTION

PIRAMID INTAN SDN BHD v. KPHDN

ISSUE

Whether the payments by the Taxpayer to Sarawak Timber Industry Development Corporation (STIDC) were allowable deduction.

CASE #4

CASE – PIRAMID INTAN SDN BHD

Taxpayer is in the business of purchase and sale timber.

Taxpayer does not have a timber licence, purchased timber from other timber licensees.

FACTS OF THE CASE

Taxpayer entered into an agreement with STIDC for sale and purchase of timber logs including the extraction of such logs.

In consideration of the rights, power. Benefit under the agreement, the tax payer is to pay RM40m to STIDC.

CASE #4

CASE – PIRAMID INTAN SDN BHD

FACTS OF THE CASE

STIDC is the holder of the forest timber licence and Taxpayer is the timber contractor.

The contract given was for Nanga Gaat Kapit concession area for a period of 20 years

It was also the term of the agreement that the Taxpayer shall pay royalties and premium to STIDC.

STIDC is a statutory body established by the Sarawak Timber Industry Development Corporation Ordinance 1973.

CASE #4

CASE – PIRAMID INTAN SDN BHD

THE LAW

- Section 33 of the ITA 1967
- Section 39 of the ITA 1967
- Margaret Luping & Ors v KPHDN [2000] 3 CLJ 409
- British Insulated & Helsby Cables Ltd v. Atherton 19TC 155

CASE #4

CASE – PIRAMID INTAN SDN BHD

DECISION

HIGH COURT

The SCIT decision was upheld. The payment made to STIDC is not deductible under the ITA 1967.

CASE #4

CASE – PIRAMID INTAN SDN BHD

GROUNDS OF DECISION:

- For a tax payer to qualify for deduction, he must first of all place the payment under Section 33 of the ITA 1967.
- Next he has to ascertained whether the payment is caught under Section 39(1) of the ITA 1967.
- The upfront payment relates to the acquisition of source of income or capital asset thus capital in nature.
- Payments were more as a consideration for acquiring right to extract, remove and sell timber logs.
- The payments had no relation with the cost of logging activity from the concession area.

CASE #5

DEDUCTION

BEDFORD DAMANSARA HEIGHTS DEVELOPMENT SDN BHD V. KPHDN

ISSUES

1. Whether expenses incurred to secure loan facilities are deductible under Section 33 of the ITA 1967.

2. Whether the time barred assessment is valid and enforceable.

CASE #5

CASE – BEDFORD DAMANSARA HEIGHTS DEV. SDN BHD

FACTS OF THE CASE

Taxpayer is in the leasing and real estate business.

DGIR disallowed all expenses incurred in raising fund (loans) used for the business. Assessment for two years were raised after six years.

The rental income received by the Taxpayer was tax as business income under Section 4(a) of the ITA 1967.

Expenditures on the loans are under writing & guarantors, commission, annual fee, annual review fee, annual management fee and surveillance fee.

CASE #5

CASE – PIRAMID INTAN SDN BHD

THE LAW

- Section 33 of the ITA 1967
- Section 91 of the ITA 1967
- Beauchamp (inspector of Taxes) v. FW Woolworth plc 1989 STC 510
- Scottish North American Trust Co Ltd v. Farmer

CASE #5

CASE – BEDFORD DAMANSARA HEIGHTS DEV. SDN BHD

DECISIONS

HIGH COURT

The SCIT decision was set aside. Cost of raising fund is capital in nature, thus not deductible under Section 33 of the ITA 1967.

On the issue of time barred years, the DGIR failed to prove negligent on the part of the Taxpayer.

CASE #5

CASE – BEDFORD DAMANSARA HEIGHTS DEV. SDN BHD

GROUNDS OF DECISION

- The court must look at the nature of the business and the purposes of the fund.
- It is a revenue expenditure if it is incurred to meet the current liabilities and in meeting day to day expenditure of making profit.
- The expenditure is not recurring in nature. It was paid to service the loan and not directly concerned with expenditure to generate profits.
- Financial arrangements are quite distinct from the activities by which their earn the income.
- In the case of time barred years, the DGIR failed to discharge the burden that there was any element of negligent on the part of Taxpayer.

CASE #6

CAPITAL ALLOWANCE

KPHDN V. JUARA TIASA SDN BHD

ISSUE

Whether the Taxpayer qualifies for industrial building allowance (IBA) for the expenditure incurred on the construction of the campus building by virtue of paragraph 42B, Schedule 3 of the ITA 1967?

CASE 6

CASE – JUARA TIASA SDN BHD

FACTS OF THE CASE

A campus building was constructed in order to rent it out to educational institution.

The campus building was rented out to two companies which run education business i.e. Kolej Aman Berhad and Maxis Segar Education Sdn Bhd.

The DGIR has taxed the rental income under Section 4(a) of the ITA 1967- business income

The Taxpayer contended that it qualifies for IBA for the expenditure incurred on the construction of the campus building under Paragraph 42B, Schedule 3 of the ITA 1967

CASE #6

CASE – JUARA TIASA SDN BHD

THE LAW/REFERENCE

- Section 4(a) of the ITA 1967
- Paragraph 42B, 50 & 60 Schedule 3 of the ITA 1967
- Section 17A of the Interpretation Act 1948 and 1967
- Budget Speech 1996
- C.I.R v Ross & Coulter (Blacdnoch Distillery) Co. Ltd [1948] 1 AER 66
- Cape Brandy Syndicate v CIR, 12 TC 358

CASE – JUARA TIASA SDN BHD

DECISION

HIGH COURT

The SCIT's decision was upheld. The Taxpayer qualifies for IBA for the expenditure incurred on the construction of the campus building under Paragraph 42B, Schedule 3 of the ITA 1967. There is no requirement that the owner of the building must operate the business.

CASE #6

CASE – JUARA TIASA SDN BHD

GROUNDS OF DECISION

- Paragraph 42B is to encourage investments in buildings used for education.
- The said building is being used for the purposes of an approved educational course.
- No requirement for the building owner (Taxpayer) to operate the business to qualify for IBA.
- In a taxing Act, one has to look merely what is clearly said.
- Schedule 3 must be read as whole.

CASE #7

REINVESTMENT ALLOWANCE

KPHDN V. BINTULU LUMBER DEVELOPMENT SDN BHD

ISSUE

Whether the cultivation of palm oil falls within the ambit of the words "cultivation of fruit" stipulated in Paragraph 9(cc) of Schedule 7A, ITA 1967.

CASE #7

CASE-BINTULU LUMBER DEVELOPMENT SDN BHD

FACTS OF THE CASE

The Taxpayer is in the business of logging, palm oil cultivation and farming.

Taxpayer had claimed Reinvestment Allowance for the preparatory works and planting of oil palm trees.

DGIR disallowed the claim.

The SCIT allowed the Taxpayer's appeal.

CASE #7

CASE-BINTULU LUMBER DEVELOPMENT SDN BHD

THE LAW/REFERENCE

- Paragraph 1A, Schedule 7A of the ITA 1967
- Paragraph 9, Schedule 7A of the ITA 1967
- Budget Speech 1996 [Paragraph 42 & 43]
- Rang Undang-undang Kewangan [No. 2] 1995 [Paragraph 12]

CASE #7

CASE - BINTULU LUMBER DEVELOPMENT SDN BHD

'A fruit is a fruit'

Special Commissioner of Income Tax makes this landmark decision

By Phyllis Wong and Peter Sibon
reporters@theborneopost.com

KUCHING: Oil palm industry players throughout the country can now rejoice following a landmark decision by the Special Commissioner of Income Tax that the cultivation of oil palm fruits falls under the same category as fruit cultivation.

The Special Commissioner of Income Tax, the highest 'Appeals Court' for income tax related cases, handed down the judgment on Tuesday.

This was revealed to The Borneo Post by Special Commissioner of Income Tax chairman Dato Zaini Abdul Rahman on the sidelines of a seminar entitled 'Appeal of Income Tax Cases before the Special Commissioners of Income Tax' at Hilton Kuching yesterday.

"One of the 10 cases we heard yesterday was on the interpretation of law whether the cultivation of oil palm fruits falls under the cultivation

> On our part, it's already final. The IRB has further avenue ... where it can appeal to the High Court. If it doesn't appeal then our decision is final.
>
> Dato Zaini Abdul Rahman, chairman of Special Commissioner of Income Tax

of fruits which give companies reinvestment allowances on capital expenditures incurred on opening up land for cultivation.

"So, we already make a summary judgment on that case. We decided that oil palm falls under the cultivation of fruits."

(Continued from Page 12)

However, Zaini said that the Inland Revenue Board (IRB) might appeal against the decision.

"On our part, it's already final. The IRB has further avenue ... where it can appeal to the High Court. If it doesn't appeal then our decision is final."

He added that the role of the Special Commissioner of Income Tax was to adjudicate for the people without sympathy, but empathy.

"We are the court of appeal in the normal sense, except the name. That's why we have this public talk to make sure members of public know about us; what are our true roles.

"Before this nobody makes an effort to let the public really understand their legal rights in tax law. They do not know where to bring up their grievances against the imposition of tax by the IRB."

Zaini explained that to some extent the IRB also did not like the public

Dato Zaini Abdul Rahman

to appeal against its decision. Fo instance, they would not advis taxpayers that if they were not happ with its decision they had the right t appeal to the Special Commissione of Income Tax.

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Topic : Tax Cases Update

Speaker : Abu Tariq Jamaluddin

LHDN MALAYSIA

CASE #7

CASE-BINTULU LUMBER DEVELOPMENT SDN BHD

DECISION

HIGH COURT

The DGIR appeal was allowed. It was held that the palm oil fruits are not within the ambit of the word "fruits" in Paragraph 9(cc) of Schedule 7A, ITA 1967.

CASE #7

CASE-BINTULU LUMBER DEVELOPMENT SDN BHD

HIGH COURT-GROUNDS OF DECISION:

Oil palm trees were cultivated as a commercial plant for the purpose of processing and production of oil

The fruits in the oil palm tree is a nomenclature which refers to the fruit bunch harvested from the oil palm tree.

The edible oily and greasy fruits after being processed become palm oil which has commercial value and is used as food. It can not be considered as fruit in the ordinary and plain meaning.

CASE #7

CASE - BINTULU LUMBER DEVELOPMENT SDN BHD

HIGH COURT- GROUNDS OF DECISION

The intention of the Parliament on giving RA was to encourage cultivation of fruits in its plain and ordinary language i.e. fruits which one can pluck from the tree and be eaten raw . This includes fruits which not Malaysian origin

No expressed provision to include palm oil fruits under "fruits" in paragraph 9(cc) of Schedule 7A.

Thus, the palm oil fruit is not the fruit in the plain and ordinary meaning as understood in the common parlance of Malaysia

CASE #8

REAL PROPERTY GAINS TAX ACT

KENNY HEIGHTS DEVELOPMENT SDN BHD. V. KPHDN

ISSUE

Whether the subject land was disposed in the year the sale and purchase agreement was signed or in the year the condition precedents was satisfied.

CASE #8

CASE – KENNY HEIGHT DEVELOPMENT SDN BHD

FACTS OF THE CASE

Sale and purchase agreement in respect of the subject land was signed on the 14.08.2000.

The agreement was subject to pre condition, among others is the approval from the Securities Commissions.

All conditions were satisfied on the 27.04.2007.

RPGT assessment was issued against the tax payer for disposal of land in the year of assessment 2000 and not for the year of assessment 2007.

CASE #8

CASE – KENNY HEIGHT DEVELOPMENT SDN BHD

THE LAW

Paragraph 16 (a) and (b) Schedule 2 of the Real Property Gains Tax Act 1976

Real Property Gains Tax Act (Exemption)(No 2) Order 2007

CASE #8

CASE – KENNY HEIGHT DEVELOPMENT SDN BHD

DECISION

COURT OF APPEAL

The High Court decision was set aside. The SCIT decision was reinstated. Disposal of the subject land took place in 2007. The gain from the disposal is exempted under the Exemption Order 2007.

CASE #8

CASE – KENNY HEIGHT DEVELOPMENT SDN BHD

GROUNDS OF DECISION

- Ground of judgment of the High Court did not demonstrate any error on the part of the SCIT.
- The High Court had a different view on Paragraph 16, Schedule 2 of the RPGT 1976 but its failed to provide reasoning for that different view.
- The SCIT fully appreciated and took into consideration that the agreements are essentially conditional agreement.
- The findings of facts by the SCIT were not perverse to the evidence. Therefore there was no reason to interfere with the findings.
- The case stated by SCIT did not contain anything that is ex facie bad in law. The decision by the SCIT was well reasoned.

THANK YOU

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