Malaysian Institute Of Taxation

The premier body for tax professionals

TAX NASIONAL

Official Journal of the Malaysian Institute of Taxation

Vol.16/2007/Q2 RM38.00

"15 years of MIT"

"A measure of progress..... as Malaysia celebrates 50 golden years of independence, MIT is proud to celebrate 15 years of representing the Malaysian tax professionals!"

KDN PP 7829/3/2008

Malaysian Institute Of Taxation

http://www.mit.org.my

The premier body for tax professionals

Continuing Professional Development (CPD)

TRAINING PROGRAMMES 3rd QUARTER 2007

Date	Training Programme	CPD	Venue	Speaker
JULY 2007				
3 July 2007 9.00am - 5.00pm	Workshop: Tax Planning for SME's & IHC's	8	Kuala Lumpur	Mr Chow Chee Yen
10 July 2007 9.00am - 5.00pm	Workshop: Tax Risk Management - A Taxpayers Guide to Minimising Risks	8	Penang	Mr Christopher Low
17 & 18 July 2007 9.00am - 5.00pm	NTC	2.5	Kuala Lumpur	Various Speakers
AUGUST 2007				
16 August 2007 9.00am - 5.00pm	Workshop: Tax Risk Management - A Tax Payer's Guide to Minimising Risk	8	Ipoh	Mr Christopher Low
17 August 2007 9.00am - 5.00pm	Workshop: Tax Planning for SME's & IHC's	8	Johor Bahru	Mr Chow Chee Yen
20 August 2007 9.00am - 5.00pm	Seminar: Transfer Pricing-TP as planning tool, TP & Supply Chain Management Planning;TP & Indirect Tax Implications	8	Kuala Lumpur	Various Speakers
21 August 2007 9.00am - 5.00pm	Workshop: Tax Risk Management - A Tax Payer's Guide to Minimising Risk	8	KK	Mr Christopher Low
22 August 2007 9.00am - 5.00pm	Workshop: Tax Risk Management - A Tax Payer's Guide to Minimising Risk	8	Kuching	Mr Christopher Low
23 August 2007 9.00am - 5.00pm	Workshop: Tax Planning for SME's & IHC's	8	Kuantan	Mr Chow Chee Yen
27 August 2007 9.00am - 5.00pm	Workshop: Tax Planning for SME's & IHC's	8	Penang	Mr Chow Chee Yen
28 August 2007 9.00am - 5.00pm	Workshop: Claiming Tax & Duty Refunds	8	Kuala Lumpur	Mr Thomas Selva Doss & Mr Tan Kok Meng
SEPTEMBER 2007				
8 September 2007 10.00am - 6.00pm	Budget Highlights	8	Kuala Lumpur	Mr Chow Chee Yen
10 September 2007 3.00am - 6.00pm	An MIT Exclusive: The Budget with Datuk Aziyah	10	Kuala Lumpur	Datuk Aziyah bt Bahauddin
12 September 2007 9.00am - 5.00pm	The 2008 Budget - At Your Fingertips	8	Ipoh	Mr Chow Chee Yen
13 September 2007 9.00am - 5.00pm	The 2008 Budget - At Your Fingertips	8	Melaka	Mr Chow Chee Yen
14 September 2007 9.00am - 5.00pm	The 2008 Budget - At Your Fingertips	8	Kuantan	Mr Chow Chee Yen
19 September 2007 9.00am - 5.00pm	The 2008 Budget - At Your Fingertips	8	KK	Mr Chow Chee Yen
20 September 2007 9.00am - 5.00pm	The 2008 Budget - At Your Fingertips	8	Kuching	Mr Chow Chee Yen
21 September 2007 9.00am - 5.00pm	The 2008 Budget - At Your Fingertips	8	Johor Bahru	Dr Veerinderjeet Singh & Mr Chow Chee Yen
25 September 2007 9.00am - 5.00pm	The 2008 Budget - At Your Fingertips	8	Penang	Dr Veerinderjeet Singh & Mr Chow Chee Yen

DISCLAIMER

The Malaysian Institute of Taxation reserves the right to change the speaker (s)/ date (s), venue and / or cancel the workshop/events without notice at their discretion.

ENQUIRIES

Please call **Nur / Latha at 03-2162 8989 ext 106 / 108** or refer to MIT's website at **www.mit.org.my** for more information on the CPD programmes

The President's Note

Dear Members and Readers,

Since its inception in MIT in 1991, MIT has come a long way. This is its 15th year of life. Read more about it inside the journal!

Three important events took place in this quarter. They are the release of the Revised Section 153 Guidelines that still requires the applicants to attend the Budget Seminar, the e-filling issue, and the RPGT Exemption Order.

With regards to the Section 153 Guidelines which were comprehensively dealt with in the previous issue of Tax Nasional, those who missed out on the 2007 Budget Seminar and are therefore "disqualified", the Ministry of Finance has authorised MIT to hold a re-run of the 2007 Budget Seminar. This seminar will be held in KL on the **29th of May 2007.**

For the e-filling issue we understand the problems faced by the IRB but coming at a time when everybody had geared themselves to meet the submission deadline, not just a few were stunned; However the IRB came up with a very swift interim solution.

The RPGT Exemption was quite a surprise to many. Those who had signed their S&P Agreements before 1st April 2007 were understandable disappointed but the majority of the public was elated! Insofar as tax agents are concerned please be reminded that the RPGT Act itself is still in force. Students, RPGT is still an examinable topic.

Readers and Members, please keep **17th & 18th July 2007** free to attend the National Tax Conference at the Kuala Lumpur Convention Centre. This year's conference promises to be as, if not more, exciting as the previous years'. The theme for NTC 2007 is ***"Progressing with the Nation"*** a timely theme as Malaysia turns 50 and MIT turns 16! The very inception of MIT is a measure of the nation's progress. The birth of an organisation representing and acknowledging the tax profession as a specialised profession is itself testament to the nations progress for is not tax revenue a mark of the income earned by the dwellers of a country? Simplistically the higher the tax revenue means that the income earned is high and therefore shows the economic prosperity of a nation…from which flows all other forms of progress and prosperity.

So, that's all for now.

Tuan Haji Abdul Hamid bin Mohd Hassan
President, MIT

Editors's Note

Dear Readers,

We have tried our best to bring you this issue of Tax Nasional due at the end of June 2007 earlier and I am glad to say that we have succeeded! We shall endeavour to keep up this momentum and be back on the fast track!

This issue and in conjunction with the Nation's 50th Birthday. MIT is presenting a short anniversary issue of sorts. MIT is but a sweet maiden of 16. A pictorial of the 1st Council to the last one together with reminiscences from some of the founding and long serving members! (FYI: of which I am one. In fact I have been here since the birth of MIT and am one of the few still around in active participation). But enough said, please read and see for yourselves.

Among our highlights, we have an "up close & personal" candid interview with the Director General of Customs Dato' Sri Haji Abd Rahman bin Abd Hamid, the second part on Tax Risk Management including the Malaysian Perspective, Mr. David Russel, QC concludes with his second part of Managing Tax Disputes in Australia and so on.

The "big" news is the exemption of RPGT. However it is only an exemption, the RPGT Act has not been abolished, as such it is still of examinable relevance to students whereas practitioners would do well not to forget it totally.

The issue of "privilege" and taxpayer confidentiality is always a matter of concern – where does privilege begin and end?! We have, in this issue the UK perspective!

Again I request and demand and ask and beg for more people to come forward to contribute your views and articles to Tax Nasional. Help us make it a better journal for you.

Adieu for now,
Harpal Singh Dhillon
Editor

Malaysian Institute Of Taxation

The Malaysian Institute of Taxation ("MIT") is a company limited by guarantee incorporated on 1 October 1991 under Section 16(4) of the Companies Act 1965. The Institute's mission is to be the premier body providing effective institutional support to members and promoting convergence of interests with government, using taxation as a tool for the nation's economic advancement and to attain the highest standard of technical and professional competency in revenue law and practice supported by effective secretariat.

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Tax Nasional

Official Journal of the Malaysian Institute of Taxation

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Malaysian Institute Of Taxation

CONTENTS

INVITATION TO WRITE

Tax Nasional welcomes original and unpublished contributions which are of interest to tax professionals, lawyers and academicians. It may cover local or international tax development. Articles contributed can be written in English or Bahasa Malaysia. It should be between 2,500 and 5,000 words (doubled-spaced, typed pages). They should be submitted in hardcopy and softcopy in Microsoft Word.

Contributions intended for publication must include the writer's name and address, even if a pseudonym is used. The Editor reserves the right to edit all contributions based on clarity and accuracy of expressions required.

Contributions may be sent to :

THE EDITOR of TAX NASIONAL
Malaysian Institute of Taxation, Kuala Lumpur office

e-mail: publications@mit.org.my

News In Tax is temporarily inactive. We hope to be back in the next issue!

NATIONAL TAX CONFERENCE

Malaysian Institute Of Taxation

The History

The National Tax Conference is jointly organised by the Akademi Percukaian Malaysia, Lembaga Hasil Dalam Negeri Malaysia and Malaysian Institute of Taxation.

A team of experienced speakers and practitioners from both government and private sectors (both locally and internationally) are invited every year to present papers on technical areas of interest in taxation.

We are proud to announce that for the past six years the number of delegates have increased progressively. The NTC 2006 recorded the highest number of delegates todate with over 1300 delegates comprising tax practitioners, tax accountants, financial planners, company directors, academicians, officials from the Lembaga Hasil Dalam Negeri Malaysia and Ministry of Finance and also representatives from other government agencies.

	Date(s)	Venue	Theme
NTC 2001	3 July 2001	Palace of the Golden Horses	Self Assessment: Towards Good Governance
NTC 2002	3 September 2002	Palace of the Golden Horses	Globalised Tax System in a Borderless World
NTC 2003	5 and 6 August 2003	Palace of the Golden Horses	Meeting Future Challenges of Tax Administration
NTC 2004	24 and 25 August 2004	Sunway Lagoon Resort Hotel, Selangor	Gaining A Competitive Edge
NTC 2005	15 and 16 August 2005	Putrajaya International Convention Centre (PICC)	An Effective Tax Regime, A Joint Responsibility
NTC 2006	22 and 23 August 2006	Putra World Trade Centre (PWTC)	Moving Forward, Managing Changes

National Tax Conference 2007

We are proud to announce that this is the seventh consecutive year for the National Tax Conference and this year's theme is *"Progressing with the Nation"*.

The NTC 2007 is scheduled to be held on 17 and 18 July 2007 (Tuesday and Wednesday) at the Kuala Lumpur Convention Centre.

Puan Hasmah bt Abdullah, Director General of Lembaga Hasil Dalam Negeri Malaysia, Tuan Haji Abdul Hamid bin Mohd Hassan, President of MIT and Co-Organising Chairmen, Puan Noor Azian bt Abdul Hamid and Mr Khoo Chin Guan in discussion.

Puan Hasmah and her officials during the discussion of the NTC 2007 programme.

The NTC 2007 promises to be one of the most exciting and important conferences in the area of taxation. This year, we expect to bring together approximately 1000 to 1500 delegates.

The key areas to be discussed during the Conference are:-

- Forum Discussion: Malaysian Taxation System in the Context of the Current Global Economic Environment
- LHDNM: Progressing with the Nation
- Towards an Efficient and Transparent Tax System – the Key to Successful Implementation of Advance Rulings and Audit & Investigation Frameworks
- Legal Issues
- GST: Progress Report/Readiness
- Malaysian Islamic Financial Centre: Tax and Business Issues
- Taxation & Globalisation: Impact on SME's
- Tax Planning for Overseas Investments
- Transfer Pricing: Recent Trends & Developments in Audit

Therefore, the Organisers would like to take this opportunity to invite you to participate in the most exciting and important tax conference in Malaysia.

Contact us NOW to avoid disappointment !

Tel : 03-2162 8989
Fax : 03-2162 8990/03-2162 3567

Registration & Enquiries

Latha : ext 108 **Elaine** : ext 115
Ellie : ext 113

Email : ntc@mit.org.my /
: cpd@mit.org.my

Sponsorship & Exhibition

Nur : ext 106
email: nur@mit.org.my

Institute News

Akademi Percukaian Malaysia (APM) visit to MIT 13 April 2007

(from left to right) Mr Khoo Chin Guan (Vice President, MIT), Ms Sunita Nathan (Executive Director, MIT), Puan Noor Azian bt Abdul Hamid (Director, APM), En Mansor bin Hassan (Deputy Director, APM), Ms Esther A.P.Koisin (Principal Assistant Director, International Training Centre, APM), Ms Katerina Maria bt Abu Bakar (Assistant Director, International Training Centre, APM) and Ms Nursalmi Haslina bt Muhd Rusli (Manager Events and Conference Management, MIT)

Tax Risk Management Seminar 3 May 2007

The Tax Risk Management Seminar held on 3 May 2007 at the Berjaya Times Square & Convention Center was well attended. Member's feedback was that despite a bit of content overlap here and there the Seminar was generally well received. Being a new area of emerging importance members were happy to be given a chance to become aware of and know a bit about the topic.

All our speakers were excellent as was the representative from LHDNM, Encik Che Omar bin A. Rahaman, Deputy DG (Compliance) of LHDNM. Attached below are photographs of the event.

Oops! That's not Dr. Joseph Eby Ruin, that's actually Encik Che Omar bin A. Rahaman, Deputy DG (Compliance) of LHDNM with Mr. Kang Beng Hoe the able Chairman for the Seminar.

Participants at the seminar in full concentration...

Farewell to Ms Mohana Devi 11 May 2007

MIT bids Ms Mohana Devi, Manager, Communications of MIT a fond farewell. Ms. Mohana was one of the longest serving Secretariat staff having joined in June 2001.MIT wishes her all the BEST always and all ways!

Welcome to Ms Lim Jiew Yan, MIT's new Technical Manager

AOTCA visit 16th - 18th May 2007

Asia-Oceania Tax Consultants' Association (AOTCA) will be holding their ***Annual General Meetings and the AOTCA's 2nd International Convention in Malaysia*** at the ***Kuala Lumpur Convention Centre from the 21st to the 23rd of November 2007.***

This year MIT has been allotted the honor of hosting the same. In conjunction with the abovesaid events, the AOTCA President Mr. Kinjiro Mori and Ms. Junko Kashiwagi visited us to view the meeting and convention facilities. They also paid courtesy visits to LHDNM and MOF.

The AOTCA was formed in 1992 in Japan. Its members' are made up of tax associations from various countries including Japan, Korea, India, China, Hong Kong, Malaysia and Australia.

Standing from left to right
Ms.Junko (AOTCA Secretariat Japan), Tuan Hj Abdul Hamid bin Mohd Hassan (MIT President), Mr. Kinjiro Mori (President AOTCA), Datuk Aziyah Bahauddin (Under Secretary of Tax Analysis Division, MOF), Mr. Khoo Chin Guan (Vice President, MIT) Puan Siti Halimah Ismail (Senior Deputy Secretary of Tax Analysis Division, MOF)

Standing left to right
Ms. Junko (AOTCA Secretariat Japan) and Ms Sunita Nathan (Executive Director, MIT)

Seated from left to right
Mr. Kinjiro Mori (President AOTCA), Tuan Hj Abdul Hamid bin Mohd Hassan (MIT President), Mr. Khoo Chin Guan (Vice President, MIT)

Unfortunately due to some technical problems we have no photos of their visit to LHDNM where they met up with all 4 of the Deputy DG's.

So please look out for our next issue for more news on the AOTCA's 2nd International Convention in Kuala Lumpur!

Malaysian Institute Of Taxation

15 Years of MIT

First Council 1991 - 1992

Sitting from the left: *Hamzah HM Saman (Vice President), Tan Sri Lim Leong Seng, Teh Kok Leong (Deputy President), Ahmad Mustapha Ghazali (President), Dato' Hanifah Noordin, Lee Hwa Beng (Vice President), YM Raja Arshad Raja Tun Uda.*

Standing from the left: *Lee Beng Fye, Yeoh Chong Swee, Yong Poh Chye, Ramli Ibrahim, Michael Loh (Honorary Secretary), Chow Kee Kan, Ranjit Singh.*

Not in picture: *Ashari Ayub, Dr Arjunan Subramaniam.*

Fifteenth Council 2006 - 2007

Sitting from the left: *Dr. Veerinderjeet Singh, Mr. Lim Heng How, Tuan Haji Abdul Hamid bin Mohd Hassan, Mr. Khoo Chin Guan, Mr. Harpal Singh Dhillon.*

Standing from the left: *Mr. Chow Kee Kan, Dr. Ahmad Faisal bin Zakaria, Mr. Adrian Yeo Eng Hui, Mr. Lim Kah Fan, Mr. Aruljothi a/p Kanagaretnam, Mr. Venkiteswaran Sankar, Dato' Liew Lee Leong @ Raymond Liew*

Not in picture: *En Nujumuddin bin Mydin, Prof Dr. Jeyapalan Kasipillai, Mr. Lim Thiam Kee(Peter), Mr. Neoh Chin Wah*

I joined the MIT shortly after its inception about 16 years ago. Although membership of the MIT was frowned upon by my boss, then, I went ahead as I thought it was a professional institution with noble objectives. I have not regretted that decision as over the years the MIT has grown to be the professional tax body that can competently cater to and advance the interests of the tax practitioners and also participate actively and effectively in resolving issues confronting members in particular and other tax professionals in general. I salute the far sighted vision of the founder members.

I am proud to say that the MIT has matured and now has the ears of the Ministry of Finance, the Inland Revenue Board and other relevant government bodies with respect to tax proposals and reforms. I hope this participative relationship will endure and strengthen in the years ahead and MIT will be the sole professionally recognized authority on taxation in the country helping to shape taxation policies and helping members enhance their technical and professional capabilities.

MIT will only grow in strength if it has the strength of membership and the will to forge ahead, led by a Council that comprise people with competence and integrity and dedicated to the cause and interests of the members. It is imperative that the tax practitioners and the professionals give their full support to the Institute.

Mr. Lim Heng How
(Currently Deputy President, MIT)

Second Council 1993 - 1994

Sitting from the left: Chow Kee Kan, Ramli Ibrahim, Michael Loh (Deputy President), Ahmad Mustapha Ghazali (President), Hamzah HM Saman (Vice President),Lee Hwa Beng (Vice President) and Lee Beng Fye.

Standing from the left: Seah Cheoh Wah, Atarek Kamil Ibrahim, Harpal Singh Dhillion, Chuah Soon Guan (Hononary Secretary), Quah Poh Keat and Ranjit Singh.

Not in picture: Lee Lee Kim, Teh Kok Leong, and Yong Poh Chye.

Third Council 1994 - 1995

Sitting from the left: Seah Cheoh Wah, Quah Poh Keat, Hamzah HM Saman (Vice-President), Michael Loh (Deputy President), Ahmad Mustapha Ghazali (President), Chow Kee Kan (Vice-President), Chuah Soon Guan (Honorary Secretary), Tn Hj Abdul Hamid Mohd Hassan

Standing from the left: Syed Amin Al-Jeffri, Kang Beng Hoe, Atarek Kamil Ibrahim, Harpal Singh Dhillon, Ranjit Singh, Chooi Tat Chew, Lee Lee Kim

Not in picture: Lee Yat Kong, Tan Sri Lim Leong Seng (Advisor to the Council)

Fourth Council 1995 - 1996

Sitting from the left: Quah Poh Keat, Chuah Soon Guan (Honorary Secretary), Michael Loh (Deputy President), Ahmad Mustapha Ghazali (President), Hamzah HM Saman (Vice President), Chow Kee Kan (Vice-President), Seah Cheoh Wah

Standing from the left: Lee Yat Kong, Atarek Kamil Ibrahim, Ranjit Singh, Teh Siew Lin, Kang Beng Hoe, Veerinderjeet Singh

Not in picture: Syed Amin Al-Jeffri, Abdul Hamid Mohd Hassan, Harpal Singh Dhillon

Fifth Council 1996 - 1997

Sitting from the left: Quah Poh Keat, Chow Kee Kan (Vice-President), Michael Loh Pooh Kee (Deputy President), Ahmad Mustapha Ghazali (President), Hamzah H.M. Saman (Vice-President), Tony Seah Cheoh Wah

Standing from the left: Ranjit Singh s/o Maan Singh, Chuah Soon Guan (Honorary Secretary), Lee Yat Kong, Atarek Kamil Ibrahim, Teh Siew Lin, Veerinderjeet Singh, Thanneermalai a/l SP SM Somasundaram, Abdul Hamid bin Mohd. Hassan, Kang Beng Hoe

Not in picture: Harpal Singh Dhillon

Sixth Council 1997 - 1998

Sitting from the left: Hamzah HM Saman (Vice-President), Michael Loh (Deputy President), Ahmad Mustapha Ghazali (President), Chow Kee Kan (Vice-President), Teh Siew Lin

Standing from the left: Ranjit Singh, Chuah Soon Guan (Honorary Secretary), Kang Beng Hoe, Veerinderjeet Singh, Lee Yat Kong, Abdu Hamid Mohd Hassan, Seah Cheoh Wah, Quah Poh Keat

Not in picture: Dato' Hanifah Noordin, Harpal Singh Dhillon, Atarek Kamil Ibrahim Thanneermalai a/l SP SM Somasundaram

Seventh Council 1998

Sitting from the left: Quah Poh Keat (Vice-President), Michael Loh (Deputy President), Ahmad Mustapha Ghazali (President), Hamzah H.M. Saman (Vice-President), Teh Siew Lin

Standing from the left: Atarek Kamil Ibrahim, Lee Yat Kong, Kang Beng Hoe, Tony Seah Cheoh Wah, Abdul Hamid Mohd Hassan, Chuah Soon Guan (Honorary Secretary), Jeyapalan Kasipillai, Chow Kee Kan, SM Thanneermalai

Not in picture: Veerinderjeet Singh, Harpal Singh Dhillon

MIT's formation in 1991 was to address the need to have a specialized body that can look after the interest of taxation professionals in Malaysia. At that time, I was one of the first Council members in MIT who represented the MIA Council, the sponsoring body.

Over the last 16 years since its formation, MIT has grown into a mature professional body whose authority on tax matters is being sought after by many, which includes government authorities, the public and other professional bodies-both, locally and overseas. MIT's close working relationship with the Inland Revenue Board has resulted in the success of many jointly-organized conferences and seminars which have benefited the members and the public.

Other notable achievements include MIT's role in the Asia Pacific region through its active participation in the AOTCA and its enhanced relationship with the major taxation bodies in Europe and America. MIT's Helpdesk is an excellent way where members' needs could be attended to and a good form of feedback of how services can be further improved. The facilities at MIT's new premises will help to cater for the expected increase in the number of members and students.

There are vast opportunities for MIT to further expand its membership base through aggressive promotion and membership recruitment drive. By promoting the Professional Examinations, MIT could also attract more new students.

In the longer term, I would like to see MIT obtain a 'chartered' status befitting of a reputable taxation body in Malaysia. It should also play a leading role in the ASEAN region in assisting the underdeveloped countries like Vietnam, Cambodia and Laos in developing their taxation systems and the tax profession.

Ahmad Mustapha Ghazali – Past President of MIT, currently Honorary Advisor

Teleconversation / Telephone Reminiscences on 21 May 2007

Mr. Michael Loh is one of the founding members who, together with Mr. Yeoh Chong Swee, mooted the idea of setting up MIT in the late 1980s as a professional body to represent tax professionals to deal with the then IRD and the relevant Government authorities. Together with the promoters as stated in the M&A, MIT was registered in 1991. Now retired from active practice MIT is still one of his passions. Herein below are his reminiscences:

"We tried for a long time to get the necessary approvals to set up MIT. Finally we had the assistance of the Malaysian Institute of Accountants (MIA) to help us in getting all the necessary approvals. In addition MIA also assisted us by providing us with the office premises and secretarial staff as MIT was not financially strong initially. In return MIT assisted MIA in their Tax functions. This symbiotic arrangement worked extremely well for both the professional bodies. We were very grateful to MIA for helping us to find our feet. But I am glad to say that MIT has since matured including having its own premises, secretariat and a full complement of staff. This is indeed an achievement.

MIT was conceived and proposed as a body to represent Malaysian tax professionals and the tax profession as a whole. Even at the end of the 1980's and early 1990's, with the onset of the concepts of globalisation, cross border transactions and so on, it was already clear that the taxation profession was entering a new level. The profession needed to prepare itself for self regulation and set standards for all Malaysian practitioners.

I am proud to say that MIT has achieved a lot despite its short history as it is now one of the premier Professional bodies which conduct annual examinations to train and churn out Tax Professionals for the industry. Many registered students have since sat for the examinations of the Institute and qualified as associate members. Their qualifications have been greatly valued and sought after by most public accounting firms. This is one of the most economical ways to train tax specialists.

My vision, and I believe the vision of many of the founding fathers of MIT, is for MIT to be the governing body for tax practitioners in Malaysia with licensing, regulatory and sanctioning powers to maintain and improve the quality of the tax profession in Malaysia. I would like to see MIT achieving this in the not so distant future.

Finally, I wish MIT Happy 16th Birthday and continue the good work!

Mr Michael Loh
Founder Member

Eighth Council 1999 - 2000

Sitting from the left: Chuah Soon Guan (Honorary Secretary), Michael Loh (Deputy President), Ahmad Mustapha Ghazali (President), Hamzah H.M. Saman (Vice-President), Teh Siew Lin

Standing from the left: Lee Yat Kong, Abdul Hamid bin Mohd. Hassan, Atarek Kamil Ibrahim, Veerinderjeet Singh, Jeyapalan Kasipillai, Tony Seah Cheoh Wah, Ahmad Faisal bin Zakaria

Not in picture: Quah Poh Keat (Vice-President), Harpal Singh Dhillon, Chow Kee Kan, SM Thanneermalai

Ninth Council 2000 - 2001

Sitting from the left: Quah Poh Keat (Vice-President), Michael Loh (Deputy President), Ahmad Mustapha Ghazali (President)

Standing from the left: Harpal Singh Dhillon, Venkiteswaran Sankar, Chow Kee Kan, Teh Siew Lin, Dr. Veerinderjeet Singh, Lee Yat Kong, Dr Ahmad Faisal Zakaria

Not in picture: Tn Hj Atarek Kamil Ibrahim, Dr Jeyapalan Kasipillai, SM Thanneermalai, Tony Seah Cheoh Wah

Tenth Council 2001 - 2002

Sitting from the left: Quah Poh Keat (Vice-President), Michael Loh (Deputy President), Ahmad Mustapha Ghazali (President), Chan Kee Kan (Honarary Secretary), Tn Hj Abdul Hamid bin Mohd Hassan (Vice President)

Standing from the left: ***Venkiteswaran Sankar,*** *Harpal Singh Dhillon, Dr. Veerinderjeet Singh, Lee Yat Kong, Teh Siew Lin, Dr Ahmad Faisal Zakaria*

Not in picture: Tn Hj Atarek Kamil Ibrahim, Dr Jeyapalan Kasipillai, SM Thanneermalai, Tony Seah Cheoh Wah, Alvin Richard Thornton

Thirteenth Council 2004 - 2005

Sitting from the left: Dr. Veerinderjeet Singh, Harpal Singh Dhillon, SM Thanneermalai,Tn Hj Abdul Hamid bin Mohd Hassan (Vice President), Lim Heng How, Dr Jeyapalan Kasipillai,Venkiteswaran Sankar,

Standing from the left: Adrian Yeo Eng Hui, Andrew Kok Keng Siong, Raymond Liew, Lim Kah Fan, Aruljothi, Dr Ahmad Faizal bt Zakaria, Khoo Chin Guan, Neoh Chin Wah.

Not in picture: Tn Hj Atarek Kamil Ibrahim, Tony Seah Cheoh Wah, Alvin Richard Thornton

Fourteenth Council 2005 - 2006

Standing from the left (first row): Nujumuddin bin Mydin, Chow Kee Kan, Ahmad Mustapha Ghazali, Tn Haji Abdul Hamid (President), SM Thanneermalai, Dr Veerinderjeet Singh,

Standing from the left (second row): Harpal Singh Dhillon, Neoh Chin Wah, Lim Heng How, Dr Jeyapalan, Andrew Kok, Venkiteswaran Sankar

Not in picture: Tn Hj Atarek Kamil Ibrahim, Tony Seah Cheoh Wah, Alvin Richard Thornton

Together with others, I am one of the founding members of MIT. In the days before the establishment of MIT , tax literature, and therefore, tax education was limited and hard to come by. Most of the professionals with in depth tax knowledge were ex-inland revenue officers.

The training and facilities for training tax professionals was limited. Ressource books and materials on Malaysian taxation were not as widespread as currently. Tax Institutes or Tax Foundations were the basis of tax knowledge and training of tax professionals in other countries. Toward this objective, that is, to provide facilities for training of tax professionals and increasing tax expertise avaiable in the country, I was a member of a team who went on to establish M.I.T.

MIT 's achievements are obvious. MIT has raised the bar of professional conduct and expertise of tax professionals. One of the main areas, I would say is training facilities by way of courses in taxation offered to new and budding tax professionals. MIT has also impacted tax policy changes in Malaysia. In other words, MIT's contribution to tax reform has been significant. The publication of the Tax National is another mile stone.

Tax National needs to be developed as a leading Malaysian tax journal. As it stands, there are few quality articles on taxation aspects. More writers need to be encouraged to write in depth articles. An «ÊInsightÊ» section should be introduced to analyse various aspects of a single issue or topic. Having said that, Tax Nasional is still contributing significantly in the field of tax knowledge.

The Institute itself could one day offer courses in various aspects of taxation at a degree level, and towards this objective should work with one of the institutions of higher learning. Alternatively I would prefer it if MIT would set up a training institute i.e. your own building with permanent teaching staff.

Wishing MIT & its staff every success.

DR.Arjunan Subramaniam
Arjunan & Co

Technical Updates

(2nd Quarter – as at 15 May 2007)

Legislation

Gazette Orders

Real Property Gains Tax (Exemption) Order 2007 [P.U. (A) 120]

All schemes of merger of a licensed discount house, licensed merchant bank or dealer for the purpose of forming an investment bank are exempted from Real Property Gains Tax provided the following conditions are complied with:

(i) A complete and detailed submission of documents for approval by the Central Bank of Malaysia or the Securities Commission pursuant to the Banking and Financial Institutions Act 1989 or the Securities Industry Act 1983; and

(ii) Submission of other documents required by the Central Bank of Malaysia or the Securities Commission.

The above is effective from 1 July 2005 until 30 June 2007

Real Property Gains Tax (Exemption) (No. 2) Order 2007 [P.U. (A) 146]

Disposals of chargeable assets by all persons are exempted from all provisions of the Act.

The above is effective from 1 April 2007

Income Tax (Exemption) (No. 8) Order 2007 [P.U. (A) 108]

Interest received by a non-resident depositor from Hong Leong Islamic Bank Berhad is exempted from income tax. Notwithstanding this, the non-resident depositors are required to submit any return, statement of accounts or other information required under the law.

The above is effective from Year of Assessment 2006

Income Tax (Exemption) (No. 13) Order 2007 [P.U. (A) 155]

Interest received by a non-resident depositor from AmIslamic Bank Berhad is exempted from income tax. Notwithstanding this, the non-resident depositors are required to submit any return, statement of accounts or other information required under the law.

The above is effective from Year of Assessment 2006

Service Tax (Amendment) Regulations 2007 [P.U. (A) 119]

Amendments were made to the Second Schedule, Group G, Subheading III of the Service Tax Regulations 1975 as follows:

Deletion of:

Item 1: "Taxable Person":

"Any person who operates one or more private veterinary clinics having a total annual sales turnover, whether combined or singly, of more than RM300,000 of any one or more taxable services mentioned within this Group."

Item P: "Taxable Service":

"Provision of veterinary services."

The above is effective from 5 September 2006

Stamp Duty (Exemption) (No.2) Order 2007 [P.U. (A) 126]

All instruments in a merger of a licensed discount house, licensed merchant bank for the purpose of forming an investment bank are exempted from stamp duty provided the following conditions are complied with:

(iii) A complete and detailed submission of documents for approval by the Central Bank of Malaysia or the Securities Commission pursuant to the Banking and Financial Institutions Act 1989 or the Securities Industry Act 1983; and

(iv) Submission of other documents required by the Central Bank of Malaysia or the Securities Commission.

The above is effective from 1 July 2005 until 30 June 2007

Income Tax (Exemption) (No.9) Order 2007 [P.U. (A) 137]

Exemption of income tax on statutory income from operating domestic tours for companies licensed under the Tourism Industry Act 1992 provided the following conditions are met by each company:

(i) A certification from the Ministry of Tourism for at least 1,200 local tourists for a year of assessment; and

(ii) A separate account is maintained for income derived from domestic tours

The above is effective from Year of Assessment 2007 until Year of Assessment 2011.

Income Tax (Exemption) (No.10) Order 2007 [P.U. (A) 138]

Exemption of income tax on statutory income from operating group inclusive tours for companies licensed under the Tourism Industry Act 1992 provided the following conditions are met by each company:

(i) A certification from the Ministry of Tourism for at least 500 tourists from outside Malaysia in group inclusive tour for a year of assessment; and

(ii) A separate account is maintained for income derived from domestic tours

The above is effective from Year of Assessment 2007 until Year of Assessment 2011.

Income Tax (Exemption) (No. 12) Order 2007 [P.U. (A) 154]

Exemption of income tax on statutory income for a 'qualifying person", i.e., International Islamic Bank, International Takaful Operator or International Currency Business Unit, on their business and "qualifying Ringgit account", i.e., an account of investment made in Ringgit Malaysia which is related and incidental to the business of a qualifying person and approved by the Central Bank of Malaysia.

Notwithstanding this, they are required to submit any return, statement of accounts or other information under the law and to maintain a separate account for the said income.

The above is effective from Year of Assessment 2007 until Year of Assessment 2016.

Income Tax (Deduction For Advertising Expenditure on Malaysian Brand Name Goods) (Amendment) Rules 2007 [P.U. (A) 171]

Amendments were made on rule 5, "Qualification for deduction" as follows:

(i) Renumbering of rule 5 as subrule "(1)";

(ii) Substituting paragraph (1)(b) with the following:

"(b) the company is the registered proprietor ***or related to the registered proprietor*** *of the Malaysian brand name used in the advertisement";* and

(iii) insertion of subrule (2) with qualifying criteria for determination of a related company to the registered proprietor of the Malaysian brand name use in the advertisement.

The above is effective from Year of Assessment 2007

Income Tax (Deduction For Allowances Under The Capital Market Graduates Training Scheme) Rules 2007 [P.U. (A) 172]

Double deduction for allowances paid to a trainee for undergoing the training scheme for 3 years from the date of certification of the training scheme. A company is required to produce a letter issued by the Securities Commission certifying the trainees and the allowances incurred in order to qualify for the deduction.

The above is effective from 2 September 2006

Income Tax (Deduction For The Cost Of Issuance Of The Islamic Securities) Rules 2007 [P.U. (A) 176]

Cost of issuance of the Islamic securities incurred by a special purpose company is allowable as a deduction.

The above is effective from Year of Assessment 2007

Income Tax (Exemption) (No. 14) Order 2007 [P.U. (A) 180]

Exemption of income tax for a special purpose company (SPC) on income derived from issuance of Islamic securities. SPC shall maintain a separate account for the said income.

The above is effective from Year of Assessment 2007

Double Taxation Relief (The Government of The Bolivarian Republic of Venezuela) Order 2007 [P.U. (A) 175]

Some salient points include:

Permanent Establishment (PE) (Article 5)

PE includes:

- a building site, a construction, installation or assembly project if it lasts more than 9 months;
- supervisory activities for the above-mentioned activities if it is more than 6 months

Withholding Tax Rates

Dividends (Article 10)	- 5% (if the beneficial owner is acompany which has a direct shareholding of at least10%);or
	- 10% (for all other cases)
Interest (Article 11)	- 15%
Royalties (Article 12)	- 10%
Fees for Technical Services	- 10%

- Customs (Customs Ruling) Regulations 2007 [P.U. (A) 149]
- Excise (Customs Ruling) Regulations 2007 [P.U. (A) 150]
- Sales Tax (Customs Ruling) Regulations 2007 [P.U. (A) 151]
- Service Tax (Customs Ruling) Regulations 2007 [P.U. (A) 152]

Some salient points in respect of the above rulings are as follows:

(i) Application of customs ruling

- Processing fee – RM200
- Application deemed withdrawn if information required is not provided on a timely basis.

(ii) Issuance of customs ruling

Upon receipt of the application, the DG may request for an analysis to be conducted before a customs ruling is made. Thus, the period required for issuance of a customs ruling varies such as follows:

- Without analysis – within 90 days after receipt of complete documents and processing fee.

- With analysis – within 150 (90 + 60) days from the receipt of analysis report and settlement of analysis fee.

(iii) Validity of customs ruling
- 3 year period but subject to amendments, modifications or revocation.

(iv) Confirmation of basis of customs ruling
- To confirm that the facts on which the ruling was based remain unchanged and that the conditions imposed, if any, have been complied with within stipulated period to avoid the customs ruling from being withdrawn.

(iii) Renewal of customs ruling
- To be submitted not later than 3 months before the expiry date of the customs ruling
- Renewed customs ruling is valid for 2 years

(iv) Request for certified copy of customs ruling
- Fee – RM50

Customs (Customs Ruling) Regulations 2007 – Effective from 1 April 2007

Excise (Customs Ruling) Regulations 2007 – Effective from 5 April 2007

Sales Tax (Customs Ruling) Regulations 2007 – Effective from 1 April 2007

Service Tax (Customs Ruling) Regulations 2007 – Effective from 5 April 2007

Dialogue

Operations Dialogue

The first operations dialogue for year 2007 was held by the Lembaga Hasil Dalam Negeri Malaysia with the professional bodies on 4 April 2007. A copy of the minutes can be downloaded from the Institute's website : *http://mit.org.my/mit03/tech_published_view.asp?eventid=373*

Others

Bank Negara Malaysia

"Liberalisation Of Foreign Exchange Administration Rules" were released with amendments to the following:

(i) ECM 2 – Dealing in Gold and Foreign Currency
(ii) ECM 4 – General Payments
(iii) ECM 6 – Credit Facilities to Non-residents
(iv) ECM 7 – Foreign Currency Accounts
(v) ECM 9 – Invest Abroad
(vi) ECM 10 – Foreign Currency Credit Facilities and Ringgit Credit Facilities from Non-residents
(vii) ECM 15 – Labuan International Offshore Financial Centre
(viii) ECM 16 – Approved Operational Headquarters

The above is effective from 1 April 2007

Iskandar Regional Development Authority (IRDA)

Incentives available to IRDA-status companies:

- Exemption from the Foreign Investment Committee rules;
- Freedom to source capital globally;
- Freedom to employ foreign employees within approved zones;
- Exemption from corporate income tax for 10 years provided operations are commenced before the end of 2015; and
- Exemption from withholding tax on royalty and technical fee payments to non-residents for 10 years from the commencement of operations.

Securities Commission

Amendments to "Guidelines For The Annual Certification For Tax Incentives For the Venture Capital Industry" whereby additional qualifying criteria for Tax Exemption Incentive and Tax Deduction Incentive have been included.

The above is effective from Year of Assessment 2007

IMPORTANT NOTE: MIT Technical Helpdesk Queries

Dear MIT Members,

While every reasonable effort is made to respond to Member's queries to the help desk, please bear in mind that ***the Institute is not authorised to and will not respond to technical queries which are advisory in nature.*** *Members must appreciate that such queries would require a degree of technical expertise and judicial interpretations which may be subjective and peculiar to the circumstances of a particular case. MIT is a not-for profit professional body representing tax practitioners. MIT is not a tax consultant or tax practitioner. At best the help desk can help guide practitioners towards sources of information relating to their queries. But practitioners have to draw their own conclusions to advise their clients.*

For technical queries which are non advisory in nature, *we would like to caution you that opinions given by MIT may not be shared by the Inland Revenue Board or the Ministry of Finance. Furthermore any queries answered by MIT shall not be construed as advisory in nature and MIT is not responsible for any direct or indirect consequences resulting from this.*

For our records of the issues raised, we would appreciate if you could e-mail your full name, membership number and queries to "technical@mit.org.my"

MIT Technical Helpdesk

The DG mingling and motivating his officers

The DG at work with his officers

THE DIRECTOR GENERAL OF ROYAL MALAYSIAN CUSTOMS

Interview with Dato' Sri Haji Abd Rahman bin Abd Hamid

Dato' Sri Haji Abd Rahman bin Abd Hamid, DG of RMC has graced MIT by allowing an indepth interview of himself, not only in his position as the DG of RMC, but also a rarely seen behind the scenes intimate glimpse of himself, his beliefs and his personality.

Having gone through the grindstone of life, he has emerged blessed and resolute to make the Royal Malaysian Customs a Government organisation for all Malaysians to be proud of.

MIT thanks Dato' Sri for his time and effort in providing this interview, specially and exclusively for you dear Members and subscribers of Tax Nasional.

A small note of acknowledgement also to En Mohd Sapin, Mr. ZT See and Puan Noorlida for all their assistance.

INTERVIEW WITH DATO' SRI HJ ABD RAHMAN B ABD HAMID THE DIRECTOR GENERAL OF ROYAL MALAYSIAN CUSTOMS

MIT: Dato' Sri, our readers would love to know a bit about your family and education background. Could you please enlighten us a bit?

ARAH: *I am the fourth in a family of nine and the only boy. My beloved father, Abd Hamid Mohd Top was the kampong imam from the age of 18 and being the only son, my father used to hoist me above his shoulders to the mosque and everywhere else. If he was giving lessons in religious knowledge, I would be sitting on his lap and during prayers, I would be sitting behind him. So you can see how close the bond between my father and me was. My family's religious background helped to shape me into the person I am today. They were there for me and they were ever willing to sacrifice everything for me. I was the son, you know and my parents would go to a lot of trouble for me.*

And in school, I would not like to go deeper...it stirs up too many sad memories for me. My primary school was Sekolah Rendah Kebangsaan Beramang, Muar. During my schooldays, I had no money for exercise books. I used blank papers which I would cut up and tie with wire. I'd wait for the other children to hand in their books before I would quietly hand in mine…because I was ashamed that mine were only loose sheaves of paper tied with wire. The class teacher came and hugged me, and between tears he said, never mind…send it in…it doesn't matter.

It must have wrenched his heart but my father was willing to separate me from my family so I could get an education in the town. I was accepted into Sekolah Menengah Datuk Seri Amar Diraja, Muar before taking up Form Six at Sekolah Menengah Mohd Yassin. I became a boarder to a few families for the next few years until there came a time when I even stayed alone and did everything by myself, cooking, washing…So it was like that for me.

There was also a time in my life when hardship was the norm. I once had to carry a dry gunnysack to help wipe the rubber trees after a downpour. My mother wanted to tap the rubber because we had no money and food was scarce, we were having rice mixed with tapioca.

One thing my father taught me, he instilled in me the belief that I am an excellent son. I don't know, I've never told anyone, even in the kampong, maybe because I am the imam's son, people expect better things of me. People regard me as the best, like my father. Therefore I had to be more vigilant, about everything, especially my personality, reputation even till now.

MIT: Could you please give us a brief history of your career till you were appointed as the DG of Royal Customs?

ARAH: *As an Arts graduate majoring in Malay Literature from University Malaya, I joined the Government service as an Assistant Superintendent of Customs in 1974. My first posting was in Johor Baru where I worked the rounds, doing import and export, prevention, becoming head of station for Subang International Airport and when I was promoted in 1983, I moved to KL where I joined the Industrial Division. I was then transferred to the Headquarters before moving back to Johor as Head of Customs Division.*

I went for my Masters in Public Administration in University of Southern California. One of the more memorable posting was in err…1994 where I was appointed as the Director for the Royal Malaysian Customs Academy or AKMAL in Melaka. You could say it was a halcyon time for me…I got to promulgate my vision of what I conceived as excellence for Customs. I succeeded in making AKMAL as the training arm for the World Customs Organisation or WCO. I also steered AKMAL in winning the DG of MAMPU TQM award. AKMAL also won the Malaysian ' Clean and Beautiful Office' Award.

I was then appointed the State Director of Customs Johor from 1997 to the year 2001. In that state I implemented a lot of innovations like introducing the SSPT or Exclusive Clearance System Scheme, creating a Traffic Control Unit, becoming one of the teaching staff for the Project Management Concept, Snapshot Planning Concept,developing a boot camp in Tanjung Surat, introducing a 5 year Strategic Planning Application, advocating holistic management inclusive of culture and self worth and winning the Secretary of State TQM Award.

I moved back to work in KL when I was promoted as the Deputy Director General of Customs in December 2001 to head the Operations Division. In June 2002 I was asked to head the Preventive Branch and I was there until October Fourth 2005. On 5th October 2005, I attained the highest

post in Customs when I was appointed to the post of Director General of Customs.

MIT: In line with the Government's vision for the RMC to be a department of international stature, the ICTR (Integrity, Core Business, Technology and Rakyat) was launched in January 2006. How successful has this been? Are there any further plans for the continuing success of this vision? Can you comment on that?

ARAH: Can you answer that? Is there success? Ok, for me, its like this, first, in this ICTR, the Customs Officer is more focused towards these four aspects which have become the yearly agenda, where we arranged certain programmes under each heading and we monitor its progress. From that, we can see a lot of changes, developments happening everywhere because we did things according to plan. For example, the message to the officers on Integrity is clear and the officers are expected to know about efforts made by the department to increase integrity compliance. Amongst the challenges in upholding integrity is in educating or disciplining our officers and educating our stakeholders and the public. It is hard to scrape away the public's perception of Customs as a corrupt public agency. We have been stonewalled by this perception throughout the decades. It is one of the prime factor moving me to introduce the concept 'Be Clean, Seen To Be Clean, Smell Clean.'

From the Core Business aspect…we have been focusing on core business and giving it top priority up to a point where everything we did, on the aspects of Integrity, Technology and Rakyat is correlated with Core Business, ok, that forms our excellent performance, and to get that excellent performance, we infused it with technology which is supported by our self worth as a Rakyat, working as a Rakyat who ardently loves his country. And from the impact it had, we can see that Customs as a whole is more unified, what is the slang for that? Gelled together? And our focus is clearer…and feedback from our clients is much better and even the complaints against our weaknesses have subsided somewhat as we strive to correct these defects.

Our action plan is for five years and this is the second year, ok? Whether we are going to continue, we are making sure that our vision is achieved through ICTR. How fast we achieve that, that depends on our efforts, but the momentum towards that will be continued, moreover in our yearly planning, we take into account ongoing changes, for example, the changes in ROF, this, no, what was it? I mean SOP, Standard Operational Procedures of the WCO so that we will really be of a world class standard.

And for Technology, it is a dynamic thing, so our stand in embracing technology will continue because technology itself is not static. And then our efforts in the core business involves not only the product but also human capital, you know right? We have our university twinning programme, e-learning….ok?

To drive home the message, Integrity becomes the criteria for leadership, promotion, career development, even an officer's future in the department depends much on his integrity. We act against those who're lax and we pave the way for those who have integrity.

MIT: The World Customs Organisation through the Revised Kyoto Convention aims to harmonise global customs procedures. What will be the immediate benefit(s) of this proposed harmonisation? How far has RMC progressed in this area?

ARAH: Yes! This is quite simple. World Customs Organisation (WCO) is an international union that has as its members all the Customs administration in the world. And its original aim is to simplify and standardise procedures. So if we can get a standard procedure, ok, we will be in the mainstream of progress along with the rest of the world. Ok, and the early impact for us is the investor's confidence in Malaysia, for example if they want to come to Malaysia, the first element they will look at is the level of our Standard Operating Procedures (SOP)? Whether we fulfil the standard or not. We have progressed a lot in this aspect, a lot of effort has been invested, for example first, we implemented WCO recommendations and guidelines where we lean towards Customs action after importation. Secondly, from the risk management aspect, we have taken action on security, and technology has its standards too, to which we will adhere and fulfil, applying the single window et al.

We say we move in tandem and we are not yet left behind in this aspect. We are committed in following WCO recommendations in standardising, harmonising and simplifying our procedures. We are using the latest technology to enhance our delivery system. For example, the use of a 3G hand phone or communication that enables us to talk and see images 'live' so that our officers can communicate on line with their colleagues either in the headquarters or the stations to confer and confirm classification decisions, thereby arriving at the same decision or code number regardless of which entry point the goods came in.

In many aspects Malaysian Customs is not merely a follower but a partner of WCO. We initiated our own twinning programme, e-learning, ASEAN enforcement, ASEM, audit management…we have led the way forward in these.

MIT: The 'Post Import Verification Unit on Wheels' was launched in January 2007. How effective has this unit been in combating "under declaration" of goods?

ARAH: Let's say it like this, Post Verification is firstly, based on risk management. Secondly, we examine goods because we have a strong reason to examine them. Thirdly,

we gather all our mechanisms within this system to outwit those who try to evade paying tax…under declare, wrongful declaration and the like and the impact we had from this system was a project where we managed to detect and collect a few millions in a few days. Nevertheless how far we can implement this will have to wait for the ICT system to be completed because we believe it will help to accelerate and develop this procedure…but one certainty is that companies will get a faster clearance.

MIT: In order to create a 'Customs Literate Society', the Malaysian Customs has signed a MoU with Universiti Utara Malaysia in June 2006 to launch a number of courses in Customs procedures from certificate level to doctorate level. Do you see a good response? Do you think these courses actually create a 'Customs Literate Society'?

ARAH: Ha, this one is a lot, now even the university students are taking up courses, recently there were 250 of them learning. This shows there is a good response for the course. Even those Customs Agents are being recognised because they are certified by the university. The subjects range from certificate level to a doctorate. So in the future, Customs subject will be a mainstream subject in the country and we hope, those teaching the subject will take up certificates, diplomas or degrees in this subject. And the most important thing that is the message coming out to the public is, if you want to deal in trade or commerce, you must know Customs legislation and procedures well. So in the end, yes, these courses do create a 'Customs Literate Society.'

MIT: Dato' Sri, what do you think is an effective way for taxpayers to address their grievances on administrative matters to RMC and the way for RMC to respond?

ARAH: Ok, firstly our office is an open office concept, we are more open, and you have your unions and societies. Secondly, you don't have to use third parties in dealing with us, the public can come direct because Malaysian Customs have a 'round table' concept of discussion. Then there is the hotline. They can use the hotline for enquiries, complaints, giving information on illegal activities, air their grievances… What they must do is to come to the right person. Mostly they come with somebody who claims he or she have the authority to help solve their problems. Now our officers are more open, more transparent, the public can come and discuss. The government has also implemented the Advance Ruling, and introduced the Customs Tribunal Appeal board to receive and expedite cases, especially appeals from clients regarding classification, valuation, licencing, manufacturing definition et al.

We also have a twice yearly Consultative Panel Meeting between RMC and the Private Sector. Whatever issues that need to be aired concerning procedures, workflow, legislation, human resource or other administrative matters can be discussed at these meetings.

MIT: How about tax agents? Do they also have a way to address their grievances?

ARAH: Like I said, they have their unions, and their unions can come to the Customs office anytime, ok? And then our officers in the states, they are not merely tax collectors, there are also the administrative and financial officers, and therefore the agents should come to these officers. And if they are not satisfied, they can come direct to the DG. They can inform the DG and usually the DG will take action to rectify the matter.

MIT: In your opinion Dato' Sri, what is the role of MIT in the tax profesion? How can MIT play a more proactive role to assist RMC?

ARAH: For me, firstly, MIT's role can be seen as assisting Customs in creating a 'Customs Literate Society.' They can help educate the public on Customs rules and regulations. Secondly, they can become the link between their members and Customs to get the correct picture and avoid preconceived opinions about the department. Thirdly, they should give feedback to us.

MIT: Can you describe the most memorable incident in you career?

ARAH: When the former DG, the late Dato' Mohd. Nor Hamid, on his last visit to AKMAL, called me and said…I am his chosen successor for the future and he hoped in the next era, the Customs man will have a renaissance. From that day onwards I became a very responsible person, having faith in myself that I would one day be a leader and I never looked back since.

MIT: In your opinion Dato' Sri, what is the role of MIT in the tax profesion? How can MIT play a more proactive role to assist RMC?

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the next era, the Customs man will have a renaissance. From that day onwards I became a very responsible person, having faith in myself that I would one day be a leader and I never looked back since.

MIT: Describe the least memorable incident of your career in Customs?

ARAH: Me? Incident? When I was slandered and I couldn't defend myself, you all know that, don't you? I was slandered and I felt like I've been isolated…by insinuations about things which never crossed my mind and I had no avenue to counter these accusations…because I was prejudged. But I held on to what my father reminded me, "A slander will not scratch anything. It is better to have patience. If we are in the right, a slander will not harm a hair on our body, therefore hold fast to God Almighty…"

MIT: What are your favourite past times and what do you do away from office to relieve stress Dato' Sri?

ARAH: Umm? If I am facing some problems, I go fishing. If I feel too comfortable I read.

MIT: Whom do you consider your role model or idol?

ARAH: Dato' Mohd. Nor Hamid. He tried to free the Customs mentality from the shackles of colonialism. He hated old timers who were still living a hedonistic life full of decadence, yet they acted as if they were little emperors. It was as if every working day, every drop of ink from his pen was dripping with vengeance…I could feel it. He was not an orator, he was more a writer, very structured in his thinking. His only problem was he had dry hands when he shakes your hand, its as if he had no feelings. I have a lot of emotions, feelings, my hands are warm. He? He can't express his feelings, even his wife was confused when in fact he loved her, and it led to his marriage breakdown. To me he had an extraordinary talent, he had extra sensory perception and he could foretell the future accurately. Only thing is he forgot the human touch but he taught me to think seriously, to put aside petty considerations, in fact pretty much groomed me to be his successor.

MIT: How do you divide your busy schedule between career and family? How does your family respond to your busy schedule?

ARAH: Me? Umm…its like this…firstly, all my children and my wife understand my commitment to my work, ok? And when I come home I'm not the DG, I become the husband, father, friend…sometimes even my wife is embarrassed with my behaviour at home, its totally different from my office demeanour, I enjoyed the shared moments with my children.

How does my family respond to my schedule? They ardently wait for the times I'm home. My children accepted that I'm a busy man and they wait when I can free myself from my schedule so we could spend the day together, going bowling…if my children are all home we would eat out together, I also indulge in karaoke sessions with my wife and children in a room, they play the guitar and I'd sing, ok? Happiness is in gardening together. My adage is, the family that gardens together stay together…hahaha…

Actually to tell you the truth, I might be the man who does not have trouble at home. I nearly don't have any trouble because maybe my wife is my friend first and she is the person who has stayed beside me through thick and thin. Therefore I find comfort at home because my wife does everything in her power to make life easy for me, she pays the bills, runs errands and everything else. I also bring my family along on weekends when, say…I go visiting Customs quarters. One of my children would be driving us, so I make my work enjoyable. Sometimes I ask my son or daughter to write down my speeches as I dictate.

MIT: In your illustrious career Dato' Sri, whom do you consider to be the person who has been supportive and the driving force behind your success?

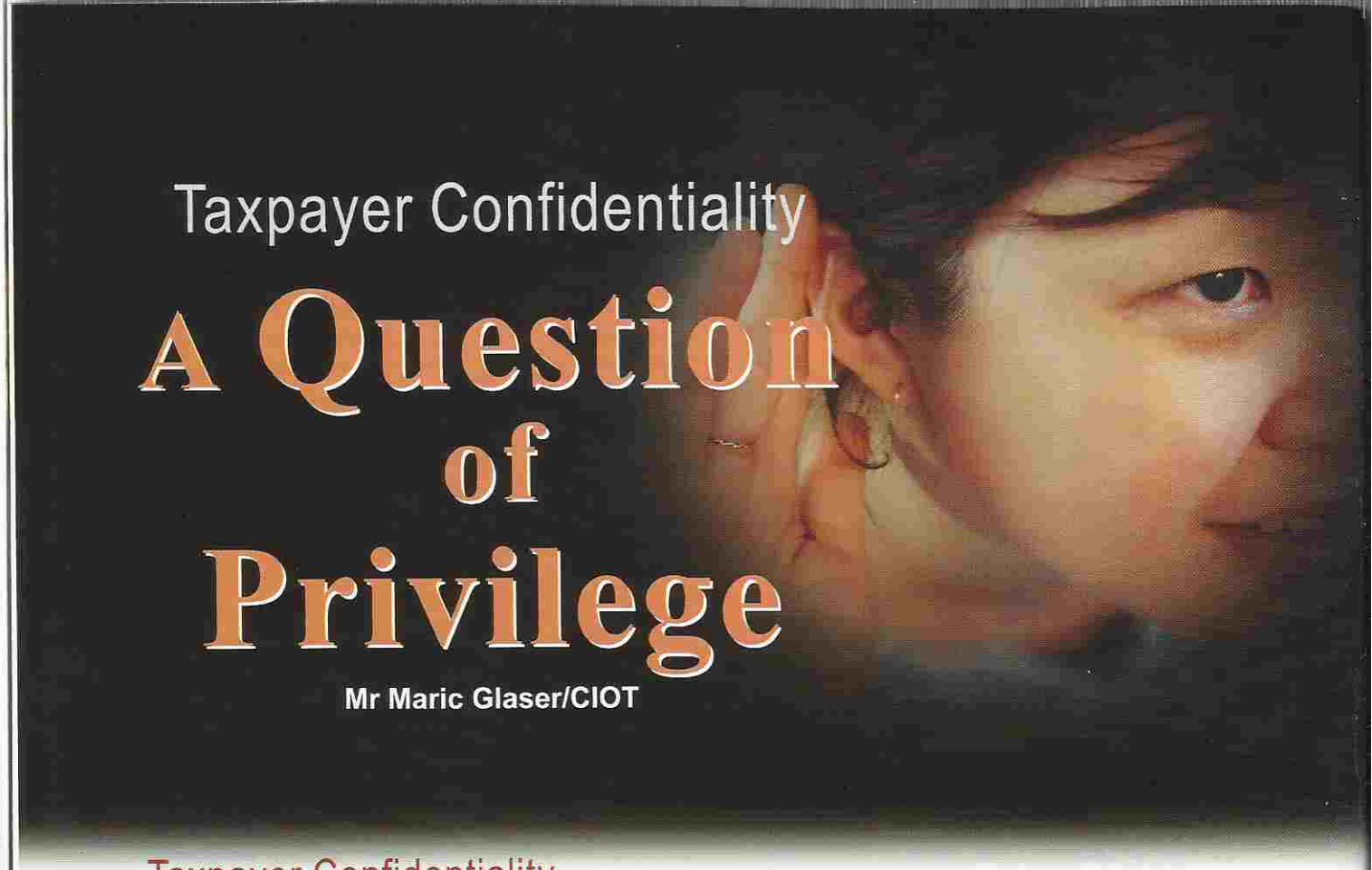
ARAH: My late father's voice. Its as if he had never left me all my life. I've always felt like I'm being watched. Maybe its because of my admiration for his leadership.

Secondly, my wife, because she fills my life with bliss.

Thirdly, my children for being proud of their father. They never doubted me. And they never took advantage of my position. Even to the extent of never wearing a shirt with a Customs' logo.

So I was never troubled, not even by my relatives or my kampong people. They have known me since childhood, so they never beleaguer me with requests…well they might ask for a bit of capital to buy a sampan or two but never about work. But the most important thing is, I have never felt burdened by my job or my success.

And my hope for the Customs people is that they must master their core business, we must be recognized and respected because of our knowledge, skills and contributions towards our core business. The people who want to succeed in Customs, those who are vying for promotion must be selected based on their ability to tackle the core business, not in other matters. We must not commit the mistake of appointing somebody because we are dazzled by their charms or talent outside the core business because it will ruin Customs. However, my expectation for all Customs officers is for them to master every aspect of the job and to master different kinds of knowledge. And never dwell on past failures, instead be a master of your own destiny. That's all.



Taxpayer Confidentiality

A Question of Privilege

Mr Maric Glaser/CIOT

Taxpayer Confidentiality

The right to privilege in today's complex legal system is precious, and HMRC must not try to erode it, argues Maric Glaser.

The High Court emphasised the importance of legal and professional privilege in the case of *General Mediterranean Holdings*.[1]

'Now that this Court has held that legal professional privilege is not a rule of evidence but a substantive rule of law, the best explanation of the doctrine is that it is "a practical guarantee of fundamental, constitutional or human rights".'

In relation to taxation, there has been continuing tension over the question of whether the public interest in the proper collection of taxation should override privilege. The importance of the principle was emphasised by Lord Hoffmann in *R (Morgan Grenfell & Co Ltd)*.[2]

What is clear is that the Courts will only override legal and professional privilege where compelled to do so by a specific and unequivocal law.

Unlike constitutional jurisdictions, legal and professional privilege arises not from statute but from Common Law. That means that it is capable of changing as circumstances demand. I contend in this article that changes in the way people seek advice, coupled with the development of human rights law, public policy and European Community law, lead to the inevitable conclusion that privilege needs to apply between legal adviser and client regardless of the adviser's status – lawyer or otherwise.

Legal and professional privilege is frequently referred to in two parts – litigation privilege and advice privilege. This article does not distinguish between the two because it is contended that the objectives behind privilege apply equally to both.

Reasons for extending the application of legal and professional privilege

The development of the principle of privilege and public policy

The representation of taxpayers has developed on a number of fronts. In her work on legal and professional privilege,[3] Maria Italia[4] traces its history from the Elizabethan concept of confidentiality to the client's right to privilege in today's complex legal system. She makes the point that, in Elizabethan times, 'confidentiality existed to protect the honour and integrity of the gentleman, the holder of the confidential information. Lawyers were not distinguished from other gentlemen - all were protected by the notion of honour'.

Thus, privilege was historically not a right attaching to the profession of a lawyer but, as stated by the Court in *General Mediterranean Holdings,* a practical guarantee of fundamental human rights. It is fairly easy to see why the principle came to be associated with lawyers – over time the only persons who were permitted to represent clients were lawyers, and so case law linked privilege with lawyers. The Courts have accepted[5] that non-lawyers may have a far greater expertise in certain fields of taxation. Further, the consultation document entitled *The future of legal services: Putting Consumers First*,[6] also accepts that consumers want and are entitled to a choice of who advises them. The consultation document points out for example that some 468 Citizens Advice Bureaux offer legal advice to individuals. It should also be noted that in the tax field a very wide industry has developed,

with advice given by many people who are eminently qualified by their extensive experience in a particular field to advise on tax issues, but not otherwise qualified. Thus, the development of public policy and the change in consumers' expectations leads to the logical conclusion that if it is accepted that some non-lawyers are better qualified than the average solicitor to give legal advice in a particular area or to represent a client before a tribunal, individuals should not be prevented from accessing such services for fear of any confidences not being protected. Legal and professional privilege is an essential tool in the provision of advice. It is the nature of the advice that determines whether privilege applies, and not the adviser's qualification.

European law

European Community law governs VAT and Customs duty but also impacts on other taxes such as income and corporation taxes. It is logical to ensure that whether or not it is required, all taxes are broadly speaking subject to the same rules and, accordingly, insofar as European Community law might grant rights to VAT taxpayers, the same rights should apply to all taxes.

A number of issues arise:

- the extent to which European law recognises legal and professional privilege;
- proportionality; and
- whether distinguishing between types of advisers may breach European Competition law.

General principles

The European Court of Justice has accepted that the member states all have a principle that protects confidences between clients and lawyers in some form or other. The Court also accepts that the same principles apply in European Community law *(see AM & S Europe Limited v Commission)*.[7] The Court of First Instance in the joined cases of *Akzo Nobel Chemicals Limited and Akcros Chemical Limited*[8] initially accepted this, and granted interim measures preventing the Commission from using papers in respect of which privilege was claimed. However, the President of the European Court of Justice subsequently overruled the Order and allowed access. Thus, as in the UK, the right to confidentiality is not absolute and can be overridden in certain circumstances. It must be recalled that article 6(2) of the Consolidated Treaty establishing the European Union provides that:

'The Union shall respect fundamental rights, as guaranteed by the European Convention for the Protection of Human Rights and Fundamental Freedoms signed in Rome on 4 November 1950 and as they result from the constitutional traditions common to the Member States, as general principles of Community law.'

Thus, the right to confidentiality guaranteed by article 8 of the European Convention of Human Rights forms a general principle of EU Community law. As such, it also forms part of UK law for the purposes of interpreting European law.

Proportionality

Tax is a creature of statute, and as such the only powers that exist for requiring taxpayers to provide information is that law that gives HMRC such powers. In relation to VAT, the law must comply with European VAT law. Member states' power to require disclosure in relation to VAT is set out in article 22 of the EC Sixth VAT Directive. Apart from certain specific requirements in relation to matters such as invoicing, sub-paragraph 22(8) provides that 'Member States may impose other obligations which they deem necessary for the correct collection of the tax and for the prevention of evasion ...'.

HMRC appear to take a very broad view of what can be required under article 22(8), but the European Court of Justice decision in Federation of Technological Industries v HMRC[9] suggests that the powers given to member states under that article may not be as broad as might appear. In particular, the principle of proportionality must apply. Indeed, the fact that the article specifies the purposes for which other obligations may be imposed implies a limit to member states' powers.

It is of interest to note that while article 22(8) refers specifically to and gives member states powers to impose obligations to prevent evasion, no such powers are provided in relation to avoidance and abuse. Given that in other articles (e.g. article 27) there is reference to 'evasion andavoidance' or to 'evasion, avoidance and abuse', this further suggests that member states' powers to override basic principles are limited in nature.

Competition law

In *Servizi Ausiliari Dottori Commercialisti Srl v Giuseppe Calafiori – Pubblico Ministero intervening*,[10] the European Court of Justice concluded that national law precluding anyone but tax advice centres from providing certain tax advice was contrary to European law pertaining to competition between undertakings.

If there is a fundamental need for confidentiality in relation to tax matters as held by case law, it must be arguable that allowing confidentiality for the clients of one group of advisers without extending the same rights to others' clients may conceivably breach competition rules by denying the one group an essential tool of trade. The refusal of confidentiality would act as an effective barrier to some clients approaching the best adviser.

While HMRC appear to recognise that a taxpayer who asks an accountant to represent him at a VAT and Duties Tribunal is entitled to privilege, there is no 'advice privilege' for accountants in the same way as there is for lawyers. This may block access to the best legal advice (and impact on competition) as much as would a total failure to recognise privilege at all.

The European Convention on Human Rights

Article 8 of the Human Rights Convention makes provision for the protection of communications between persons.

The application of article 8 in relation to legal and professional privilege was considered in *Campbell v United Kingdom*. The issue there was in essence whether the prison authorities' interference in a prisoner's rights to confidentiality in his correspondence with the European Commission on Human Rights could be justified on the grounds that it was necessary for the protection of the rights and freedoms of others.

The Court concluded that the prisoner's rights had been violated in respect of any opening of correspondence between himself and the European Commission on Human Rights. In relation to correspondence with the prisoner's solicitor, the Court concluded that it was legitimate to open but not read the correspondence where the authorities have reasonable cause to believe that there is an illicit enclosure that ordinary methods might not disclose. The judgment therefore makes it clear that there is a very heavy burden of proof before it can be accepted that it is legitimate for the State to interfere with a prisoner's correspondence. It will be clear that what the prison authorities were seeking to protect with their interference in the prisoner's right to confidentiality was the possibility that escape plans or some other crime might be communicated in the correspondence. Indeed, the potential crime could have included acts that threatened the personal security of others.

Since tax avoidance is not criminal and is therefore not as serious as the risks the European Court of Human Rights considered in *Campbell*, it is difficult to see any justification for interfering with the confidences between taxpayer and adviser.

The OECD

The OECD issued a paper in its tax guidance series in October 2003, entitled *Taxpayers' Rights and Obligations – Practice Note.* On the issue of the taxpayer's right to privacy, the document notes:

'11. All taxpayers have the right to expect that the tax authorities will not intrude unnecessarily upon their privacy. In practice, this is interpreted as avoiding unreasonable ... requests for information which is not relevant for determining the correct amount of tax due... Similarly, strict rules apply to obtaining information from third parties on the affairs of a taxpayer.'

It is sometimes averred that tax authorities require sight of such correspondence to determine motive, e.g. to show abuse of law. For reasons outlined in the section dealing with EU law, it is difficult to see how such a right can be argued. The law in many countries has for a considerable time accepted that matters sometimes have to be proved by inference – even in criminal law. The weight of proof required may change, eg, it may be necessary to prove by inference that it is beyond doubt that there was criminal intent, but that does not override the principal that a party may not require disclosures of another just because it might be easier to establish a fact by doing so.

Further, the burden of proof will usually start with one party and switch to another and perhaps back and forth, but that also does not affect that basis right to confidentiality. In relation to taxes in many countries, the taxpayer has to prove the tax authorities wrong (although EU law sometimes places a burden of proof on the tax authorities – see for example the EU cases dealing with claims to recover taxes unduly levied). That means that in many cases taxpayers are already significantly disadvantaged before tribunals and courts. To add to that burden is unnecessary, and breaches the principle stated above.

Conclusion

It is often argued in different areas of law that the public interest should override individual rights. That is inevitable – rights such as those set out in the European Convention on Human Rights – because the whole reason for giving individuals rights is to protect them from abuse by the State. The need for confidentiality in tax matters is not limited to a need to prevent the tax authorities disclosing data to others – as the OECD statement above indicates. HMRC should not therefore try to erode this by legislation or litigation.

FOOTNOTES

1. General Mediterranean Holdings SA v Patel and another [1999] 3 All ER 673 (QBD)
2. R (Morgan Grenfell & Co Ltd) v Special Commissioner of Income Tax [2003] 1 AC 563
3. The history of legal professional privilege and its role In tax advice by tax professionals
4. School of Accounting and Finance, Footscray Park Campus, Victoria University of Technology, PO Box 14428 MCMC, Victoria 8001, Australia
5. See for example, Andre Agassi v S Robinson (H M Inspector of Taxes) (Bar Council and Law Society intervening) [2005] EWCA Civ 1507 at paragraph 80.
6. Cm 6679 October 2005
7. Case C-155/79
8. Cases T-125/03 and T-253/03
9. Case C-384/04
10. Case C-451/03

Author's Profile

*The CIOT commissioned this article from **Mr Maric Glaser**, one of its Technical Officers, to initiate a discussion of an important right for taxpayers. However the views expressed herein are Maric Glaser's own personal views.*

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Editor's Note: Look out for the Malaysian Perspective on Taxpayers Confidentiality in the next issue of Tax Nasional (Q3/2007)!

Managing TAX Disputes

- An Australian Perspective-

Mr David Russell QC

(Part II)

Part IVC proceedings – section 14ZZO TAA 1953, *Rio Tinto* and the Model Litigant

Once an assessment issues and an appeal is commenced within Part IVC, the matter proceeds in the Federal Court and in accordance with its rules unless the taxpayer has decided instead to seek a review of the objection decision by the Administrative Appeals Tribunal under Division 4 of Part IVC.

The traditional perception of the role played by the Revenue in Court proceedings was discussed by the Federal Court in *Lighthouse Philatelics Pty Ltd v. Federal Commissioner of Taxation* [32] in the following terms:[33]

> If a dispute arises between the Commissioner and a taxpayer and it is forwarded to a Court or referred to a Board the Commissioner, although as a result of the adversary system adopted in Australia an opponent of the taxpayer, appears before the relevant tribunal not to exact tax improperly payable but to assist the tribunal in coming to an answer of (sic) the statutory question as to whether the assessment is excessive having regard to the real facts and the law. In fulfilling this role, the Commissioner can never be disadvantaged if the real argument as to why the assessment is excessive is put to the relevant Tribunal.

Tax litigation has changed a great deal over the years. The implication of the observation in *Lighthouse Philatelics* that "His (i.e. the Commissioner's) task is to ensure that the correct amount of tax is paid, "not a penny more, not a penny less" would seem to be that the Commissioner should adopt a position analogous to a Crown prosecutor, rather than an aggressive commercial litigant. If that ever was the position, it must be seriously questioned whether or not it still is.

In a recent unpublished article on the contingencies of taxation litigation, Robert Venables QC observed:

> That is where the English Bar is at a premium - when you are saying, "This works technically, but are the courts going to wear this? Are they going to put up with it? Are judicial doctrines going to apply? How are they going to construe this legislation?" One good thing about the United Kingdom is that we do not have a GAAR, a general anti-avoidance provision or a general anti-avoidance doctrine, although - as David Goldberg says - the "smell test" is very important. One of the first things I learnt at the Bar is that an ounce of prejudice is worth a ton of law. There is no doubt that courts still start off saying to themselves, "Who ought to win here?" They then try to find out if they can possibly legitimately get to that conclusion, and intelligent judges will not reach that conclusion if they are unable to. Less intelligent judges do not have these intellectual problems and will reach the results through totally inadequate reasoning.
>
> When we are sitting - as it were - at the drawing-board stage, and we are drafting our fantastic strategies, we sometimes fail to take into account what it is like when the Revenue does challenge: you hold out, you go to court and you have to stand your ground. Very few cases, nowadays, go to court- especially in direct tax. But, of course, you are only going to get a "good deal" if you know that at the end of the day, if necessary, you can. You have to have that strength of position. Firstly, everything has to be properly done. The number of strategies I have seen which have been absolutely perfect in conception and yet, somewhere along the line, somebody has cut a corner and not done it properly and so it does not work in practice! That happens time and time again. When I was a Junior, the Revenue would happily agree one page of facts and not look at the documents; now they ask for all the documentation, use their search powers and look through very carefully, and if it is has not worked - if, for example, you have overlooked some principle of trust law which means that your appointment out of a trust is void - they will seize the point and your tax planning will fail. So, everything has to be done properly, but not only that - and taking up a point that David Goldberg makes - under the UK system, if the Revenue think you are liable to tax, they make an assessment. You appeal against it, and then the burden of proof is on you to show that the assessment is wrong. It is not merely enough that the facts are in your favour. You have to prove those facts and you have to prove them by lawful evidence. I do not know if you

remember the famous fictional case of Bardell v. Pickwick where Mr. Pickwick is sued for breach of promise by Mrs. Bardell. He has never promised to marry her in the first place. It is all a big misunderstanding. But - as his counsel says - how is that to be proved? In those days, English law took the view that the parties to an action were not allowed to give evidence. The temptation of perjury, which would offend God's law, was so great that they could not be allowed to give evidence. So, although he had never promised to marry Mrs. Bardell, he could not give straight evidence to that effect. Nowadays, you have to think not only "what was the situation" but "how can we prove it?". David mentions the case of the key witness who has a nervous breakdown and cannot be brought to the United Kingdom. What we would do now is to get a witness statement which would be a lot better because it means he is not going to be subject to cross-examination. If he is seriously ill, that is a very good reason why he cannot come to the United Kingdom, and therefore no adverse criticism can be made of the fact that we have not brought him in person. But it is not enough that everything has been properly done, you need to prove everything has been done properly. This means that you need a good paper trail, and also - if you are using people, i.e. directors of companies, trustees etc., they must be people who know what they are doing and are able to give good, clear evidence which will stand up under cross-examination, people who will not flinch and will not say the wrong thing.

The wrong thing can be all sorts of things. I had a case, about ten years ago, which was a straight bit of what I thought was vanilla tax planning. A big corporate group had a perfectly valid unrealised loss, but it took a slightly artificial means of realising it so it could set it off against a gain. I regard that as relatively vanilla planning, because - after all - the unrealised loss was there and was inherent. But what was done was undoubtedly done to enable the loss to be realised for capital gains tax purposes and set off against the gain. It was obviously tax planning, and I said to the finance director of the group, "If you are asked in evidence, you admit that. That is why we did it, but we say it works." Under examination he pretended that there were all sorts of commercial reasons which did not stand up. He was slaughtered in cross-examination: the real issue in the case was obfuscated, and it was lost before the Special Commissioners. If he had simply told the truth, none of the prejudicial appearance would have been generated in the first place.

One problem, rarely articulated, is the tendency of some judges at least to see the contest between a taxpayer and the revenue in moral terms which favour the Revenue. Thus a taxpayer is likely dishonest[34] and fairly deprived of part of his costs in a tax avoidance context even when wholly successful[35] but the Revenue is rarely seen as anything other than an emanation of conscientious public administration.[36]

Prior to institution of the proceedings it may be wise to consider how the litigation will be conducted and the personnel to conduct it. Those who have advised the taxpayer up to this point may well not be the best professionals to conduct the litigation, either because of potential conflicts or because the skills appropriate to the giving of competent tax advice are not necessarily the skills necessary to pursue a hard-fought tax dispute in the Courts. That will be particularly so where their advice may be relevant to the issue of penalties due to the existence of reasonable care, as the opinions of advisers actually given in relation to the fact of the taxpayer may well show a reasonable arguable position:

It is true that opinions of counsel are not referred to in the definition of 'authority'. On the other hand it may be said that the definition is inclusory so that recourse to the opinions of counsel is not necessarily ruled out by the definition. It is unnecessary in the present case to decide this question, although I am inclined to think that the opinion of eminent counsel practising in the field such as Mr Gzell QC and Mr Edmonds QC, if directed at the actual facts of a case, might well fall within the definition.[37]

The obligations of taxpayers when making pre-assessment disclosures to the ATO were considered earlier in this paper. Just as taxpayers have clear obligations in relation to disclosure, so does the ATO in relation to assessments and determination of objections as, indeed it does generally:

It is intended that (the Commissioner) shall take a high position in this matter and shall not claim for the Crown more than he sees the Crown is entitled to, and he shall not allow any taxpayer to escape payment of any amount which the law intends him to be liable to pay.[38]

By the time any appeal has been lodged, one may expect that the Commissioner has considered the legal and factual contentions of the taxpayer, and decided which are accepted and which are not. Hence, upon lodgment of the appeal, the Federal Court Rules require that the Commissioner within 28 days file, inter alia:

a statement outlining succinctly the Commissioner's contentions and the facts and issues in the appeal as the Commissioner perceives them[39]

This document, and the corresponding Statement filed by the taxpayer, are intended to take the place of pleadings.[40] How the Federal Court expects matters will proceed after that was stated thus by Beaumont J, speaking extrajudicially: [41]

The Statement is divided into three distinct parts as follows:

- First, a comprehensive statement of the facts, including background or

historical facts, which the particular party, in accordance with its own professional advice, contends ought to be found by the Court.

... the Crown is expected to act, and does act, as a 'model' litigant, so that it may be anticipated that the Commissioner's response to the taxpayer's statement of facts will not seek to put in issue facts which the Commissioner ought not to place seriously in question.

The ATO has never really accepted the underlying logic of these procedures.The arguments go back a long way. In *Steinberg v. Federal Commissioner of Taxation* [42] Barwick CJ observed: [43]

It should also be said that, if asked by the taxpayer, the Commissioner should inform him of the basis of the assessment in cases in which the adjustment sheet served with the notice of assessment does not do so. Just as in other litigation, there must be issues in an appeal against assessment under the Act to which both parties are confined. As matters presently stand, the relevant file of the Commissioner and the objection of the taxpayer should be the source of those issues. It should not be the case that by reason of the appellant taxpayer must negative all possible bases upon which, having regard to the material adduced before the appellate tribunal, the statement of liability to tax in the notice of assessment might be based. So to use that section is, as I have said before, to make that section a scourge for the citizen rather than a reasonable protection for the revenue. It is high time that rules of court provided for the determination of the issues in income tax appeals and expressly confining both Commissioner and taxpayer to them in an appeal which is to be resolved by an adversary process and in which the contest should not be unequal.

Subsequently, the issues were reventilated in *Bailey v. Federal Commissioner of Taxation* [44] and the following observations of Aickin J are pertinent: [45]

Whatever the position may be at the time of the issuing of a notice of assessment and whether or not it is correct to say, as Williams J. said in H. R. Lancey Shipping Co. Pty.Ltd. v. Federal Commissioner of Taxation (1951) 25 ALJR 145, that the Commissioner is under no obligation to furnish an "alteration sheet" indicating the adjustments which he has made to the taxable income as returned whether by way of addition of income or denial or allowable deductions, when an appeal comes before this Court or a Supreme Court from the Commissioner's disallowance of an objection, the position is quite different. Under and such appeals go to the Supreme Courts of the States, and until regulations are made, are conducted under the High Court Rules which provide by O. 65, r. 2 that, subject to that order, the provisions of other orders also apply to taxation "appeals", which are of course in the original jurisdiction. It has not been the practice in this Court to require pleadings in taxation appeals, though it may well be that the rules are wide enough to enable this to be done. (See the definitions of "plaintiff", "defendant" and "proceeding" in O. 1, r. 5 and the terms of O. 20.) In the absence of pleadings, the provisions of O. 20, r. 6 may not be directly applicable but in my opinion this Court and the Supreme Courts of the States hearing taxation appeals have inherent jurisdiction to require parties to give particulars if it appears just to do so. The fact that a proceeding may go forward without pleadings does not deprive the Court of such control as is necessary to ensure that the issues are defined and that each party is provided with the necessary information as to the case which he has to meet. The basis of the decision in Philliponi v. Leithead (1959) SR (NSW) 352 applies equally in the High Court.

The purpose of particulars is to assist in the defining of issues and there is in my opinion no reason why in appropriate cases the Commissioner should not give particulars where they are necessary in order that both the appellant and the court may understand the basis upon which the assessment has been made. See Spedding v. Fitzpatrick (1888) 38 Ch 410, R. v. Associated Northern Collieries (1910) 11 CLR738, at pp 740-741 and Astrovlanis Compania Naviera S. A. v. Linard (1972) 2 QB 611, at pp 619-620. No doubt there are many cases in which the return, the notice of assessment, the alteration sheet and the notice of objection will reveal the issues with sufficient certainty so that no particulars are necessary. This however is seldom the case where an assessment has been issued upon the basis of s.260. To tell a taxpayer and the Court that an assessment is based upon s.260 reveals nothing beyond the fact that the Commissioner contends that there is some contract, agreement or arrangement which falls within the ambit of that section and that either the whole or some part of it, or some step taken pursuant to it, or in the course of carrying it out, is void as against the Commissioner and that a taxable situation stands revealed by such avoidance. If no more is said the taxpayer and the Court are left entirely in the dark as to critical matters and the issues remain undefined except as to the ultimate conclusion contended for by each party.

There is nothing in the policy of the Act nor in general considerations of policy to require that the Commissioner should not inform the appellant prior to the commencement of the hearing of those details so that the case may proceed in an orderly and comprehensible manner. It is not in the interests of the proper administration of justice that, when the matter comes before the court, the appellant should have to speculate about, and adduce evidence to negate, every possible kind of agreement or arrangement and avoidance which the imagination of his advisers can conjure up. Such a process is not merely time-wasting but is likely to obscure the real issues. It is no doubt possible that in the course of the evidence facts may emergewhich were not previously known to the Commissioner and which suggest

that there was some contract, agreement or arrangement other than that which he had previously supposed existed and which would support the actual assessment, but that is a situation which can readily be cured by amendment and it cannot be doubted that the Commissioner would in those circumstances be permitted to amend his particulars even though he would again have to specify the details of the arrangement which he was then alleging.

An examination of the authorities does not in my opinion suggest that the Supreme Court or this Court has no power to direct the Commissioner to give appropriate particulars of the basis of the assessment. The fact that the Commissioner does not himself have to prove any particular fact and that the onus of proof rests upon the taxpayer by virtue of s.190 cannot determine this question. There are many situations in which the party who gives a general denial to the pleading of the party on whom the onus rests may none the less be required to give particulars if the general denial really involves some positive allegation. This general principle is well established - see, e.g., Pinson v. Lloyds and National Provincial Foreign Ltd. [1941] 2 KB 72 and George v. Federal Commissioner of Taxation, per Kitto J. (1952) 86 CLR 183, at p 190. This is exactly the case where s.60 is relied upon to support an assessment.

In recent times, the ATO has taken to including a "Preamble" in Statements of Facts Issues and Contentions filed on its behalf along the following lines:

The respondent relies on section 14ZZO(a) of the Taxation Administration Act 1953 ('TAA53'). The respondent also relies on section 14ZZO(b) of the TAA53 and, save for any facts expressly agreed or admitted in writing, puts the applicant to proof of all facts on which it seeks to rely. The respondent's perception of the facts is primarily derived from documents and information supplied by the applicant and its advisers. For the purpose of identifying the issues in dispute between the parties in these proceedings, the respondent states that, on the information currently available to him, it appears that the facts, issues and contentions are as follows.[46]

It is difficult to reconcile this attitude with the notion that the only matters which will be disputed are those seriously in contention. The nature of the Crown's obligations as a model litigant are set out in Legal Services Directions issued by the Attorney-General pursuant to section 55ZF of the Judiciary Act 1903, which are appended to this Paper. Subsection 55ZG(1) of that Act makes those directions binding on the ATO in litigation. However the section goes on to provide:

(2) Compliance with a Legal Services Direction is not enforceable except by, or upon the application of, the Attorney-General.

(3) The issue of non-compliance with a Legal Services Direction may not be raised in any proceeding (whether in a court, tribunal or other body) except by, or on behalf of, the Commonwealth.

The Direction itself notes that, quite independently of any statutory obligation, there is authority in case law for the view that the Crown ought to so act[47] and at the very least litigants who contend that the ATO is not acting in compliance with its obligations need to be aware that unless the attention of the Court is drawn to that fact, the Court may well proceed on the basis that the ATO is acting in accordance with its obligations.

In addition to the special position of the ATO as a (supposed) model litigant, the Courts are increasingly becoming impatient with forensic games as an alternative to resolution of the real issues. For example, the (Queensland) Uniform Civil Procedure Rules provide that their purpose "is to facilitate the just and expeditious resolution of the real issues in civil proceedings at a minimum of expense"[48] and provide the following in relation to denials and non-admissions:[49]

Denials and non-admissions

(1) An allegation of fact made by a party in a pleading is taken to be admitted by an opposite party required to plead to the pleading unless-

(a) the allegation is denied or stated to be not admitted by the opposite party in a pleading; or

(b) rule 168 applies.

(2) However, there is no admission under subrule (1) because of a failure to plead by a party who is, or was at the time of the failure to plead, a person under a legal incapacity.

(3) A party may plead a non-admission only if--

(a) the party has made inquiries to find out whether the allegation is true or untrue; and

(b) the inquiries for an allegation are reasonable having regard to the time limited for filing and serving the defence or other pleading in which the denial or non-admission of the allegation is contained; and

(c) the party remains uncertain as to the truth or falsity of the allegation.

(4) A party's denial or non-admission of an allegation of fact must be accompanied by a direct explanation for the party's belief that the allegation is untrue or can not be admitted.

(5) If a party's denial or non-admission of an allegation does not comply with subrule (4), the party is taken to have admitted the allegation.

(6) A party making a non-admission remains obliged to make any further inquiries that may become reasonable and, if the results of the inquiries make possible the admission or denial of an allegation, to amend the pleading appropriately.

(7) A denial contained in the same paragraph as other denials is sufficient if it is a specific denial of the allegation in response to which it is pleaded.

On one view of the matter, such an approach might be expected to commend itself to a model litigant, particularly one who has the protections arising from the fact that

the other party cannot misstate the facts in dealings with him without commiting a criminal offence [50] or change his position without the leave of the AAT or Court (as the case may be).[51] The writer's experience has been somewhat different.[52]

In *Rio Tinto* itself, Sundberg J appears to have regarded the ATO approach to section 14ZZO as misconceived:

Relevance Of s 14ZZO(b)

30 At all material times the income tax legislation has included a provision imposing on the taxpayer the burden of proving that the assessment is excessive. At the time of Bailey it was s 190(b) of ITAA36. The more expansive form of s 14ZZO(b) is not relevantly different. *The respondent, in my view, overstates the significance in an Order 52B rule 5(a)(v) context of the fact that the burden is on the taxpayer. Rule 5(a)(v) and s 14ZZO(b) deal with different issues and different stages of a tax appeal.* The section is concerned with the ultimate disposition of the appeal. Unless the Court otherwise orders, the appellant is limited to the grounds stated in its objection, and has the burden of proving that the assessment is excessive or incorrect. The rule, on the other hand, is concerned with the management of the appeal in its early stages. There are no pleadings in taxation appeals, and the rule was introduced to formalise the practice that had developed in the Court of providing an alternative to pleadings so as to ensure that each party is aware of the other's case. See, for example, Binetter at 647. That the section and the rule (or the earlier practice) are dealing with different issues is reflected in Gibbs J's observations in Bailey at 219 that the fact that the taxpayer bears the onus of proving that the assessment is excessive "makes it all the more necessary that he should be given particulars of the basis of the assessment".

Subjecting Respondent to a Plaintiff's Obligation

31 Related to the onus submission is the respondent's contention that the applicant seeks to subject the respondent to the obligations of a plaintiff having a cause of action which he is required to plead in accordance with the usual rules applicable to pleadings. This is said "in effect, to invert the onus of proof". The respondent placed much emphasis on Hill J's remark in Evans at 4544 that a statement of issues is a "less formal procedure than would be involved in the filing of pleadings". His Honour was there describing the order made by Lockhart J, before the introduction of Order 52B, that the parties file an agreed statement of issues, and failing agreement each file a statement of the issues as seen by them. The pleading regime in the Rules is formal, detailed, structured and well-developed by case law. Hill J's use of the words "less formal procedure" is intended to reflect the absence of such a regime in taxation appeals, and the practice of giving curial directions designed to fill the gap so as to ensure that each party knows the case that has to be met. As Aickin J said in *Bailey* at 227 (quoted by Hill J in *Evans* at 4544):

"The fact that a proceeding may go forward without pleadings does not deprive the Court of such control as is necessary to ensure that the issues are defined and that each party is provided with the necessary information as to the case which he has to meet."

In any event, since Order 52B was made there is a formal procedure in place. Doubtless for this reason, Hill J in *Bartlett* at 265 described the Statement of Facts, Issues and Contentions as "intended to take the place of pleadings". Whether one looks to the pre-Order 52B practice or the current regime, the real point is not whether what the Order mandates is less formal than pleadings or takes the place of pleadings, but that the intention behind the practice and the Rule is that "both parties to the litigation know what the case is which they have to meet": per Aickin J in *Bailey* at 227 and per Hill J in *Bartlett* at 265.

Commisioner's Knowledge of the Facts

32 In my view, the respondent also places undue emphasis on the significance of the respondent's "second-hand, hearsay knowledge of the transactions purported to have been implemented" by the applicant. The facts in this case are not all within the knowledge of the taxpayer. The relevant facts include the view of the facts on which the respondent has based his assessment and the manner in which he has arrived at his assessment. See per Barwick CJ and Mason J in Bailey at 217 and 221 respectively and per Gummow J in Jackson at 469. Further, it is apparent from the information contained in the document that the respondent is in possession of the transaction documents, and is aware of the background facts and concerns that led the applicant to bring them into existence. All that can in truth be said is that the applicant may have a more cpmplete understanding of the events that happened and their timing. Other matters that are within the knowledge of the respondent relate to the respondent's s 46A "satisfaction" that payment of the dividend was by way of dividend stripping, the matters that led the respondent to exercise the discretion conferred by s 177F in the way he did, and the imposition of penalties and the decision not to remit or not wholly to remit them. *(italics supplied)*.

Until the Federal Court deals expressly with the acceptability of this approach[53] taxpayers would be wise to ensure that tax appeals proceed in accordance with directions which deal with the following issues (where appropriate):

- obtaining adequate particulars of the ATO's Statement of Facts, Issues and Contentions.
- Delivery of Notices to Admit Facts and Documents and responses thereto so as to encourage the ATO to comply with its obligation as a model litigant or suffer a consequence sounding in costs;
- Finalisation of an Appeal Record;
- early identification of any issues concerned with admissibility of affidavit material or documents;
- identification of witnesses required for cross-examination; and
- limitation of the material before the Court to the affidavits, cross-examination arising therefrom and the documents included in the Appeal record

Whilst the Federal Court Rules provide for mediation and arbitration in respect of matters before the Court[54] these opportunities seem not to have commended themselves to litigants in the taxation context.

In recent times the Courts have emphasized the responsibility of parties to seek to settle disputes by penalizing parties who unreasonably persist in litigation with adverse costs orders. There is no reason in principle why this approach should not apply in the context of tax litigation.[55]

Two final points should be noted at this stage. The first, if Part IVA is involved, is the somewhat peculiar structure of the review provisions if a compensating adjustment is sought under subsection 177F(3) of the 1936 Act. Frequently this is done in the objection against the original assessment, particularly if timing differences for the same taxpayer are involved or there are a number of assessments against members of the same corporate group. The ATO may not respond to this request as part of the objection decision and if it does not there is nothing to which to object.[56] A further objection is required if the request is denied.[57]

The second is that the ATO remains uncomfortable with the decision in Lighthouse Philatelics, seemingly preferring the views of Dr Grbich in the AAT decision which it overruled,[58] and has argued, with some encouragement,[59] that the transfer of the objection, review and appeal provisions has created a materially different statutory regime under which this decision no longer applies. Until this contention is addressed at appellate level it would be unwise to assume that the rights of amendment contemplated in sections 14ZZK and

14ZZO of the Tax Administration Act 1953 may always be availed of. In any event the remedy is discretionary.

Post-assessment Corporations Act responsibilities

Once a notice of an assessment is served, the ATO by relying on section 59 of the Taxation Administration Act 1953 or, in the income tax context, section 177 of the Income Tax Assessment Act 1936 is in a position to enforce payment of the tax debt. Whilst the ATO will, if the revenue is not at risk, normally not insist on payment before determination of the objection and will generally allow half the tax to remain in abeyance after that pending the hearing, General Interest Charge will be payable and, if there are multiple assessments, the amount involved may be substantial.

From time to time statements are made by the ATO that it will seek to collect only one amount of tax even where there are multiple assessments. Whilst, as a matter of justice, there is much to be said for this exercise of discretionary mercy, it needs to be kept in mind that ultimately it is possible that more than one liability will be maintainable and the ATO may well be in a position[60] where its obligation is to collect both.

Where the taxpayer is a company, it may be engaged in trading transactions. If an assessment, or assessments are correct it may well be impossible for the amount claimed, together with the other debts of the company concerned, to be paid in full.In those circumstances, the directors of a company may need to consider the steps which they ought now to take in relation to its affairs by reason of the insolvency provisions of the Company law.

Section 588G of the Corporations Act 2001 provides:

Director's duty to prevent insolvent trading by company

(1) This section applies if:

(a) a person is a director of a company at the time when the company incurs a debt; and

(b) the company is insolvent at that time, or becomes insolvent by incurring that debt, or by incurring at that time debts including that debt; and

(c) at that time, there are reasonable grounds for suspecting that the company is insolvent, or would so become insolvent, as the case may be; and

(d) that time is at or after the commencement of this Act.

(2)By failing to prevent the company from incurring the debt, the person contravenes this section if:

(a) the person is aware at that time that there are such grounds for so suspecting; or

(b) a reasonable person in a like position in a company in the

Note: This subsection is a civil penalty provision (see subsection 1317E(1).

(3) A person commits an offence if:

(a) a company incurs a debt at a particular time; and (aa) at that time, a person is a director of the company; and

(b) the company is insolvent at that time, or becomes insolvent by incurring that debt, or by incurring at that time debts including that debt; and

(c) the person suspected at the time when the company incurred the debt that the company was insolvent or would become insolvent as a result of incurring that debt or other debts (as in paragraph (1)(b); and

(d) the person's failure to prevent the company incurring the debt was dishonest.

(3A) For the purposes of an offence based on subsection (3), absolute liability applies to paragraph (3)(a).

Note: For absolute liability, see section 6.2 of the Criminal Code.

Section 95A of the Corporations Act provides:

Solvency and insolvency

(1) A person is solvent if, and only if, the person is able to pay all the person's debts, as and when they become due and payable.

(2) A person who is not solvent is insolvent.

Particularly if substantial penalties or multiple assessments (or both) are involved a situation may arise where a company is unable to fund the payment of the tax and its other debts from its assets as they fall due.

Prior to the issue of the assessment, the company will presumably have been advised that there was no outstanding tax liability in relation to the subject matters of the assessment. But the issue of assessment, coupled with the conclusive evidence provisions in section 59 of the *Taxation Administration Act,* produces the result that if the debt(s) asserted by the assessments are, the purposes of section 95A, debts of the company, the result may be an insolvency.

Section 588G of the *Corporations Act,* unlike preceding provisions which made it an offence to incur liabilities which might not be discharged, makes the incurrence of the debt an offence, even where the debt is subsequently discharged by a third party. This means, in my opinion, that it is not sufficient merely to establish an arrangement whereby a taxpayer is indemnified in respect of liability to pay debts as and when incurred (with the result that each debt now incurred can be confidently predicted to be repaid): rather, no future "debts" can be incurred.

There is a distinction between incurring a debt and paying one: indeed, item (1) of the table forming part of subsection 588G(1A) (not set out in the above excerpt) makes the distinction clear.

It follows that a company is free to continue to discharge liabilities which are already incurred, including, in that context, existing contractual obligations in relation to future payments. What it is not entitled to do is to incur further liabilities. This may present no difficulties if there other members of the company group are free to enter into agreements whereby services will be provided for the company without it incurring a liability to pay for them unless it is solvent. This may have the effect of deferring tax deductibility for the payments to a later tax period, but should otherwise not be productive of commercial inconvenience. On the other hand this may not be feasible.

All of this casts a very heavy burden on the directors of a corporate taxpayer, and in particular upon directors of a corporate group where multiple assessments have issued to more than one member of the group in respect of the same income.

Conclusion

For so long as tax legislation continues to be as complex as it is, it is inevitable that there will be disputes about what it means in particular cases.

However the expense and potential consequences of such disputes increasingly means that they should be actively managed bearing in mind both the starting point and collateral issues such as solvency in a corporate context.

In this regard tax disputes are not immune from developments in the wider area of litigation generally, where court initiated case management techniques have moved to the fore in place of the former approach in which much was left to the parties so that the pace of litigation largely depended on them.

The remedies available to parties are not unchanging and a whole of dispute approach is called for at all stages.

Appendix

Directions On The Commonwealth's Obligation To Act As a Model Litigant

1. Consistently with the Attorney-General's responsibility for the maintenance of proper standards in litigation, the Commonwealth and its agencies must behave as a model litigant in the conduct of litigation.

Nature of the obligation

2. The obligation requires that the Commonwealth and its agencies act honestly and fairly in handling claims and litigation brought by or against the Commonwealth or an agency by:

(a) dealing with claims promptly and not causing unnecessary delay in the handling of claims and litigation,

(b) paying legitimate claims without litigation, including making partial settlements of claims or interim payments, where it is clear that liability is at least as much as the amount to be paid,

(c) acting consistently in the handling of claims and litigation,

(d) endeavouring to avoid litigation, wherever possible,

(e) where it is not possible to avoid litigation, keeping the costs of litigation to a minimum, including by:

(i) not requiring the other party to prove a matter which the Commonwealth or the agency knows to be true, and

(ii) not contesting liability if the Commonwealth or the agency knows that the dispute is really about quantum,

(f) not taking advantage of a claimant who lacks the resources to litigate a legitimate claim,

(g) not relying on technical defences unless the Commonwealth's or the agency's interests would be prejudiced by the failure to comply with a particular requirement,

(h) not undertaking and pursuing appeals unless the Commonwealth or the agency believes that it has reasonable prospects for success or the appeal is otherwise justified in the public interest, and

(i) apologising where the Commonwealth or the agency is aware that it or its lawyers have acted wrongfully or improperly.

NOTES:

1. The obligation applies to litigation (including before courts, tribunals, inquiries, and in arbitration and other alternative dispute resolution processes) involving Commonwealth Departments and agencies, as well as Ministers and officers where the Commonwealth provides a full indemnity in respect of an action for damages brought against them personally. Ensuring compliance with the obligation is primarily the responsibility of the agency which has responsibility for the litigation. In addition, lawyers engaged in such litigation, whether Australian Government Solicitor, in-house or private, will need to act in accordance with the obligation and to assist their client agency to do so.

2. In essence, being a model litigant requires that the Commonwealth and its agencies, as parties to litigation, act with complete propriety, fairly and in accordance with the highest professional standards. The expectation that the Commonwealth and its agencies will act as a model litigant has been recognised by the Courts. See, for example, Melbourne Steamship Limited v Moorhead (1912) 15 CLR 133 at 342; Kenny v State of South Australia (1987) 46 SASR 268 at 273; Yong Jun Qin v The Minister for Immigration and Ethnic Affairs (1997) 75 FCR 155.

3. The obligation to act as a model litigant may require more than merely acting honestly and in accordance with the law and court rules. It also goes beyond the requirement for lawyers to act in accordance with their ethical obligations.

4. The obligation does not prevent the Commonwealth and its agencies from acting firmly and properly to protect their interests. It does not therefore preclude all legitimate steps being taken to pursue claims by the Commonwealth and its agencies and testing or defending claims against them. The commencement of an appeal may be justified in the public interest where it is necessary to avoid prejudice to the interests of the Commonwealth or an agency pending the receipt or proper consideration of legal advice, provided that a decision whether to continue the appeal is made as soon as practicable.

5. The obligation does not prevent the Commonwealth from enforcing costs orders or seeking to recover its costs.

FOOTNOTES

32. 91 ATC 4942, 22 ATR 707, (1991) 103 ALR 156, (1991) 32 FCR 148

33. quoting from the Administrative Review Council, a statutory body established pursuant to the AAT Act, in deliberations which led to that Council submitting to the then Attorney-General its report on the "Review of Taxation Decisions by Boards of Review" (Report No 17), itself quoting with evident approval the submission of the Taxation Institute of Australia to the Council in the context of that Review

34. see per Fullagar J in *Pascoe v. Federal Commissioner of Taxation* (1956) 30 A.L.J. 402 at p.403, and note *contra* the observations of Barwick CJ in *Gauci v. Federal Commissioner of Taxation* (1975) 135 C.L.R. at p.81 and Gibbs J in *McCormack v. Federal Commissioner of Taxation* 79 ATC 4111 at p.4,121

35. see, e.g., per Dowsett J in *Weyers and ors. v. Federal Commissioner of Taxation (No.2)* [2006] FCA 1319

36. as opposed to a rent-seeking activist with an agenda – see *Essenbourne Pty Ltd v. Federal Commissioner of Taxation* 2002 ATC 5201; (2002) 51 ATR 629; [2002] FCA 1577; *Walstern Pty Ltd v FCT* (2003) 138 FCR 1 (Hill J); *Spotlight Stores Pty Ltd v FCT* 2004 ATC 4674 (Merkel J); *Caelli Constructions (Vic) Pty Ltd v FCT* 2005 ATC 4938 (Kenny J); *Cameron Brae Pty Ltd v FCT* [2006] FCA 918 (Ryan J); *Indooroopilly Children Services (Qld) Pty Ltd v. Federal Commissioner of Taxation* [2006] FCA 734

37. per Hill J in *Walstern Pty Ltd v. Federal Commissioner of Taxation* 2003 ATC 5,076 at p.5,096

38. per Isaacs J in *Commonwealth Agricultural Service Engineers Ltd (in liquidation) v. Commissioner of Taxes (S.A.)* (1926) 38 C.L.R. 289

39. FCR O.52B r.5(a)(v)

40. per Hill J in *Bartlett v. Federal Commissioner of Taxation* (2003) 54 A.T.R. 261 at p.265, 2003 ATC 4,962 at p.4,965

41. *Anatomy of a Federal Court Tax Case* (2000) UNSW Law Journal 237 at 238-239

42. (1975) 134 CLR 640

43. at p.686

44. (1977) 136 CLR 214

45. at pp.227-8

46. taken from *Rio Tinto Ltd v Commissioner of Taxation* (2004) 55 A.T.R. 321 at p.324

47. see, e.g., *Melbourne Steamship Limited v Moorhead (1912)* 15 CLR 133 at 342; *Kenny v State of South Australia (1987)* 46 SASR 268 at 273; *Yong Jun Qin v The Minister for Immigration and Ethnic Affairs* (1997) 75 FCR 155.

48. UCPR, rule 5(1)

49. UCPR, rule 166

50. *Taxation Administration Act* section 8K

51. **ibid**, paragraphs 14ZZK(b), 14ZZO(b)

52. One recent example was the refusal, in a Statement of Facts Issues and Contentions, to admit the statements that "The Gove alumina refinery, and the associated bauxite mine, is located near Nhulunbuy on the Gove Peninsula in the Northern Territory" and "The GJV is a vertically integrated bauxite mining and alumina refining operation. The refinery operation, in particular, is highly technical. The GJV has a skilled work-force", only the first of which was subsequently admitted in response to a Notice to Admit Facts. Another was the refusal to admit documents which were relied upon in particulars given in relation to other parts of the ATO case as supporting a conclusion that fraud or evasion was involved.

53. Certainly the observations of Sundberg J in *Rio Tinto* do not appear to have encouraged a change of approach on the part of the ATO, although it seems clear that his general approach is viewed as correct, given the views of the Full Federal Court as expressed in another interlocutory appeal in the same matter: *Commissioner of Taxation v Rio Tinto Limited* [2006] FCAFC 86.

54. See O.72

55. There is, moreover, nothing about the position of the Revenue which would place it outside the category of litigants in respect of whom an order for indemnity costs might be made: such an order was made in *Westpac v Commissioner of State Revenue* [2004] QSC 19 following on unreasonable rejection of an offer to settle.

56. subsection 177F(6)

57. subsection 177F(7)

58. Case X88 90 ATC 640

59. see *Silly Solly Management Pty Ltd v Commissioner of Taxation* [2001] FCA 710

60. As Hill J. observed in *Walstern* (supra) at p.5,079: "If indeed it be the case that both the deductions claimed and the fringe benefits tax contested were respectively disallowed and the assessments upheld, it is difficult to see how the Commissioner could fail to proceed to collect tax found to be properly payable under the law."

Author's Profile

Mr David Rusell QC *was called to the Bar in 1977, having been admitted as a solicitor in 1974. Admitted to practice in New South Wales, Queensland, Victoria, the Northern Territory, the Australian Capital Territory and Papua New Guinea, David took silk in 1986 and holds that office in all the above jurisdictions except Papua New Guinea.*

Tax Risk Management

- Various Perspectives on Corporate TRM -

(Part II) India, New Zealand, Malaysia

India

Mr Atul Dua

1. Introduction

Businesses operate in a dynamic environment, with ever changing governmental policy and demand side dynamics. As a result, the decisions, activities and operations undertaken by such businesses leads to a number of uncertainties. One such uncertainty facing businesses today is the uncertainty arising from a fluid fiscal policy and regulatory regime. These fiscal uncertainties may stem from the interpretation and application of law to a particular set of facts and may arise over facts or from an incomplete understanding of the current requirements of a particular system. The problem gets compounded as most businesses look to establish their presence and operate out of multiple jurisdictions, some of which may actually be less developed jurisdictions lacking sophistication both with respect to the fiscal policies and regulation. Such a situation increasingly necessitates that head offices evolve various mechanisms such as a tax risk management framework to monitor, identify and develop strategy to manage tax risks, bearing in mind the local laws, transfer pricing regulations, accounting guidelines etc.

Tax Risk Management framework

The Tax Risk Management (TRM) framework should essentially address critical risks such as compliance, accounting, transactional, operational risks etc. and for the purpose cover the following components:

1. Tax efficient operational management

The attitude of the management towards tax risk, their objectives and their strategy to achieve the same gets reflected in the way operations of the organization are performed. This outlook can be gauged from whether there exists a completely codified tax risk minimization policy to achieve the organizational goals with negligible tax risk.

2. Strong accounting and reporting system

Accounting system should attempt to capture organizational processes and transactions in a manner that tax risk is minimized. The hallmark of an efficient accounting system is the ability to identify the changes in the external factors as well as the internal factors and achieve the expected level of assurance. In order to establish such a responsible reporting framework, it is imperative that competent individuals are allocated significant role in management of tax risks through the accounting function.

3. Tax and legal compliance system

This refers to the detailed procedures established to manage the tax risks from the perspective of compliance. It involves compliance of all the tax laws implied in the operations as well as the general legal compliance. It is also important that such a compliance management system integrates management of tax risks with the overall risk control framework of the organization.

4. Establishment of true compliance and governance culture

The term carries a very wide import and refers to inculcating a spirit of voluntary compliance. The spectrum of such a culture should cover legal and tax risks as well as risk of an adverse corporate image and reputation. Additionally, risk of a poor perception on corporate governance front about the enterprise is also an important

focus area in the present times. Interestingly, solutions that are designed to address all these risks also cater to TRM in a major way, as there is a very close and direct linkage among them.

In India, TRM framework is a new development and business enterprises are still coming to terms with the exigencies of a TRM system. As a function, TRM is not amenable to complete segregation from the overall enterprise risk control framework and hence is managed by a combination of outsourcing of functions like procedural compliances and in-house execution of the critical aspects. The whole concept is still evolving and does not therefore enjoy access to settled methodologies and relevant benchmarking tools.

TRM awareness

The last few decades have been years of massive challenges for the world economy. There was a depression at the American stock market in the early 2000s and stock prices continued to be low for several years, until recovery began in 2003. The period of depressed prices had its fair share of various corporate scandals. The numerous acts of malfeasance that came to light such as Enron, Parmalat generated a lot of support for introduction of reforms towards disclosures, transparency, responsibility et al. As part of the exercise to restore trust in corporations and securities markets, Sarbanes Oxley Act of 2002 ("SOX" or "Act") was enacted which introduced sweeping governance changes. In terms of sections 302, 404, 409 of the Act, companies are required to disclose material changes affecting financial reporting and operations.

Section 302 of the Act obligates the principal executive officer and the principal financial officer to certify in each annual report or quarterly report that they have evaluated the effectiveness of the internal controls. The Officer is also required to certify that he has reviewed the report and that the financial statements and the financial information included in the report fairly presents in all material respects the financial condition and results of the operation of the company and does not contain any untrue statement of any material fact or omits to state a material fact necessary in order to make the statements. The report is also required to comment on the effectiveness of the internal control system.

Similarly, Section 404 of the Act prescribes that each annual report shall contain an internal control report which shall state the responsibility of management for establishing and maintaining an adequate internal control structure, procedures for financial reporting and shall contain an assessment of the effectiveness of the internal control structure and procedures followed by the company.

Additionally, Section 409 obligates the companies to disclose to the public on a "rapid" and "current" basis additional information concerning material changes in the financial condition or operations of the company.

In order to ensure compliance with the provisions of the Act, companies are required to report all material facts affecting the company. The fact that taxes aspect every business transaction and represent one of the largest expenses incurred by the company makes it imperative that the internal control system of the company is designed to effectively identify and manage the tax risks.

Similarly, in Australia, the Commissioner of Taxation[1] had written to the public company boards requiring them to identify the taxation risks associated with their organizations, determine which risks are acceptable and which are not and put in place a process to manage the risks. In this context, the Australian Commissioner also posed ten questions that the boards needed to consider in relation to their businesses. The boards are required to consider the possibilities of perverse findings in tax adjudications, evaluate the risks arising there from. The Australian tax office has also published a list of seven criterions that are being used by them to assess an organization's tax risk. The seven criterions are:

- Business and transactions;
- Globalization;
- Attitude;
- Systems of Compliance;
- Perceptions of stakeholders;
- Materiality; and
- Application of law.

In addition, the Australian Tax Office has also listed six key areas that it is going to focus on at the time of reviewing the tax risk profile of a business:

- Whether the group's financial or tax performance varies substantially from industry norms?
- Are there significant variations in the amounts or patterns of tax payments?
- Are there unexplained variations between economic performance, productivity and tax performance?
- Are there unexplained losses, low effective tax rates, and cases where part or the entire group consistently pays low tax?
- Is there a history of aggressive tax planning?
- Are there weaknesses in the group's structure, processes and approaches to tax compliance?

Similarly, in India, listed public companies are required to comply with the provisions of the Clause 49 of the listing agreement ("Clause 49") entered by them with the relevant stock exchange. The clause prescribes corporate governance norms including the formation of audit committee and board composition that need to be adhered

by the listed entities. Audit Committees are required to review the internal audit reports relating to internal control weakness. Additionally, in terms of Clause 49, the CEO (Managing Director or Manager appointed in terms of the Companies Act, 1956) and the CFO (the whole time Finance Director or any other person heading the finance function) are required to certify to the board that they have reviewed the financial statement and the cash flow statement and that the statements do not contain any materially untrue or misleading statement or omit any material fact. The CEO and the CFO are also required to certify that they have indicated to the auditors and the audit committee any instances of significant fraud that they may have become aware of. The certification contemplated under Clause 49 is broadly in line with certification required under the provisions of section 302 and 404 of the SOX. Additionally, the company is also required to keep the board informed about the risk assessment and minimization procedures. The procedures are subject to periodic review. Thus, in view of the above noted provisions of Clause 49 it becomes imperative that risk assessment and minimization procedures are established and designed so as to:

- Enable the identification of the tax risks pertaining to the enterprise;
- List out the risks based on their potential threat;
- Communicate the risks to persons engaged in dealing with the risk;
- Put in place a detailed set of procedures and system to manage such risks;
- Establish a mechanism to constantly monitor the efficacy of the risk assessment and management procedures, determine the deficiencies in the present set of procedures if any;
- Communicate the deficiencies in the present set of procedures if any; and
- Initiate the process of change in the mechanism based upon any new risks or lacunas that may have been identified in the existing system.

It acquires particular importance given the challenges offered by the dynamic and ever-changing fiscal environment in India and the fact that tax payments constitute a major component in terms of the total expenditure incurred by the company. A recent survey[2] conducted by Ernst and Young reveals the issue of frequent changes in the tax laws as the most important factor affecting TRM process. This is demonstrated by the introduction of new legislations and amendment to old legislations such as the introduction of the controversial Fringe Benefit Tax, migration to Value Added Tax (VAT) regime,[3] widening service tax net etc. The tax risk, as a result, gets accentuated due to lack of clarity relating to the interpretation and application of fiscal laws and the absence of timely access to tax information. This has led the majority of Indian businesses to treat tax risks as an operational risk (risk underlying the application of tax laws, regulations and decisions about the day to day functioning of the company) rather than transactional risk (risk associated with the specific transactions undertaken by the company). Further, as more and more businesses establish their presence in India, there is a greater incidence of risk arising from the related party transactions also. This risk is in the nature of transactional risk and needs to be specifically addressed by corporates in view of introduction of transfer pricing regulations in India in 2001. The survey also revealed that 28% of the respondents had put in place a full-fledged tax risk policy in place. Another 53% reported to have put in place some form of tax risk policy. The increased emphasis on tax risk management has meant that it has become a key performance measure of the efficiency of the tax function. The survey found that 83% of the respondents indicated that tax risk management was an important criterion for measuring the performance of the tax function. Of these, more than 50% felt that tax risk management had emerged as a measure of performance of the tax function over the past two years.

TRM in global environment

Highly volatile and tightening tax regulatory regime has cast a spell on taxation issues arising out of international operations and corporate transactions as well. Cross border taxation of various payments on account of royalties, fee for technical services, interests etc. are presently being audited ever more closely by revenue authorities. Pricing of products, services and other transactions in course of international relations between businesses referred to as 'transfer pricing' has also been viewed with lot of additional tax potential. In fact, Indian revenue authorities have recently concluded transfer-pricing audits in respect of tax year 2003-04 and have sent additional tax bills to many multinational corporates including leading automobile companies in order to garner revenue lost due to allegedly fabricated valuation of international transactions.

Implications of this new kind of tax risk in India are as follows:

- Increased chances of audit of international transactions.
- Increased formalities in respect of documentation of valuation, contracts and ascertainment and justification of pricing.
- Increased chances of misapplication of arms length principle and suspicion over reference value used in transfer pricing studies by revenue authorities.
- Increased complexity of the nature of transactions, contracts, concession agreements emerging out of public-private partnership leading to ever-new interpretations and adverse inferences being drawn by revenue authorities.

Therefore, there is now an awareness and concerted effort to gauge the threats and challenges thrown at transnational corporates. A determined endeavor is being made to work out a strategy for risk management and to exchange information by businesses engaging in international transactions.

The effective practices pursued in wake of these developments are:

- Streamlining of tax accounting information system
- Finalize a schedule of events that tax function must adhere to, activities that it must prioritize and preparing a complete compliance calendar.
- Providing a tax expert perspective into the deliberations of the audit committee.
- Appointing an international tax risk manager to take a global view of the risk assessment.
- Developing a constant updating and research culture to not only keep abreast of the latest amendments in tax laws but be able to pre-empt and pre-conceive probable risk arising out of subsequent amendment in laws and plan accordingly.
- Dealing with procedural and substantive issues at different priority level. It is important that newly adopted compliance culture helps in avoidance of violation of fiscal laws.
- Harnessing the power of IT to develop an effective and potent compliance mechanism.

Long term implications of the changes to TRM

It is true that tax risks are no longer an issue between revenue authorities and a business enterprise. The risk actually impact company's overall finance function, operations, compliance framework and its overall corporate reputation. In wake of the recent changes to the risk environment certain implications have emerged.

There is an increase in the involvement of the CFO in order to create an effective momentum in respect of:

- Designing a reporting system that provides comprehensive documentation.
- Effective communication of compliance and planning issues associated with control of tax risks.
- Spreading a culture of extended and updated awareness of the current business climate in respect of emerging tax risks.
- Developing ability to deal with increasing scrutiny by the board as well as audit committee.
- Suitable focus on satisfying ever-increasing disclosure and transparency requirements in a time efficient manner.
- Maintaining a balance between true compliance with disclosure requirements and the necessary confidentiality implicit in tax matters.

It is generally understood that these changes to TRM process requires increased budgetary allocation to accommodate and suitably adjust the risk control framework without any long-term benefit to the organization. However, it needs appreciation that world over, revenue authorities are under pressure to garner resources for welfare measures and are catching up with inventive and thoughtful tax planning that corporates indulge in general. Therefore, new fiscal laws and amendment to the existing laws shall remain order of the day leading to consequent requirement of continuous fine-tuning of the risk management system. Hence any cost benefit analysis of changes to TRM system needs to consider these realities.

Tax risk management has implications not only for the entire enterprise risk framework, finance and tax function but also for external advisors like accounting firms, tax advisors, legal advisors, investment bankers and specialist consultancy firms etc. Increasing complexity of business laws and the current climate has led to demand for higher level of specialization on part of the professional services firm and the consequent increase in their professional liability. In India, external auditors are required to verify and report on a whole new corporate governance mechanism at work [4] and are also required to report on tax payments and controversies pending at various forums in their annual audit report [5] under company law. Additionally, there is a well-defined system of Tax Audits [6] to be conducted by qualified accounting professional under Income tax laws in India. It is however observed that all these professional services firms are providing satisfactory services even as they are expected to put up with increased expectations of the business. Today, there is no end to the 'knowledge of business' required on their part together with complete understanding and anticipation of the client's perspective. They are increasingly perceived as 'partners in progress' providing pragmatic and cost effective business solutions.

Conclusion

Tax risk management and its perception as a potential stumbling block in smooth conduct of business has always been there in the Indian corporate boardrooms. It has always been considered as a part of the overall risk control infrastructure. However, it is also true that it has been visualized as a corporate goal in itself, only of late. Therefore, a cultural change is required in respect of compliance, acceptance, trust, credibility and fairness in all spheres of corporate business. Though there is already an increased focus on compliance but planning and voluntary action on part of the tax function is also important. Formulation of a balanced approach is also an extremely important tool to identify all significant tax risks to ensure their time bound management. While benchmarking to the existing practices is essential, it is also important thatthe risk management system put in place also raises the bar of transparency and compliance to higher levels.

It is obvious that some companies have done better on the risk management front only because their tax directors were part of the overall risk control framework and hence were able to deal with tax risks in a much more efficient manner. Empowerment of tax directors, removing the problem of resource allocation and strengthening of the audit committee as an institution shall definitely allow corporates to contribute effectively to a well-defined code of best practices on the issue of tax risk management.

FOOTNOTES

1. PricewaterhouseCoopers LLP- Tax Risk Management Report, 2004
2. India Tax Survey – undertaken by Ernst and Young between September and November 2005.
3. Fiscal policy makers in India have planned a national unified VAT in the nature of GST from April 1, 2010. Recently, VAT has replaced the age-old sales tax system at the state level.
4. Owing to introduction of clause 49 on corporate governance norms in the standard listing agreement prescribed by capital market regulator i.e. SEBI.
5. Vide Para 4 (ix) (b) of the Companies (Auditor's Report) Order, 2003. Section 44 AB of the Income Tax Act, 1961 prescribes compulsory tax audit of business enterprise on fulfillment of certain conditions relating to quantum of turnover / professional receipts.
6. Section 44 AB of the Income Tax Act, 1961 prescribes compulsory tax audit of business enterprise on fulfillment of certain conditions relating to quantum of turnover / professional receipts.

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1. Introduction

Corporates are in an era of continuing tax reform and ongoing tax audit activity both nationally and globally. Corporates in New Zealand face increased tax risks due to many recent legislative changes, the global governance environment and increased tax audit activity. In this type of environment, tax risk management (TRM) has become an integral part of corporate governance in New Zealand.

It is possible to identify the importance of TRM in New Zealand corporate governance through the increased involvement of regulatory agencies, creation of TRM strategies by corporates and global pressure. Importantly, research undertaken in 2004 showed that 90% of New Zealand corporates identified risk management and tax audits as a key challenge they would face within the following two years.[1] TRM and corporate governance are inseparable as tax is a significant aspect of financial reporting. In order to comply with financial reporting requirements corporates must ensure that the correct tax treatment is being applied across the entire organisation to arrive at the correct final tax position. However, corporates must not only be compliant with tax law, they must also ensure the implementation of tax decisions accords with corporate governance principles.

2. Increased Involvement of Regulatory Agencies

A significant pressure on corporates to ensure tax decisions accord with corporate governance principles derives from the increased involvement of regulatory agencies in the area. The fallout from corporate failures in the United States (US) led to new rules and regulations that would have worldwide effect, such as Sarbanes-Oxley legislation (SOX) in the US. The changes occurring in foreign jurisdictions and the global environment caused New Zealand to question how rigorous its domestic corporate governance standards were and how regulatory agencies could encourage good governance.

On this basis, New Zealand's regulatory agencies undertook a review of corporate governance standards. This work was considered necessary from a governmental standpoint to preserve New Zealand's reputation as an expert economy that maintained the highest standards according to international principles.[2]

The review took place between 2002 and 2004 by governmental and non-governmental regulatory agencies including:

- The Securities Commission (Independent government regulator of investments);
- NZX (Private regulator of New Zealand's listed exchanges);
- The New Zealand Inland Revenue Department (NZIRD); and
- Accounting Standards Review Board (Independent government entity for accounting standards).

The review was informal and did not constitute a co-ordinated effort across each organisation.

New Zealand companies where shares are traded on US exchanges or US companies with New Zealand subsidiaries already had to comply with the onerous requirements of SOX. On conclusion of the review, New Zealand regulatory authorities decided not to have to duplicate the SOX rules and add to the compliance burden. Instead, New Zealand undertook a principle-based approach to corporate governance and financial reporting and introduced legislative change where it was deemed necessary which would affect TRM.

Another foreign change that had a direct affect on New Zealand regulation was the decision by Australia to adopt International Financial Reporting Standards (IFRS) for Australian accounting purposes. The speed of Australia's decision was in part a response to the Enron and WorldCom accounting catastrophes.[3]

When deciding if New Zealand should adopt IFRS those consulted considered that the credibility of New Zealand's financial reporting would have been placed at risk had New Zealand standards been continued with.[4] Additionally, the Government believed the enhanced transparency of IFRS would ensure New Zealand continues to be perceived to have a robust corporate regulatory framework.[5]

3. New Zealand Domestic Measures

The Securities Commission on 28 November 2002 released a document outlining its views on corporate governance and financial reporting.[6] On the request of the Government, the Securities Commission subsequently issued non-binding principles and guidelines for corporate governance.[7] Relevant principles for TRM include:

- "The board should demand integrity both in financial reporting and in the timeliness and balance of disclosures on entity affairs.
- The board should regularly verify that the entity has appropriate processes that identify and manage potential and relevant risks."

A key platform of the principles is to encourage corporates to report methods used to achieve compliance. Therefore, these principles impose on boards certain obligations, albeit non-binding, such as reporting the company has rigorous processes for assuring the integrity of entity financial reports, dual sign off of accounts by the Chief Financial Officer (CFO) and Chief Executive Officer (CEO), reporting to investors and stakeholders on risk identification and management and relevant internal controls amongst others. These responsibilities are explained in the guidelines accompanying each principle.

Several changes were introduced to securities legislation in 2002 and 2004. The changes included imposing a continuous disclosure obligation on listed companies, providing the Securities Commission with wide inspection and enforcement powers, and prohibiting companies from indemnifying its directors.[8] These legislative changes were being considered prior to the Enron collapse, however, a disaster on that scale underlined the need for law reform in the corporate governance and securities area.

Complementing the changes made to securities legislation was the work completed by New Zealand's stock exchange, the NZX. The continuous disclosure provisions specifically refer to such rules in the listing requirements of a registered stock exchange. The NZX introduced continuous disclosure rules for listed companies and also introduced changes to the rules on corporate governance increasing the number of independent directors on boards and the establishment of audit committees. Additionally, the rules encourage the adoption of a Corporate Governance Best Practice Code.[9] The rules state the audit committee is responsible for such tasks as updating the board on financial matters, ensuring accurate financial records are maintained and reviewing financial reports.

It is clear that the Securities Commission Corporate Governance Principles and the NZX rules are equivalent to the provisions found in Title III of the SOX legislation. As stated above, it was considered that a non-prescriptive approach would be more effective in New Zealand for companies not required to comply with SOX.

The NZIRD has reacted in a less formal way to the increased awareness of corporate governance by changing its focus in the auditing and reviewing of taxpayers by introducing a risk analysis system.[10] The new "risk identification focus" is intended to ensure a more timely review of taxpayer's affairs, to keep up-to-date with current commercial tax practices and reduce the costs associated with tax audits. Accordingly, the NZIRD now proactively undertakes risk reviews of large corporates to establish a risk profile of each company before a tax audit is even considered. Targeted corporates will receive questionnaires asking for certain information, such as:

- significant tax adjustments;
- effective tax rate;
- approach to TRM (formal systems, board involvement, responsibility etc); and
- international tax issues.

From this information, the NZIRD builds a risk profile to identify whether the corporate is a high or low risk entity. In future this approach will be extended into the mid tier of companies as well.

The effectiveness of the changes made by the regulatory authorities was proven when New Zealand was reviewed by the International Monetary Fund (IMF). New Zealand's financial system and securities regulation were given a clean bill of health, subject to some minor recommendations under the IMF's financial sector assessment programme.[11]

3.1. New Responsibilities Of CEOs, Boards And Audit Committees In New Zealand Due To Regulatory Changes

The implementation of the above changes has introduced new responsibilities for CEOs, boards and audit committees in New Zealand.

The requirements of the SOX legislation must be adhered to by New Zealand companies listed in the US and US subsidiaries based in New Zealand. Therefore, affected New Zealand corporate directors must establish audit committees, ensure separation of service providers between audit and non-audit work, introduce "whistleblower" procedures, introduce and adhere to codes of ethics and ensure appropriate internal controls are in place under SOX 404. The affected companies have been in the process of ensuring compliance since 2002 and audit fees in New Zealand have increased significantly during this period.[12]

Changes are currently being considered in the US to adapt less strict SOX 404 rules, as company listings are driven to foreign exchanges in London and Hong Kong.[13] This review will not benefit the New Zealand companies that have completed the process of checking internal controls. However, if the intended change of deferring the SOX 404 compliance deadline is introduced, then New Zealand companies in the compliance process or intending to issue securities in the United States will be of assistance.

Where the SOX rules are not relevant to New Zealand companies, the principles issued by the Securities Commission and the NZX will apply.

The principles and guidelines on corporate governance issued by the Securities Commission duplicate the SOX requirements such as the requirement of not allowing the position of CEO and Chairman to be held by the same person. The principles are not prescriptive, because of the market shift in New Zealand towards improved transparency. Most large New Zealand companies have instituted best practice corporate governance principles. The majority of New Zealand directors see the voluntary model as delivering ideal results and moving to a more prescriptive model would be a step backward.[14]

Where the NZX Corporate Governance Principles & Guidelines (NZX CGPG) are adopted, significant obligations are imposed on officers of a company. Individually, directors are required under the NZX CGPG to:

- adhere to ethics codes which impose a high standard of care;
- undertake continuous training including a director certification course;
- have their performance formally assessed; and
- not have a disqualifying relationship as an independent director (i.e. no conflicting relationships that could influence decisions).

It is also a requirement that at least one director has a financial background.

Requirements for the board as a group include quarterly financial reporting, if the company is in the top 50 listed companies, a minimum number of independent directors, separation of the CEO and Chairman, disclosure of material differences to NZX CGBP, and establishing an audit committee. The audit committee must consist of a majority of independent directors, keep a written charter outlining committee responsibilities and be subject to performance reviews.

The continuous disclosure requirements introduced through the changes to securities legislation requires issuers, and therefore the directors of an issuer, to disclose all material information to the market under the NZX listing rule.[15] If an issuer does not comply, the company is liable to suffer penalties of up to NZD 300,000 and can be forced to disclose the information to market by the Securities Commission. Further, directors are required to disclose all of their interests held in public companies.[16]

While the above changes impose specific obligations on CEOs, boards, and audit committees in New Zealand, no explicit requirements have been issued by the NZIRD. In contrast, NZIRD's actions supplement specific requirements as a check on how the corporate governance procedures are affecting a company's tax obligations.

If information gathered from the NZIRD risk analysis suggests that a company may have poor controls and significant tax exposure, the company will be given a high-risk rating and is more likely to be audited. Therefore, the NZIRD's shift to risk analysis has meant corporates

have to consider their tax risks, reduce them and introduce the appropriate controls to avoid a tax audit.

There have been no New Zealand examples of dramatic corporate failures in recent times. However, the collapse of several low-level New Zealand finance companies and the near collapse of a listed company have brought increased awareness to governance issues. These examples have caused regulators, companies and their directors to re-examine industry regulation and its effectiveness.

3.2. Emerging TRM Process Risks For Businesses

Prior to Enron, TRM as a concept was not on the radar of most corporates. The increased focus on financial reporting and risk management has brought attention to tax as a corollary. Therefore, TRM is a new endeavour for many corporates and the emerging process risks in developing their TRM practices relate to ensuring its TRM framework accords with the best practice and is aligned with their business goals.

Many corporate governance principles and pieces of law affecting governance practices have been recently introduced in New Zealand. Companies need to ensure TRM processes conform to both legislative and best practice requirements. Where they do not, unwanted consequences may occur. For example, under new securities legislation in New Zealand, if directors do not disclose all of their interests held in other companies they can be fined up to NZD 30,000.[17] Additionally, if failure to follow best practice creates a negative (and newsworthy) situation, company's reputation will be at risk. Therefore, companies need to be aware of the rules and law that applies and introduce TRM processes to ensure the business is compliant.

This approach applies equally to individual directors. Directors are operating in a new era of corporate governance and need to ensure they are familiar with the necessary requirements. Therefore, a process risk for directors is ensuring they are aware of their obligations and the applicable rules.

The new rules can be very detailed and/or require a great deal of work by companies and directors to obtain compliance. Section 404 of the SOX is an example of a governance rule that has required a lot of work by companies, much to their chagrin.[18] Companies risk getting lost in the detail and losing track of the higher goal of getting the TRM process right. Consequently, an emerging process risk is not aligning the TRM framework with business strategy. If TRM is not aligned with business strategy, there is a possibility its implementation will be counter-productive, adding stress to both compliance and administration of the business.

Additionally, changes to tax legislation and the increased involvement of some regulatory agencies have resulted in an increase in stress to the New Zealand tax environment.

New Zealand is currently in an ongoing period of significant tax change that began in 2004. There is a risk that corporates are not complying with tax rules accurately after the rules change. Research of Australian and New Zealand corporate taxpayers shows that 80% believe tax is becoming more complex and the workload is increasing accordingly.[19] Therefore, it is difficult for businesses to initiate an effective long-range tax plan that recognises all the newly introduced technical risks. Changes to tax rules are likely to occur frequently; therefore this pressure will always be a factor to a TRM framework and should be included in the risk assessment.

The corporate governance and financial reporting changes have not added new tax reporting requirements. Companies do not have greater obligations over what they are required to report for tax purposes, but they have a greater responsibility to ensure the process undertaken to achieve the results is more robust. Companies recognise that in the current environment there is no room for inaccurate financial statement provisions for tax, as inaccurate reporting will damage both public perception and share price of the company. As such, additional stress is applied to the TRM framework to ensure that the disclosures regarding tax are correct and will withstand a tax audit review.

Notwithstanding the above, the increased involvement of the NZIRD by introducing tax risk questionnaires has created another compliance requirement for businesses. A corporate is not required by law in New Zealand to complete the questionnaire. But to avoid gaining a reputation of being non-compliant, corporates will need to enter into the risk analysis process. This is an additional burden that stops those responsible for tax matters from focusing on their job. However, it is arguable that entering the process will make companies who have not considered tax as a risk think twice about how TRM is perceived by the company.

3.3. Perceived Responsiveness And Helpfulness Of The Regulatory Agencies In Assisting The Businesses In Dealing With The Tax Risks

The additional chore of completing the NZIRD's risk analysis process adds to the tax compliance burden. Tax compliance already represents the greatest proportion of compliance costs for businesses in New Zealand and so more compliance obligations are not welcomed by corporates.[20] Added to this burden is the perception that the NZIRD is one of least helpful government agencies in New Zealand, placed 8th out of 12.

Respondents to the 2005 Business New Zealand & KPMG survey have a negative view of the NZIRD. Issues raised in the survey included a lack of expertise, administrative inefficiencies and general lack of helpfulness. Some respondents commented that the NZIRD has a prevailing view that the taxpayer is guilty unless they are able to prove they are innocent. The response of businesses is in contrast to the NZIRD's aspiration to improve its perception in the community.[21]

The Securities Commission and NZX are perceived favourably in the regulatory environment, but it is noted that they have duplicate roles in some areas.[22]

Notwithstanding additional stress on TRM frameworks, a majority of directors (58%) believe a regulatory body should be introduced to oversee financial reporting. Such a move would increase public confidence and ensure consistency of reporting.[23]

4. Corporate Responses and Strategies in New Zealand

For a corporate, TRM determines where tax risks lie and making sure appropriate processes and procedures are in place to ensure management is informed of risks, exposure is reduced and potential liabilities managed.

Although tax may be considered a 'centralised' service (that is, the responsibility of the CFO and the finance team), many other personnel across the firm are involved in functions and processes that may have a tax impact. Despite the broad impact of tax on the business, recent research undertaken has shown that in 60% of the corporates surveyed, no one is responsible for tax at board level.[24] Generally, the board relies on the CFO bringing tax matters to their attention on an ad hoc basis. In the new environment of increased emphasis on corporate governance and NZIRD activity, this historic approach is no longer acceptable.

Global companies in New Zealand receive the benefit of the corporate governance practices from their parent. But New Zealand companies involved with TRM are creating their own corporate governance practices that reflect global best practice from both a strategic and operational level.

At an operational level, TRM processes are being introduced in New Zealand corporates for each type of tax paid by a company (including direct, indirect (i.e. Goods and Services Tax) and withholding taxes). These processes include a properly documented and tested TRM framework that asks, investigates, documents and tests:

- whether the existing process is documented;
- who has responsibility for the process (and who provides backup when they are not there);
- contingency plans, including dealing with NZIRD audits, mistakes and tax shortfalls;
- changes required to processes and responsibilities; and
- risk priority, for all of the following areas:
- tax technical policy;
- tax procedures/controls;
- instructions for both the finance team and the business units;
- tax issues management/requests for advice;
- staffing delegations/signing authorities;
- training processes;
- financial systems/data integrity /controls;
- tax report/return preparation processes;
- tax report/return review processes; and
- tax payments.

At a strategic level, TRM is being incorporated into the responsibilities of the audit committee. Audit committees have undertaken in their charter to ensure that tax planning and compliance reflects the standards required of the board according to best practice. Best practice under the NZX and Securities Commission's principles ensures that performance of directors on the audit committee in this area will be reviewed and scrutinised.

The effect of the actions listed above is that boards will develop a formal TRM profile with fully developed risk mitigation and management strategies. TRM strategies are taking an enterprise/all taxes view to enable the board to have a thorough understanding of the tax function and associated risks. The board is then able to assess if risks are controlled at the appropriate level and no issues exist that could affect the bottom-line or the reputation of a business. Additionally, external tax advisors are being invited into board meetings to present reports on the risks being faced by their company.

The broad TRM framework for effective management of risks in New Zealand is usually made up of three key elements:

- A board policy statement setting out such things as the board's desired risk profile, board responsibilities and management reporting requirements and how the tax risk strategy fits in with the board's broader priorities;
- A tax charter derived from the board policy statement setting out roles and responsibilities, reporting and communication channels, guidelines for engaging external tax advice, and processes around significant transactions (including the sign-off of tax risks); and
- A tax risk register recording the identified tax risks, the processes in place to manage those risks and the recommended changes to bring those risks within the desired risk profile set by the board.

Normally, the identified risks in the register are ranked by their likely impact on the company. This allows a company to prioritise processes for dealing with the risks.

The risk rating of the identified risks is a function of the likelihood of the adverse event occurring and the potential damage that could arise. An event that would be catastrophic for the company, should it occur, may have a high risk rating even if the likelihood of it occurring is relatively small due to the controls in place. Similarly, if it is almost inevitable that a company will make an error in one aspect of its tax obligations, these risks are treated as high even when the financial cost is relatively small.

Where tax risks are not known, procedures will require that external advisors be appointed to help either formulate a solution or confirm the business is taking the right approach. Where a knowledge gap exists, training is required to upskill employees so they can carry out tax related duties. As each transaction in a business can have a tax effect, procedures are being established to check completed work for errors by independent review or reasonability testing.

Implementing the processes above demonstrates an organisation is adhering to their obligations under their TRM framework and corporate governance best practice principles.

4.1. Pertinent Types Of Risk In New Zealand

Of particular concern to the NZIRD are pertinent tax technical risks, such as:

- related party financing into New Zealand;
- intangible property (sale and leaseback of intangibles and transactions between associated parties with transfer pricing implications);
- asset valuations and allocations for depreciation purposes; and
- international financial reporting standards (IFRS) and transitional year tax filing disclosures.

The risk for a business is an increased probability of being audited, should the NZIRD identify that the business is involved in one of the practices above without a sound risk management framework.

Another risk is the significant tax changes that are being implemented. New Zealand's main piece of tax legislation, the Income Tax Act, is being rewritten creating both intended and unintended changes and new rules are being introduced. The cumulative effect of the changes is that the New Zealand tax environment is in a state of flux. Companies are trying to keep up with the change in order to take the correct technical positions and avoid making mistakes.

5. Benefits of a Sound TRM Framework

Introducing a TRM framework is intended to be a positive planning measure taken by a company. In 2004, 60% of New Zealand companies thought they did not spend enough time on planning and risk management, and they did not have a long-range tax plan or TRM framework.[25] Therefore, it would be possible to conclude that in 2004 most New Zealand organisations recognised the need to manage their tax risk. Subsequently, New Zealand organisations have reacted positively to the new governance and financial reporting changes.

The benefits delivered by a TRM framework, as perceived by corporates, include:

- shifting the tax function's workload from one of
- compliance to strategy and alignment of tax strategy to business strategy;
- the reallocating of resources from 'fire fighting' to more time spent on evaluating risks and opportunities can deliver positive financial outcomes;
- containing and controlling costs more effectively through the accurate identification of tax exposures and opportunities;
- strengthening the relationship with the NZIRD by demonstrating best practice and thus minimising the discomfort and distraction of an audit or investigation;
- providing the board, company executives and other stakeholders with confidence that risks have been understood and managed proactively alongside other business risks carrying similar financial or punitive consequences; and
- ensuring that tax positions taken by the company and ultimately represented in its financial statements are consistent with its tax risk profile and are correct and supportable in a regulatory sense.

5.1. Industry Differences and Ensuring Best Practice

As discussed above, TRM for a corporate means determining where tax risks lie and making sure appropriate processes and procedures are in place to ensure management is informed of risks, exposure reduced and potential liabilities managed. On this basis, there are no differences between industries on the objectives of TRM. However, the focus of a TRM framework can depend on the type of industry in which a company operates. For example, there are specific tax rules applying to the life insurance industry. Consequently, TRM will have a different tax technical risk focus in the insurance industry than the computer industry. It follows that the technical risk focus in a TRM framework, and how the risk is managed and identified, will accord to the tax rules that apply to an industry. However, tax risks that apply to industries equally, such as an NZIRD audit, can be identified and managed in a similar manner.

5.2. Managing the TRM Control Framework

Based on the TRM framework, procedures and process are implemented into each department relating to each tax type (including direct, indirect and withholding taxes). Risks are managed by documenting the existing process and regular reviews. Responsibility for each process is clearly defined and contingency plans are created for each tax area.

Whether the function is normally in-house or outsourced will depend on tax type. For example, it is usual practice in New Zealand corporates for value-added tax (known as Goods and Services Tax (GST)) and fringe benefit tax (FBT) [26] to be an in-house function. These companies will use computerised accounting packages to determine their GST/FBT liability and complete returns to the NZIRD. Review or reasonability testing will be undertaken to establish whether the function is operating correctly by using computer modelling. External advisors are engaged to help with reviews of GST and FBT in order to confirm the business is taking the right approach.

Responsibilities for other tax functions are commonly outsourced to external advisors, such as the preparation of income tax returns. As each transaction in a business has an income tax effect, it is not common to see a coherent strategy in relation to income tax, except in large transactions. Therefore, the income tax return is a key annual process to review the tax positions taken by a company and determine where improvement is required. However, the income tax return is commonly viewed as a compliance procedure and not a vital tool in TRM.[27] For example, corporations are not using benchmarking procedures to compare themselves to similar entities within their industry. Unfortunately, data can be difficult to obtain due to the confidential nature of information relating to corporate transactions. However, the NZIRD, through its risk questionnaires, is developing a comprehensive body of knowledge regarding effective tax rates, common tax positions and other income tax related issues. Therefore, the NZIRD is developing a powerful information advantage over corporates who are unaware of these issues creating a significant risk.

6. TRM in a Global Environment

New Zealand is one of the smaller players in a global context but is fully integrated into the worldwide economy as an exporting nation with no domestic trade barriers. Therefore, the foreign change in attitude to TRM has had an affect on how New Zealand corporations manage their tax risk. New Zealand companies do not want to be seen to be lagging behind international best practice.

As New Zealand is an export economy, a significant risk for companies is the amount of tax they are required to pay in foreign jurisdictions. Where a New Zealand company operates in many jurisdictions its goal is to maintain a low effective tax rate. To achieve this goal transfer pricing is used as a tool to manage a company's tax risk.

Transfer pricing between New Zealand taxpayers and their overseas associates continues to be an important focus for the NZIRD at the operational level. The NZIRD includes transfer pricing questionnaires as part of their risk analysis of both larger corporates and "middle market" companies with turnovers between NZD 50 million and NZD 150 million.

This increased transfer pricing focus means there is an increased risk that a New Zealand company investing offshore is susceptible to disputes with tax authorities in foreign jurisdictions. Importantly, transfer pricing is firmly in the sights of both New Zealand and Australian tax authorities, with an increasing number of companies under audit scrutiny in both countries.[28] For example 31% of Australia/New Zealand parent companies surveyed in the 2005/06 Ernst & Young Global Transfer Pricing survey have been notified by the tax authorities with a request to view transfer pricing documentation outside of an audit. The implications for a New Zealand company investing offshore is that the company needs to ensure that transfer pricing planning and procedures are implemented to avoid tax disputes in countries which they are operating.

The increased focus on transfer pricing is being supported by changes to double taxation agreements (DTA) between countries. For example, the DTAs with the United Kingdom, Netherlands and Australia have been updated in the last two years to allow for greater information sharing and mutual tax collection. Consequently, there is significant cooperation between New Zealand and foreign tax authorities.

On this basis, greater transparency will exist of a business' global tax position. Tax authorities will be able to determine if a company is managing its tax liabilities appropriately or, for example, double dipping with deductions. Consequently, not only will transfer pricing policies will be scrutinised but so will all tax policies of a business.

6.1. Dealing With The Increased Tax Complexity When Operating Internationally

New Zealand companies are able to deal with increased international tax complexity through the network of DTAs and transfer pricing.

Since 2004, New Zealand has accomplished significant tasks in the DTA area with four new DTAs being signed. New Zealand is now party to 32 DTAs covering all of its major trading partners. DTAs provide certainty to taxpayers by determining which country has the right to tax income. This enables taxpayers to structure their operations accordingly.

Transfer pricing is another tax concept that aids companies with international operations. In conjunction with principles developed by the Organization for Economic Co-operation and Development (OECD), international practices are harmonious in many areas, providing economic certainty to companies operating overseas. If transfer pricing policies conflict between jurisdictions, the mutual agreement procedure in a DTA can be invoked.[29]

An important transfer pricing tool is the Advance Pricing Agreement (APA). An APA is an agreement between a company and the revenue authorities of relevant jurisdictions setting the transferred prices of goods between countries. The main benefits associated with an APA include (i) certainty, (ii) substantial risk reduction or risk elimination of being audited, (iii) reduction in ongoing compliance costs, (iv) co-operative dealings with the NZIRD, and (v) flexibility in approach on the part of the NZIRD.

It is to be noted that where no DTA exists, tax certainty for companies is drastically reduced and tax risk rises accordingly.

7. Long-Term Implications of the Changes to TRM

The long-term consequences of changes to TRM are largely beneficial to the New Zealand regulatory and business environment.

From the perspective of New Zealand directors, the introduction of audit committees has been successful and the scope of financial reporting is appropriate.[30] However, the positive attitudes reflect a high-level view of the issues affecting corporate governance. When the detail of compliance costs are analysed, the outlook is not as rosy.

Tax compliance costs currently represent the highest proportion of statutory compliance costs in New Zealand. That proportion increased by 33% between 2003 and 2005 during a period of minor tax change.[31] Compliance-type regulation has only long-term negative impact on New Zealand businesses as it draws the focus away from a business' main goals.

Fortunately, from 2005 onwards, broad tax changes to reduce compliance costs were introduced. Additionally, the current New Zealand Government has proposed further change to reduce tax compliance costs to achieve its goal of increasing productivity in New Zealand.[32] TRM is a process that can facilitate easy transition to new tax rules and help change corporate opinion from the current negative view.

Added to the increasing tax compliance costs is the cost and time of:

- completing NZIRD risk questionnaires;
- the transition to IFRS; and
- adherence to SOX and domestic corporate governance requirements.

When complying with these changes, the short-term implications for corporations are negative as costs erode the bottom line. However, from a long-term perspective, the corporate governance and financial reporting changes are considered to have positive and beneficial implications. For example, it is considered accounting harmonisation with Australia (by adopting IFRS) will simplify transactions between each market.[33]

The NZIRD hopes their new risk-based approach will reduce costs and provide greater timeliness of tax audits.[34] However, in pursuing this new approach, the NZIRD may, unwittingly or otherwise, can interfere unduly with a business's day-to-day processes and operations. Dealing with the new risk questionnaires can be a time consuming and costly process for businesses, a fact often lost on the NZIRD. However, where there is uncertainty in a company's tax portfolio its risk exposure can be reduced by ensuring adequate controls are in place around identified risk areas.

7.1. Implications For Third Parties

The long-term implications of increased awareness in TRM are significant for third parties.

Tax advisors will benefit as demand for their expertise and services increases. Businesses face a high risk-exposure to tax in New Zealand due to legislative changes and the need to manage tax for corporate governance purposes. The services of tax advisors will be needed to help formulate TRM frameworks and provide advice where required by their tax risk policy.

The intention of implementing TRM is to benefit all stakeholders in a corporate. However, where a company fails in its tax obligations the effects can be considerable. Increased tax to pay, penalties and interest that are imposed, will affect the earnings of a business. Publicity can have negative implications for a company's reputation. In turn, the share price of a company can be forced down. The directors of a company could be considered to have failed shareholders and important customers. In the end, TRM is an opportunity for the exercise of good business judgment consistent with other corporate governance measures. If the board takes a leadership role with tax it will be able to promote the necessary fiscal and ethical responsibility that will benefit all stakeholders and avoid negative consequences.

8. Conclusion

At the time of the Enron collapse (and to the date of writing), there have been no New Zealand examples of dramatic corporate failure. Nonetheless, New Zealand regulatory authorities have adjusted to the new global environment by implementing corporate governance and financial reporting best practice. These measures have had a subsequent effect on the introduction of TRM in New Zealand corporations.

New Zealand corporates face increased tax risks due to continuing tax reform, the global governance environment and increased NZIRD activity. In this type of environment, effective TRM is crucial. Business taxpayers are incorporating TRM into their corporate governance processes at both a strategic and operational level. This means determining where their tax risks lie and making sure appropriate processes and procedures are in place to ensure management is informed of risks, exposure reduced and potential liabilities managed. These companies recognise TRM is an opportunity for the exercise of good business judgment consistent with other corporate governance measures.

The collapse of several low-level New Zealand finance companies, caused by a combination of poor management and the economic slowdown, has caused a rude awakening into the need for effective regulation congruent to the industry. In another example, questions have been raised regarding potential conflicts of interest of directors in a listed company at risk of collapse that has witnessed its share price drop to less than 10% of its initial public offering value. These examples show that despite New Zealand not experiencing a major corporate failure to the extent of the US at the beginning of this century or the United Kingdom in the early 90s (e.g. Polly Peck, BCCI), New Zealand remains susceptible. Indeed, in a 2004 speech, Roel Campos of the US Securities and Exchange Commission warned New Zealand against complacency when he told a local audience "Maybe you just have not found out about [the failures] yet".[35]

1. *Ernst & Young, Australasian corporate tax function survey, (2004).*
2. *New Zealand Parliament, speech by Margaret Wilson (Minister of Commerce) to the Accountancy Standards Review Board: "Adoption of International Financial Reporting Standards" on 24 November 2004.*
3. *Bebbington, Joseph and Song, Esther, Preliminary report on the adoption of IFRS in the EU and New Zealand, University of Canterbury, National Center for Research on Europe (2004).*
4. *Ibid.*
5. *See note 2.*
6. *New Zealand Securities Commission, Strengthening confidence in New Zealand's capital markets: Statement on certain aspects of corporate governance and financial reporting, (2002).*
7. *New Zealand Securities Commission, Corporate governance in New Zealand principles and guidelines, (2004).*
8. *Securities Amendment Act 2002, Securities Markets Amendment Act 2002, and Securities Amendment Act 2004.*
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10. *NZIRD, Corporates Contact, (2005).*
11. *International Monetary Fund, Financial sector assessment programme report: Detailed assessment of standards and codes: IOSCO objectives and principles of securities regulations, (2004).*
12. *Allen, S., A whole new way of auditing, Dominion Post (26 November 2004).*
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14. *PricewaterhouseCoopers New Zealand,Corporate Issues Report, (2006).*
15. *Sec. 19B, Securities Markets Act 1988.*
16. *Sec. 19T, Securities Markets Act 1988.*
17. *Ibid.*
18. *See note 13.*
19. *See note 1.*
20. *Business New Zealand & KPMG, Business NZ and KPMG compliance cost survey, (2005).*
21. *NZIRD, Statement of intent 2006-2009, (2006).*
22. *See note 14.*
23. *Ibid.*
24. *See note 1.*
25. *See note 1.*
26. *Fringe benefit tax is a New Zealand tax imposed by the Income Tax Act 2004 on non-cash benefits provided to employees.*
27. *See note 1.*
28. *Ernst & Young, Ernst & Young Global Transfer Pricing Survey 2005-06, (2006).*
29. *If a transfer pricing adjustment has been made by a foreign tax administration that results in double taxation, a taxpayer may request competent authority consideration under the Mutual Agreement Procedure Article in New Zealand's DTAs (Tax Information Bulletin [2000] 12(1) Transfer Pricing Guidelines).*
30. *Ibid.*
31. *See note 20.*
32. *New Zealand Parliament, media statement by Michael Cullen (Minister of Finance) and Peter Dunne (Minister of Revenue) on 25 July 2006.*
33. *Ibid.*
34. *NZIRD, Corporates Contact, Issue 28 (2005).*
35. *Campos, Roel, Sarbanes Oxley and the regulatory environment in the United States, Wellington (19 February 2004).*

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Malaysia

Dr Nakha Ratnam Somasundaram

Introduction

Modern businesses operate in a fluid environment – constantly changing to accommodate the needs of a demand side economy, shifting government policies, intricacies of tax laws in the various tax jurisdictions and other variables of a "global village" business environment.

This requires the corporations operating in such environments to evolve various risk management strategies, with Tax Risk Management (TRM) gaining relevance and importance on a global scale.

This article explores the issue of TRM in the context of the Malaysian corporate scene and the Malaysian revenue administration.

The economic environment

There is presently a demand for improved corporate governance by the shareholders and even Revenue authorities – a result of the recent high profile corporate scandals like Enron and Palamat. Such scandals have an unfortunate effect of drawing the unwanted attention of the authorities. As a consequence, business organisations are required to disclose more information to the stakeholders – the investors, the Revenue authorities and anybody interested in the company. Thus came about the Sarbanes-Oxley Act of 2002 which focused corporate attention on risk management including the management of tax risk associated with the financial reporting process.

In addition the Corporate Law Economic Reform Package (CLERP 9) requires boards of listed entities to be confident that the financial reports present a true and fair view in all material aspects of the organisation's taxation responsibilities and, furthermore, that it has established policies on TRM.

What is TRM?

It is basically a risk management strategy, but TRM is a relatively new development brought about by increasing pressure of the authorities in relation to the conduct of business.

TRM essentially involves identifying existing and potential tax risk in the organization, prioritizing those risks, developing appropriate strategies for each of the risk area and more importantly communicating these to the key stakeholders. As an added measure of continued sustenance TRM requires establishing procedures for evaluating future tax risk, the tax tolerance of the organization, and where possible, identifying tax opportunities, considered by tax pundits as a by-product of TRM.

TRM has begun to take hold of organisations as it has come to be recognized that tax and related cost can have a significant impact on the profitability of the corporations.

The TRM framework

What is involved in a TRM framework?

It involves a wide range of systems that must be put in place to work seamlessly and in harmony with business operations.

As such the objective of TRM is to identify critical risks in tax compliance that will have flow-back impact on accounting, transactions and business operations.

Under a TRM strategy, a strong accounting system should also capture all the organizational process and transactions achieving a level of expected assurance and confidence in the system.

There should be a detailed procedure to achieve tax compliance. But since tax compliance is not an isolated risk, it has to be integrated with the organizational legal compliance system, with appropriate competent professionals managing the system.

The culture in the organisations should be tuned towards achieving a high level of voluntary compliance and self imposed responsibility.

The tax risk exposure

Tax risk arises for several reasons, one major factor being the variant interpretation of the tax law giving rise to uncertainties in its implementation. In Malaysia this

uncertainty is compounded by the Inland Revenue Board, in certain instances, taking a defiant attitude to court decisions, for example by issuing Practice Statement that are not in consonance with particular court decisions.

In the case of *Ketua Pengarah v Penang Reality Sdn. Bhd. & Anor* [(2006) 2 CLJ 835] a taxpayer carrying on the business of housing developers bought land and from time to time disposed certain undeveloped portions; and later, on the remaining land, the company built houses, of which some were let out for rent, and others were sold off from time to time. The profits on the sale were brought to charge by the Revenue and the company paid the taxes raised. Two pieces of land that were bought as early as 1956 were however acquired by the government in 1980 for which compensation of RM 1.03m was paid in 1982. The Revenue sought to tax this amount as business income; but the taxpayer contended that it is capital, and appealed against the assessment on the grounds that as the land had been held as a capital asset, the receipt from the disposal would not constitute a revenue gain. Furthermore, the land was compulsorily acquired by the government and in such a situation there cannot be imputed a trading intention into the transaction.

The Special Commissioners of Income Tax found for the Revenue. When the case came up to the Court of Appeal, the issue was dismissed – the disposal of the land by way of a compulsory acquisition does not constitute a sale proceeds as the "element of compulsion vitiated the intention to trade". The decision was significantly influenced by the case of *Lower Perak Co-Operative Housing Society Bhd v KPHDN* [(1994) 3 CLJ 540 where Edgar Joseph Jr. SCJ in delivering judgment had said:

'...The finding of the Special Commissioners that there was some element of 'forced' selling of the subject lots' (and) because of the circumstances beyond its control was amply justified by the evidence (and) ... a forced sale cannot constitute a sale the proceeds of which are subject to tax because the element of compulsion vitiates the intention to trade...'

The Inland Revenue Board then came out with a 'Decision Impact Statement' where attention was drawn to section 24(1) (a) of the Income Tax Act 1967 which provides that any debt that arises in respect of stock-in-trade which is compulsorily acquired shall be treated as gross income from the business. The statement emphasized that the DGIR is of the opinion that section 24(1) (a) of the Income Tax Act 1967 (as amended) is applicable 'to other cases where the asset compulsorily acquired is a stock-in-trade of a person.'

The issue that was not resolved was of course what constitutes stock-in-trade and what constitutes investment, particularly in companies that deal in land! The law on what is gross income and its taxability, of course, could also give rise to varying interpretation and consequently to disputes that could involve costly litigation.

In the case of *EB v KPHDN* [(2006) AMTC 1197] the taxpayer incorporated as a private limited company, and later becoming a public company was an investment holding company providing management services to its subsidiaries in its group. In 1994 the company was awarded a contract under which it would be required to build, operate, supply and deliver hydroelectric power. For this specific purpose a new company, Bakun Hydroelectric Corporation Sdn. Bhd. was incorporated as a wholly owned subsidiary. The objective was to provide solely engineering services. By a letter dated 16 Feb 1995, the Economic Planning Unit gave the Bakun Hydroelectric Corporation Sdn. Bhd sole power and authority to carry out the project. However one and a half months later the government announced that the project will have to be carried out with a joint venture partner – resulting in the taxpayer's share in Bakun Hydroelectric Corporation Sdn. Bhd.'s being whittled down to a mere 42%. Consequent to the loss of power and control the taxpayer then gave up all its rights and power in the project to Bakun Hydroelectric Corporation Sdn. Bhd for a consideration of RM 300m. The amount, recognized in the accounts as 'management fees' – but later in the appeal admitted as an error of classification - was taxed and the taxpayer appealed, claiming that it was payment for loss of rights in the project. The Special Commissioners found for the taxpayer.

In Malaysia for example, companies eager to take advantage of murky laws and legislation can run foul of the law and often find themselves in hot soup. Claiming a seemingly innocuous allowance 'allowed' by the legislation could be a tricky adventure – requiring delicate tax risk management.

Under Schedule 7A of the Income Tax Act 1967 (as amended), for instance, companies can claim reinvestment allowance on capital expenditure incurred on a factory, plant or machinery used in Malaysia for the purposes of a qualifying project.

A 'qualifying project' is defined to mean:

Para 8(a) A project undertaken by a company in expanding, modernizing or automating its existing business in respect of manufacturing, processing of a product or any related product within the same industry or in diversifying its existing business into any related product within the same industry.

This allowance is popular because it enables the company to reduce the tax charged - on account of the higher allowance available on the expenditure incurred. In fact the reinvestment allowance is in addition to the capital

allowance available on the same expenditure under schedule 3 of the Income Tax Act 1967 (as amended) and this account for its popularity.

Another attraction is that the reinvestment allowance given would qualify for a two tier tax exempted dividend distribution under Para 5(a) and (b) of Schedule 7A.

However terms like 'expanding', 'modernizing', 'automating' etc are not defined. Furthermore, the term 'manufacturing' and 'processing' are prone to subjective interpretation – in a wide sense by the taxpayer and in a narrow sense by the Revenue authorities.

In this context there is a need to understand the business, the commercial circumstances surrounding a transaction and the tax law that allows for a deduction of expenditure or the taxability of a receipt. Taxpayers must assess the risk, plan and implement strategies to eliminate, avoid or, at its worst, mitigate any tax risk.

It would be useful therefore, for board members of corporation to ask some relevant questions suggested by Michael Carmody, the Australian Tax Commissioner, in a media release in June 2003.

Bearing in mind that 'judgments about tax compliance need to be part of the corporate governance process of every company and board' he had suggested that corporate board members, while not necessarily tax experts, nevertheless must ask some pertinent questions as responsible board members. Questions asked could range from whether the board has any confidence in the accounts and the tax advice given by the professionals to whether how such advice falls in line within the existing law and practice, and so on.

In case the advice given is, for example, contrary to the current practice of the tax office, what is the inherent risk and, should the case goes for litigation, what is the risk of the matter being determined in favor of the tax office? More important, the board should consider any potential fiscal and economic risk that may spill out should the case be decided against the company.

In the case of a proposed transaction, it was suggested by the Taxation Commissioner that the board should consider whether any proposed transaction (particularly for example in the case of transfer pricing issues) would increase the risk profile of the company and thereby increase the risk of a possible audit scrutiny (... in plain language it means: If we do this, are we asking for trouble?).

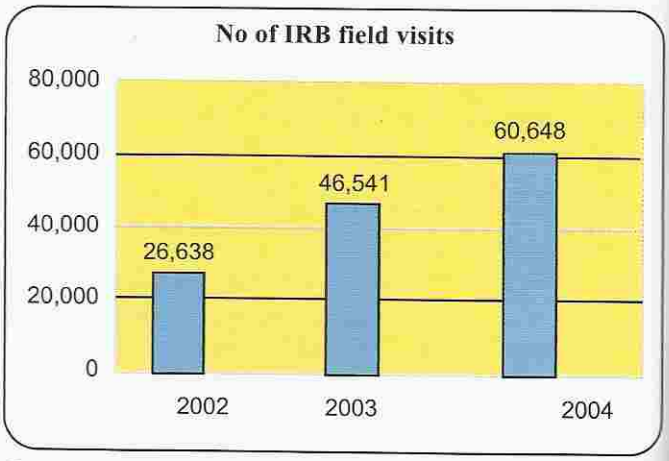
In situations where both the board, and the professionals advising them, is not too sure of the legal fallout, then it may be desirable to approach the Revenue authorities for guidance.

But then again, with the Revenue authorities giving 'guidance' with a host of caveats attached, one must be prepared to take all the risk necessary, albeit a considered one.

What is your risk from the Inland Revenue Board?

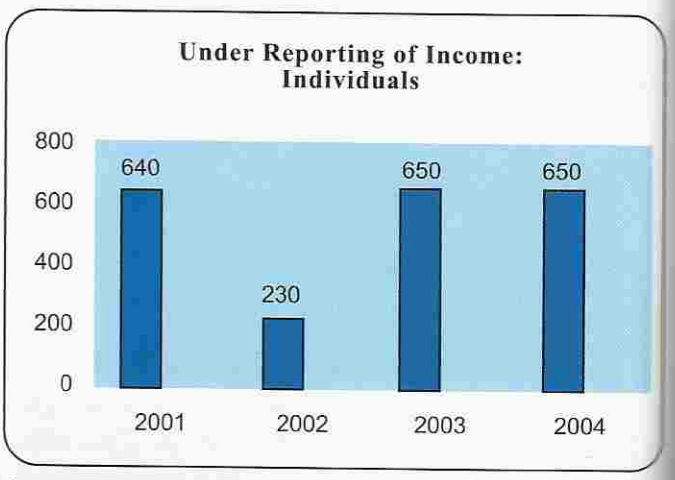
The Inland Revenue Board has been very active on the ground since the introduction of the self assessment system in Malaysia. It has taken an aggressive approach to taxpayer compliance – ranging from identifying taxpayers who have not notified their chargeability to the Inland Revenue Board, to picking up taxpayers who have under declared their income. (See Charts 1, 2 and 3).

Chart 1
Number of Inland Revenue Board field visits



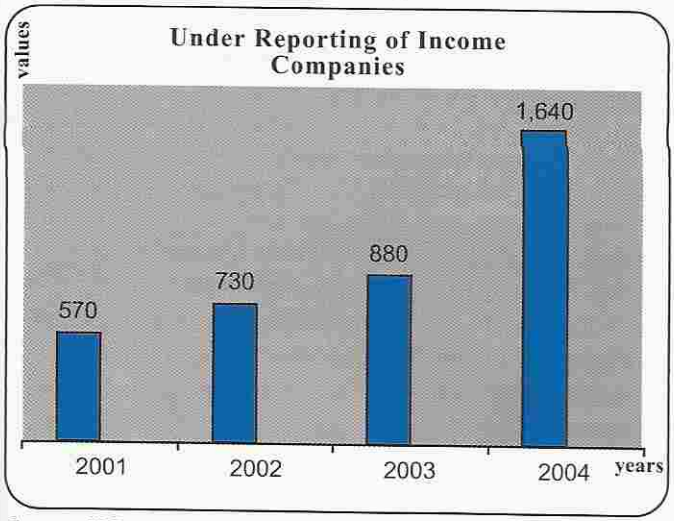
Source: IRB Annual Report

Chart 2
Under reporting of Income: Individuals



Source: IRB Annual Report

Chart 3
Under reporting of Income: Companies



Source: IRB Annual Report

The figures indicate that the Inland Revenue Board has certainly good reasons to be suspicious of taxpayers. And so one could expect that the Inland Revenue Board would continue in its assiduous pursuit of the not-so-diligent taxpayers, in keeping with the operational policy to enforce 'voluntary' compliance.

With this new role of the Inland Revenue Board, are you at risk?

It has been the avowed ambition of the Inland Revenue Board to audit all taxpayers at least once in five years – this means a 20% 'turnover' every year. Whether this target will be achieved or not is not the issue – what should worry taxpayers (and potential taxpayers) is that the Inland Revenue Board will come knocking on their door sooner…or later. It is only a question of time.

As an IRB's field audit has a potential to spill over into a full blown investigation, it would help if taxpayers could prepare themselves against a tax risk by avoiding specific trigger points. For a start, they could ensure that the financial and tax performance does not vary substantially from that of the industry standards. Any significant variation in the amount or even in the pattern of tax payments in the present, as compared to the past that could not be explained by proper economic indicators, is another area of risk - particularly where the economic performance, productivity and the tax assessed do not synchronize convincingly, or are inconsistent with the policy intent of the tax law.

Some aggressive corporations with a high degree of tolerance for tax risk should beware of continuous and unexplained losses, especially where part or all of the entities in the group consistently pay little or no taxes – these are entities that would be either picked up by the IRB's computer, or by some sharp nosed Revenue officer. This could be compounded by a weak management structure, improper process and compliance strategy towards tax issues.

TRM and the Inland Revenue Board

The Inland Revenue Board has contributed tremendously to the effort of TRM by the taxpayer both individuals and corporations by issuing several public rulings that range from the treatment of bad debts and its recoveries, treatment of rental income and indemnity insurance to mention a few. In fact, to date the IRB has issued 34 Public Rulings, 58 Procedural Instructions and 10 Guidelines including the Transfer Pricing Guidelines.

Under the self assessment system of taxation, the taxpayer is required to compute his own tax and the Inland Revenue Board would conduct tax audits to ensure that the compliance is complete. Towards this end the tax return requires the taxpayer to indicate whether the public rulings have been complied with.

Of course non-compliance is not a crime – where the taxpayer strongly feels otherwise, he could choose not to comply with a particular public ruling – but it would be wise to make a disclosure of such 'non-compliance' as required by another public ruling.

The Tax Agent and TRM

Most taxpayers leave tax compliance matters to the tax agent, or have the tax agent to advise them on the pertinent matters.

In doing so what is the tax agent's responsibility?

The effect of the self assessment system is to shift the determination of the income and the computation of the taxes thereon to the taxpayer – and taxpayer inevitably will shift this burden to the tax agent. Where the matter is complicated, the tax agents may advice the client on the appropriate course of action or stand to be taken. In offering such advice or in assisting the taxpayer the tax agent is expected to exercise 'reasonable care', the duty of which is enshrined in a new section 114(1A).

The Inland Revenue Board has explained in a Public Ruling (No 8 of 2000) that the term 'reasonable care' means 'the degree of care or conscientiousness in paying proper attention to a task that is expected, in a similar situation, of an ordinary person who, considering the circumstances and the foreseeable consequences, acts within reason, sound judgment and responsibility'.

The law comes with a minimum fine of RM 2,000 to a maximum of RM 20,000 or to an imprisonment of not more than three years – or both. Tax agents therefore have to cut a delicate balance between advising clients on tax

compliance and in situation of tax avoidance make sure that the boundary is not crossed over into tax evasion which would constitute a serious offence indeed.

Should the tax agent have in place a TRM program?

Apart from buying indemnity insurance, it would be wise for the tax agent to have a TRM infrastructure securely in place, and it might help to avoid cutting corners on experienced staff.

Tax Planning Risks in Malaysia

Can tax agents in Malaysia do tax planning for their clients? And in doing so, do they face any risk?

While expert legal opinion in Malaysia hold that if the tax planning process is transparent and is within the meaning and letter of the law – in other words, as long as the tax agent does not assist the taxpayer to file an incorrect return, or does nothing that can be construed as wilful, or having the intent to evade, or assist another person to evade tax – then such tax planning is acceptable.[2]

However if one observes the recent trend in the tax law changes in Malaysia, it would appear that even tax planning within the letter of the law can backfire in the long run.

For example in Malaysia, companies that have losses which are not fully deducted or set off against other income, and capital allowances that is not absorbed or not fully absorbed, can carry forward these losses and capital allowances to be set off against the income of the following year, or any subsequent year of assessment – i.e. it could be carried forward indefinitely. The losses can be set off against the statutory income from all business sources; and the capital allowance can be deducted from the same business source.

This feature of the tax law provided a simple and convenient tax planning mechanism to shift taxable income from a profit making entity to a company that is carrying an excess baggage of losses and capital allowances. Usually this is done by acquiring a loss making company and injecting the profitable business into this loss making company. The profits generated will be absorbed by the existing losses, thus giving the tax benefit to the acquirer. However law changes were put in place in the recent 2006 Budget whereby the amount of business losses and capital allowance ascertained for a year of assessment shall not be available for deduction in subsequent years of assessment if the shareholders of that company on the last day of the basis period for that year of assessment were not 'substantially the same'[3] as the shareholders of the company on the first day of the basis period for the year of assessment in which such amount would otherwise be deductible or given to that company.

The amendment which appears to be an anti-avoidance measure effectively restricts the deduction for the losses and capital allowances ascertained for prior years of assessment if 'substantial' changes take place in the shareholders of the company – an event that take place in mergers, amalgamations and reorganizations etc.[4]

Donations made to an approved institution are given a deduction against the aggregate income of the company, and this has the effect of reducing the taxable income by the amount of the donation made. While tax planning is rarely done by giving donations, one company in Malaysia literally wiped out its tax liability by paying out its income by way of a donation - all within the letter of the law.

In the local case of *Sabah Berjaya Sdn. Bhd. v KPHDN* [(1993) 3 MLJ 145], the taxpayer, a commercial company was asked to pay over all its surplus funds to the controlling body which was a non-profit making institution. Payments of 'donations' to this institution is exempted from tax as it is an 'approved institution' for income tax purposes.[5] The subsidiary then paid the surplus funds by way of a donation, instead of declaring dividends, over a period of eight years.

The Inland Revenue Board then took issue on the grounds that the payment has the effect of altering the incidence of tax (which is what all tax planning is about...!) and applied section 140, thereby disregarding the transaction.

On appeal, the Malaysian Court of Appeal held that the transaction, namely, the payment of the profits to the controlling body was a donation within the meaning of the relevant law, and therefore the company is entitled to a deduction for such 'donations' made.

Notwithstanding the fact that the donations made have the effect of a reducing the company's tax liability, the court held this was merely a tax mitigation scheme (there was a donation actually made and therefore expenditure actually incurred, and losses – by way of cash outflow – actually suffered). The company was 'not engaging in tax avoidance' and as such section 140 would not apply.[6]

The Inland Revenue Board however did not take too kindly to the matter and amended the law on deduction for gift and donation, introducing a proviso to restrict the amount of deduction for 'donations' in the case of companies to not more than 5%, and later revised to 7%, of the aggregate income of the company.

It would appear the Revenue authorities are taking a very close look at motives behind a transaction to determine whether it can be fairly regarded as one that was done

in the course of the trade or whether it is one that is designed to merely secure a fiscal advantage.

The latter is apparently not in the Revenue's menu.[8]

Future of TRM

In Australia, for example, the concept of 'Forward Compliance Arrangement' has been initiated under which it will be a voluntary arrangement between a large corporation and the Australian tax office, working together on a forward basis. While it is expected to minimize tax risk significantly, engaging in such a 'partnership' would require a substantial investment in TRM process and a commitment to transparency and continual disclosure – something large corporation may be loathe to do – and therefore its success will be a limited one.

Will Malaysia's Advance Ruling legislation[9] pave the way for such co-operation?

While the Advance Ruling allows the taxpayer to request for a ruling from the DGIR on a particular 'arrangement', it is not regarded as safe by Malaysian taxpayers, since the DGIR can pull the carpet from under one's feet – at any time - by withdrawing such rulings [10]

One would think that such uncertainties would be the very reason to warrant the setting up of a full fledged TRM structure in the boardroom.

Is Malaysia Ready for Tax Risk Management?

The writer had occasion to raise the issue of TRM in Malaysia with several leading corporate figures and tax agents recently.

The response:

...We have just started working on a program to make our clients aware of TRM....

...There is not much urgency or importance shown in this area by CEOs ...but there are signs that there is some sort of awareness

...We have put TRM infrastructure in place for a few selected clients but it was done at the request of the overseas parent company ... as part of a global program of transfer pricing strategy...

...We leave the tax matters to our tax agents who will tell us what to do...

Answers like these seem to indicate that Malaysian companies have a long way to go in incorporating TRM as an integral part of their management scene.

FOOTNOTES

1. *Public Ruling No. 8 of 2000.*
2. *Datuk D.P. Naban (2007), 'An Analysis from the Legal Perspective and the Consequence Under Sec. 114 and 114(1A) of the ITA 1967 and the Powers of the DGIR under Sec. 140 of the ITA 1967'. Paper presented at the 'Tax Risk Management Workshop' 3 May 2007, Malaysian Institute of Taxation, Kuala Lumpur.*
3. *The amendment is now contained in section 44(5A) and 44(5B) of the Income Tax Act 1967 (as amended) effective for the year of assessment 2006 and subsequent years of assessment [Act 644 of 2005, Sec. 9(b)].*
4. *Dr. Nakha Ratnam Somasundaram, (2006), 'Budget at a Loss: A Commentary of Selected Proposals in the 2006 Budget' Tax Nasional, Journal of the Malaysian Institute of Taxation, Vol. 14/2005/Q4 pp. 18-23*
5. *Donations made to approved institutions are deductible in full, subject to the availability of an aggregate income, under section 44(6) of the Income Tax Act 1967 (as amended).*
6. *This decision is in line with the approach adopted by the Privy Council in CIR v Challenge Corporation Ltd [(1986) STC 548.*
7. *The proviso to section 44(6) was effective from the year of assessment 2001 and subsequent years of assessment.*
8. *In Indofood International Finance Ltd v JP Morgan Chase Bank NA, London Branch [(2006) EWCA Civ. 158], a tax saving scheme using a special purpose vehicle was dismissed as not being commercially justifiable since the 'main purpose of the new financing structure is to avoid the increased withholding tax ...'*
9. *An Advance Ruling is a written statement from the tax authorities expressing their opinion on how a relevant tax provision would apply to a taxpayer in relation to a specific transaction or arrangement to be undertaken by the taxpayer. The Ruling is obtainable on the application of the taxpayer.*
10. *Under section 138B (1) of the Income Tax Act 1967 (as amended) the DGIR 'may withdraw any advance ruling made under subsection (1) by giving notice in writing of such withdrawal to the person to whom the ruling applies...'*

Author's Profile

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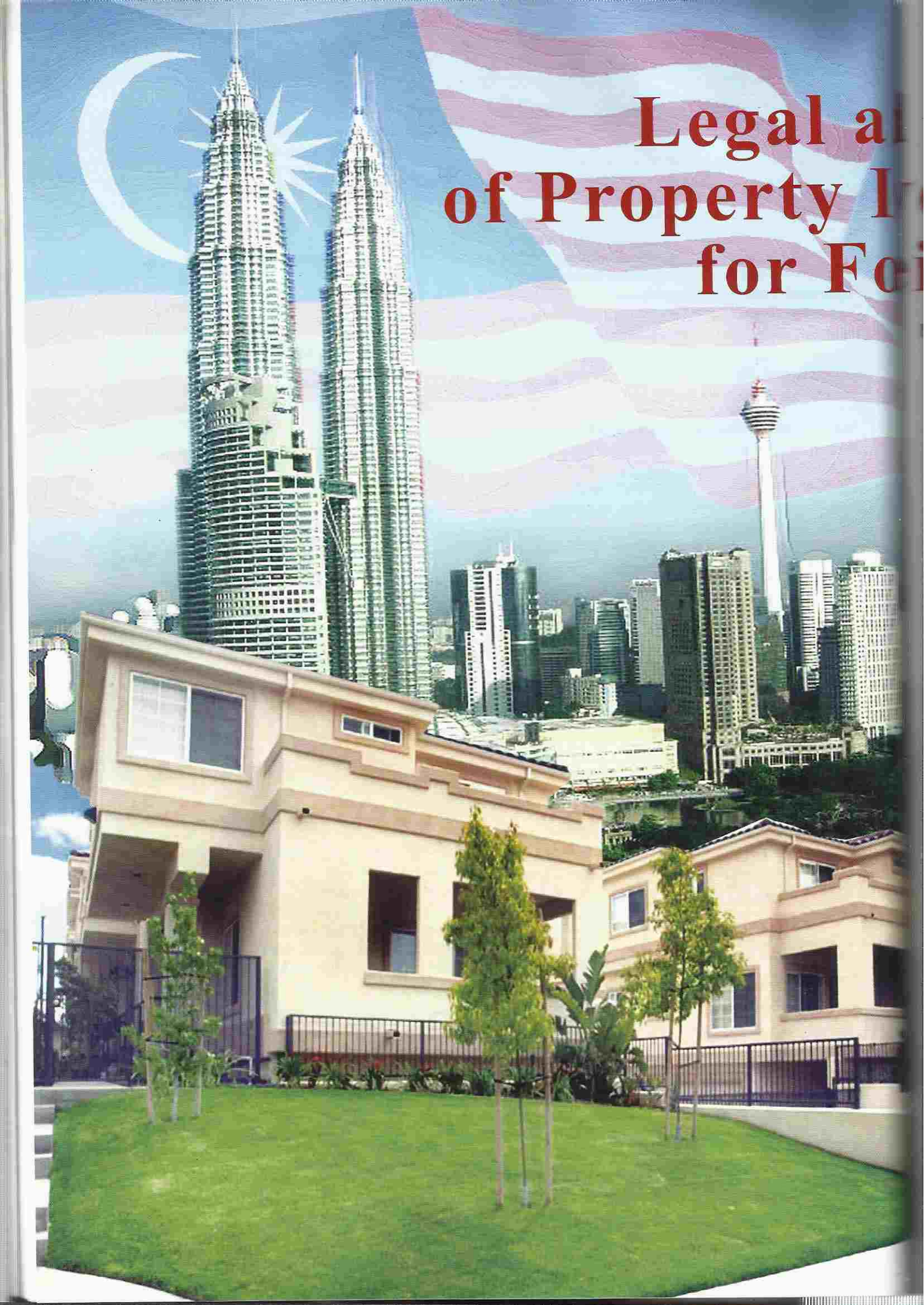
entertainment tax

- ***Regular naps prevent old age... especially if you take them while driving.***
- ***Marriage is a relationship in which one person is always right and the other is husband !***
- ***I believe we should all pay our tax with a smile. I tried - but they wanted cash***



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Other Aspects Investment in Malaysia Foreign Investors

Mr Benjamin Poh

The recent currency appreciation and strong economic growth, primarily driven by a surge in exports and commodities prices, has made Malaysia a favorite place to invest in for foreigners. On 21 December 2006, the Malaysian government officially removed the requirement of FIC (Foreign Investment Committee) approval for the purchase of residential properties priced at more than RM250,000 by foreigners in order to further stimulate the interest in high end property markets.

A foreign investor who is considering buying Malaysian property, should evaluate the potential investment return and risk and should also be aware of issues such as relevant authority approvals, succession, taxation, legal fees, financing and repatriation of funds.

The following table summarizes the legal benefits and disadvantages between a foreign individual holding property investments and/or incorporating a Company to hold property investments:-

	Individual	Company
i) FIC approval	Only allowed for property (e.g. residential, commercial and industrial) price at more than RM150,00 and require approval from FIC except for residential property price more than RM250,000. Disposal of property to another foreigner require FIC approval. Disposal of property price less than RM20 million to Malaysian need to notify FIC.	Only allowed for property (e.g. residential, commercial and industrial) price at more than RM150,00 and require approval from FIC except for residential property price more than RM250,000. Acquisition of industrial property without price limit is allowed but must form a locally incorporated company. No approval is required if industrial property purchased by the company is licensed by Ministry of International Trade & Industry for own manufacturing use. Disposal of property to another foreigner require FIC approval. Disposal of property price less than RM20 million to Malaysian need to notify FIC.
ii) Succession	Property will be frozen till obtaining Letter of Administration (if without a will) or Grant of Probate (if with a will), if one of the join holders passes away. Under the Malaysia Land Laws, the Tenancy In Common will operate where property held by 2 persons and above, the deceased person shares will pass to his/her successors not to the joint holders.	Business as usual, as the corporate is a separate legal entity, even if one of the shareholders passes away. It is advisable to draw up a shareholders' agreement to avoid unnecessary interruptions to business operation.
iii) Stamp Duty	Disposal of property subject to stamp duty as follows:- Duty First RM100,000 1% Next RM400,000 2% In excess of RM500,000 3%	Disposal of shares subject to stamp duty as follows:- RM3 per RM1,000 or part thereof

	Individual	Company
iv) Income Tax on Capital Gains	If found to be trading, a non-resident may be subject to income tax on gains at a flat rate of 28%.	If found to be trading, a company may subject to a flat rate of 28% unless paid-up capital is RM2.5 million or less, then subject to income tax on gain at 20% for the first RM500,000 and 27% in excess of RM500,000 in YA2007, 26% in YA2008.
v) Income Tax on Rental Income	Rental income may be taxed as non-business source if it is passively managed, therefore only direct expenses such as interest, quit rent and assessment, fire insurance and repair and maintenance will be allowed for full tax deduction. Whereas, indirect expenses such as administration expenses will be allowed 25% of tax deduction subject to limit of 5% of gross rental income. Any losses will not be allowed to carry forward for future tax deduction. Rental income may be taxed as business source if it is actively managed (e.g. usually not less than 4 units of properties), therefore both direct and indirect expenses will be granted full tax deduction and losses will be allowed to carry forward for future tax deduction.	Same for individual
vi) Real Property Gains Tax on Capital Gains *(Note: Income tax and Real Property Gain Tax on capital gain is mutually exclusive, e.g. The investor will only subject to either income tax or real property gain tax on capital gain but not both.)*	Disposal by an individual who is not a citizen or PR:- **30%** for disposal within 5 year after the date of acquisition. **5%** for disposal in the 6th year after the date of acquisition or thereafter.	Disposal by a company by transferring the property:- % Within 2 years 30 In the 3rd year 20 In the 4th year 15 In the 5th year or Thereafter 5 If it is a real property company (e.g the market value of property is 75% or more of the total tangible assets of the company and with not more than 50 members and controlled by not more than 5 persons), a non citizen or PR if disposal by transferring his shareholdings to others then the tax rate is **30%** for disposal within 5 year after the date of acquisition. **5%** for disposal in the 6th year after the date of acquisition or thereafter.
vii) Legal fee for drafting legal agreements	**Lease Agreement** **Monthly rental** — **Fee** For first RM10,000 — 50% (subject to a minimum fee of RM600) For the next RM90,000 — 20% In excess of RM100,000 — Negotiable On excess (shall not exceed 20% of such excess) **Tenancy Agreement** **Monthly rental** — **Fee** For first RM10,000 — 25% (subject to a minimum fee of RM300) For the next RM90,000 — 10% In excess of RM100,000 — Negotiable On excess (shall not exceed 10% of such excess)	Same for individual

<table>
<tr><th></th><th>Individual</th><th>Company</th></tr>
<tr><td>vii) Legal fee for drafting legal agreements (contd)</td><td><u>Sale & Purchase Agreement</u>
May be waived if purchase from developers directly. Otherwise, subject to the following:-
<table><tr><th></th><th>Fee</th></tr><tr><td>For first RM150,000</td><td>1%(subject to a minimum fee of RM300)</td></tr><tr><td>For next RM850,000</td><td>0.7%</td></tr><tr><td>For next RM2 million</td><td>0.6%</td></tr><tr><td>For next RM2 million</td><td>0.5%</td></tr><tr><td>For next RM2.5 million</td><td>0.4%</td></tr><tr><td>In excess of RM7.5 million</td><td>Negotiable On excess (shall not exceed 0.4% of such excess)</td></tr></table><u>Charges, Debentures and other Security or Financing Documents</u>
<table><tr><th></th><th>Fee</th></tr><tr><td>For first RM150,000</td><td>1% (subject to a minimum fee of RM300)</td></tr><tr><td>For next RM850,000</td><td>0.7%</td></tr><tr><td>For next RM2 million</td><td>0.6%</td></tr><tr><td>For next RM2 million</td><td>0.5%</td></tr><tr><td>For next RM2.5 million</td><td>0.4%</td></tr><tr><td>In excess of RM7.5 million</td><td>Negotiable On excess(shall not exceed 0.4% of such excess)</td></tr><tr><td>Principal instrument</td><td>full scale fee</td></tr><tr><td>Each subsidiary</td><td>10% full scale instrument fee (subject to a minimum fee of RM200 & maximum RM1,000)</td></tr></table></td><td></td></tr>
<tr><td>viii) Incorporation Fee</td><td>Less than RM500 if registering a sole proprietorship or partnership</td><td>Less than RM2,500 if incorporating a private limited company with an authorized capital of RM100,000</td></tr>
<tr><td>x) Other Maintenance Fee</td><td>Annual accounting and tax reporting fee, usually less than RM1,500 but also depending on number of property acquired</td><td>Annual accounting, audit, tax and secretarial fee, usually less than RM3,000 but also depending on number of property acquired</td></tr>
<tr><td>xi) Financing</td><td>Local bank may extend ringgit facilities up to a maximum of 3 property loans to a non-resident to finance or refinance the purchase or construction of immovable properties in Malaysia, excluding financing for purchase of land only which requires approval from Central Bank Malaysia</td><td>Same for individual</td></tr>
<tr><td>xii) Remittance</td><td>Free to repatriate any amount of own funds in Malaysia any time, including capital, divestment proceeds, profits, dividends, rental, fees and interest arising from investments in Malaysia</td><td>Same for individual</td></tr>
</table>

Disclaimer: *The Law is stated as at 31 December 2006. The views are provided gratuitously and without liability. You should consult your accountants or lawyers before relying on the above view for investment.*

Author's Profile

Mr Benjamin Poh *CA, LL.B (Hons), CFA, ATII, Senior Partner of Inpact International Affiliate, PCS & CO, Chartered Accountants. He is a qualified chartered accountant, law graduate from London University, a CFA Charterholder and Associate of Malaysian Institute of Taxation.*

The Post Importation Audit

Mr Thomas Selva Doss

The Customs Department has focused its attention this year on a number of crucial issues. One of them being the increasing number of importers intent on under-declaring the value of imported goods. The lower the value, the lower the import duty and sales tax paid. With increasing competition among the importers, it appears as though keeping the costs low legally is no more the rule of the day. Among the various methods to import goods as inexpensively as possible is to pay the least tax possible. The Customs Department has been aware of this for decades since the time the *Brussels Definition of Value* (BDV) for imported goods was implemented. With the introduction of the new World Trade Organisation (WTO) Valuation system since 1 January 2000 and the emphasis by the World Customs Organisation (WCO) to combat smuggling and under declaration of goods, the Malaysian Customs has been cautiously implementing measures to detect areas of high risk whilst balancing the economics of not hindering trade by embarking on a programme of "**risk management**".

This risk management programme is a modern, effective and efficient way of working. Importantly it assists the planners in Customs to manage their various functions properly and also assists them in deploying their resources more effectively. One of the most effective techniques in this programme is the post importation audit or *'pasca'* audit. Post importation audits are generally carried out for compliance verification purposes in the areas of valuation, origin, tariff classification, duty exemption and drawback. The objective is to verify the accuracy of the information provided at the time of importation and whether the goods were cleared within the framework of the laws, regulations and standard procedures. Post-importation audits are conducted "post" entry or after the goods have been cleared from Customs control.

The Audit Proper

The whole process starts with the Form *Customs No1A* commonly known as the value declaration form which is filled in together with the Import Declaration Form *Customs No.1* at the time of import. These two forms need to be presented to the Customs officer on duty at the Import Section of the port or airport via the Electronic Data Interchange or EDI system. This officer will then verify the particulars presented on both the forms and issue an approval for the goods to be released from Customs control. In many cases, a physical examination of the goods is carried out by the Customs officer on duty at the warehouse. Once the import duty and/or sales tax is paid, the goods are released from Customs control.

At the end of each day, all the hard copies of the value declaration forms will be forwarded to the *'pasca'* unit which controls the port or airport. With the help of a Customs database of goods entering the country diligent officers will examine the value of each consignment declared. Certain risk assessment techniques are used. Declarations which prove to be suspicious will be removed and forwarded to an audit officer in the unit. Once in the hands of the audit officer, the post importation audit will begin with the issuance of a letter to the company concerned. The auditor will then request for a number of documents pertaining to the importation of that consignment such as contracts and agreements between the consignor and consignee, supplier's invoices, proof of payment for the imported goods, bill of lading or airway bill, freight invoices and insurance certificates, purchase order and confirmation of orders, accounting records, financial statements and any other record or document that are relevant to the imported goods. Once all these information and documents are forwarded to the auditor, he will begin the post importation audit. There are standard operating procedures that need to be followed in conducting this audit. Most of them are classified information under the Official Secrets Act 1972. However, in a post importation audit basically three phases are employed – the selection phase, the auditing phase and the assessment and follow-up phase.

In the selection phase, profiling of the companies, risk assessment and audit selection is done. In the auditing phase, a pre-audit survey is conducted followed by a field audit and then the final report. In the assessment and follow-up phase, an internal assessment of audit performance is conducted and the Bill of Demand is issued. Throughout the whole process, the audit officers objective

is to ensure that the value declared for the imported goods is the 'transaction value' that is the price actually paid or payable for the goods when sold for export to Malaysia. Various adjustments to the value may be made either by adding certain costs or deducting certain costs from the value declared. Whatever it is, before the final Bill of Demand is issued, the audit officer must provide a clear explanation to the importer as to how he arrived at that final figure and also provide him with an opportunity to accept or refute that assessment. Normally both parties will have to agree to the assessment before the final Bill of Demand is issued. However, if the importer is not satisfied with the final assessment, he can appeal to the Customs Appeal Tribunal and argue his case before it. After the tribunal has reached its decision, if he is still not satisfied, he can always appeal to the High Court.

Customs Database

Malaysian Customs has encountered difficulties with building up a good database. The huge volume of goods moving in and out of the country means keying in tons of data into the computer each day. This is an area which should be given much importance by Customs. It is not easy to create an effective and up to-date database. Building a valuation database with both historical and current import data is a daunting task, particularly if it has to incorporate details of description of the goods, along with differences in quantity, quality, commercial levels, country of origin, name of manufacturer, brand etc. to provide meaningful comparison. It requires adequate financial, human and computing resources to build, maintain and update such a database particularly if the basket of imported goods is very large and varied. Moreover, the types of goods imported into Malaysia are basically raw materials and consumer goods varying in quantity, quality and price. Disparate fluctuations in price also makes it difficult to maintain an accurate database.

Customs officers will always look at the 'audit readiness' of the company in terms of record keeping. Contrary to the usual notion that the 'records' refer simply to import records, the officers will actually look at any records that relate to import declarations. They will also examine the internal company controls and procedures to assess the level of risk in the company's business transactions. Most of the companies that have been investigated face the basic problem of not maintaining consistent records of their importations. In addition to the absence of import records, many companies have a problem locating the necessary financial and accounting information to support the value declaration to customs. Even companies that pride themselves in having compliant practices and the best record keeping procedures are rarely ready for a Customs audit.

When faced with such an audit, most companies are at a loss on how to handle it. Questions such as

i) what are the specific issues involved in the audit?
ii) What are the records that Customs will request for?
iii) How is Customs going to conduct the audit etc. etc will arise.

Handling a post importation audit requires competent knowledge of customs procedures and documentation plus a clear understanding of the WTO Valuation system. Past working experience in the Customs Department will prove to be invaluable. Dealing with a *'pasca'* officer requires skill and experience. Almost all of these companies have no experienced personnel to handle the audit and will turn to their forwarding agents for help thinking that their experience in clearing goods from customs will help them in handling the audit. Few are aware that most forwarders are in no way competent to act on their behalf in handling the audit. Forwarders are registered with the Customs Department under Section 90 of the Customs Act 1967 to clear goods from customs control. Their primary role is to assist companies in preparing the relevant customs declaration forms for submission to Customs and facilitate the clearance of their goods. The initial customs training these forwarders undergo before attending the interview in order to obtain a licence to operate as a forwarder hardly prepares them to be competent in complex Customs and audit matters. Yet many importers are contented enough to let them represent their company in a Customs audit.

Enforcement

To show the importers how serious the customs department is in combating under-declaration of goods, the Director-General of Customs on the 24th January 2007 launched the post import verification unit on wheels. Twenty-one units of the vehicles known as Delta Tax rolled out by the end of January 2007. These MPVs are equipped with lap-tops, 3G data cards, digital and web cameras, fax machines, scanners, printers and equipment for teleconferencing together with sophisticated security features. Each unit comprises of three officers who would act as 'mobile auditors' and conduct checks on importers to verify the authencity of the information provided when the goods were brought into the country. The Director-General also stated that the mobile unit will stop as much leakages in taxes and duties as possible. They can check on companies and within minutes know if there are any discrepancies. However, identifying a discrepancy is only the beginning of the problem, proving that the importer has under-declared the value is a tedious task. Often Customs auditors are handicapped by the lack of information or uncooperative attitude of the importer. Without this information, it is extremely difficult for the auditor to have a proper basis for assessment.

Most importers look at Customs operations from a logistics perspective. Rarely do companies look at the compliance requirements for their import operations. Most of the functions in import-export operations are outsourced to forwarding agents and companies seldom verify the correctness and completeness of what is being declared to Customs. On the other hand, forwarders are more focused on Customs clearance and in practice, do not focus on the level of compliance in Customs operations. The intense competition among forwarders has made them more unscrupulous in their dealings. Their objective is always to help the importers to pay as low taxes and duties as possible. The Customs department is well aware that may forwarders work hand in hand with the importers to under-declare their goods. To point a finger at them is easy, but to come up with documentary evidence to penalize them is often difficult.

Companies should ensure that the forwarders not only clear the imported goods in the most efficient and fast manner but also ensure compliance of all Customs requirements. Past experience has shown that multinational companies put great emphasis on compliance as they do not want to be caught by Customs. Due to the volume of their goods, penalties can be pretty high. On the other hand, the medium sized and small importers try very hard to bring down the value of their goods to pay as little import duty and sales tax as possible. Customs has blacklisted a number of these companies and are constantly watching their import and export operations. Customs declarations are thoroughly scrutinized and in many cases their containers go through heavy screening.

Customs operations is a high-risk activity for importers and there are many reasons for this. The rules of the game have changed, and continue to change, putting importers at a high risk of committing errors in what is being declared to Customs. For importers, Customs forwarding is a high impact service and is integral to the supply chain. While there are numerous forwarding companies in Malaysia, the selection of a good and reliable forwarder is often difficult. There are basically two reasons why importers have to be careful when selecting its customs forwarders. One, Customs has increasingly become stricter in implementing its rules resulting in hefty fines for non-compliance. Secondly, the *'pasca'* unit has been beefed up with more trained and experienced officers. Their training and experience often aid them in looking at areas which inexperienced customs officers will often miss out. Any errors discovered by Customs not only lead to heavy penalties but may also cause future delays at the point of importation.

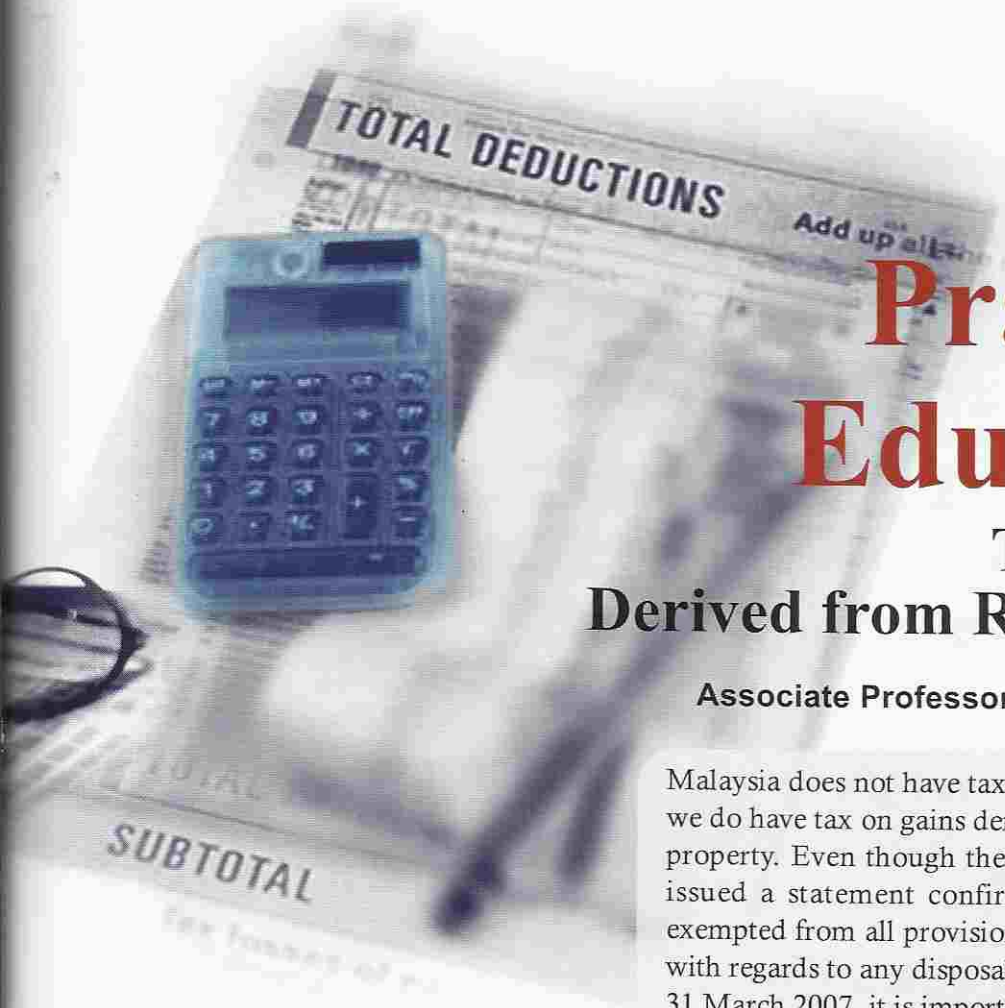
The need for compliance reviews

The modernization of the Customs department during the last few years has changed the fundamental relationship between Customs and importers. Importers are now more responsible for determining and reporting accurate classification and valuation information to Customs. This change has vast implications for importers as failure to comply in the current environment can disrupt their imports. Therefore, presently many companies realize the need for a compliance review to be conducted on their records especially in the area of valuation. A compliance review is basically a customs audit of an importer's internal controls to ensure compliance to the Customs act and regulations before the Customs auditors arrive. There are basically three phases in a compliance review. The first phase is a compliance assessment which is intended to evaluate the systems used by an importer in dealing with Customs. The second phase is a detailed audit of the importer's control systems intended to determine the extent of the importer's compliance and non-compliance. The third and final phase is a follow-up phase which is intended to rectify any of the importer's non-compliance issues and procedures as legally as possible. Usually the top management is informed of the results of the review together with the necessary recommendations.

A compliance review should be conducted by a competent Customs professional, preferably by a former senior officer of Customs with considerable experience in the Malaysian Customs Department, trained in various aspects of Customs audits and having knowledge of the various types of taxes and enforcement procedures. First hand experience in conducting Customs audits cannot substitute mere knowledge of Customs audit procedures as many areas can be seen only through the eyes of a Customs officer. Therefore, companies engaging the services of a Customs consultant to conduct a compliance review should verify the competency and experience of such person before entrusting him with such an important task. This will make a lot of difference in the outcome.

Author's Profile

Thomas Selva Doss *has served as a Senior Officer of Customs in the Royal Malaysian Customs Department for 13 years. He is trained in customs audits and investigations at the Malaysian Customs Academy. Currently he runs his own firm Dossnett Consulting Sdn. Bhd. providing customs advisory services to clients in Malaysia and Singapore. He can be contacted at 012-2309417 or e-mail customs@streamyx.com.*



Practical Education

Tax on Gains Derived from Real Property

Associate Professor Puan Faridah Ahmad

Malaysia does not have tax on capital gains, however we do have tax on gains derived from disposal of real property. Even though the Ministry of Finance has issued a statement confirming that any person is exempted from all provisions of the RPGT Act 1976 with regards to any disposal of chargeable assets after 31 March 2007, it is important for property owners to know the laws and regulations surrounding the real property owned and disposed by them.

Q1. What kind of assets are treated as real properties and what is meant by a chargeable asset.

Ans. *Real property is defined by Real Property Gains Tax Act 1976 as "any land situated in Malaysia and any interest, option or other right in or over such land".*

Land will include the following :

- *The surface of the earth and all substances forming the surface.*
- *The earth below the surface and substances therein (such as tin mining, gold mine).*
- *Any buildings or structures attached to land (such as factory, warehouse, house, school etc).*
- *Standing timber, crops and other vegetarian growing on land (such as padi field).*
- *Land covered by water (such as swimming pools and fish ponds).*

Chargeable assets are those real properties as mentioned above and also shares in real property companies.

Q2. Will there be any real property gains tax imposed on other capital assets such as motor vehicles, paintings and jewellery?

Ans. *Malaysian tax authorities have a limited regime of capital gains tax since only capital gains derived from the disposal of real properties or shares in real properly companies are subject to real property gains tax. Thus, capital gains from the disposal of other capital assets such as jewellery, paintings, motor vehicles are not taxable under RPGT.*

Q3. Who is chargeable to real property gains tax?

Ans. *Section 6 of RPGT Act 1976 provides that every person whether resident or non-resident in Malaysia is chargeable in respect of any chargeable gain that he has made on the disposal of a chargeable asset. The various persons include individuals, partnerships, companies, incapacitated persons, executors, trustees, a Hindu joint family, Rulers and Ruling Chiefs.*

Q4. How is a chargeable gain derived?

Ans. *Chargeable gain will arise when the disposal price is higher than the acquisition price.*

Example 1 :
Mr. Tan disposed of his factory on 21 May 2006 to Mr. Joseph for RM 560,000 in cash. The factory was purchased by him on 2 January 1997 at a cost of RM 270,000.

Disposal Price	RM 560,000
Acquisition Price	RM 270,000
Chargeable Gain	RM 290,000

Q5. How is real property gains tax computed?

Ans. *Real property gains tax is computed by multiplying the chargeable gain to a scale rates as prescribed by the Act. The rate applied will depend on the period of ownership*

of the chargeable asset. For resident individual, if the disposal took place within 2 years from acquisition date the rate is 30%, within 3 years (20%), within 4 years (15%), within 5 years (5%) and if disposal was made after 5 years, zero rate applies, thus no RPGT is payable.

Example 2 :
Ms Yeoh purchased a condominium situated in Damansara on 16 January 2003, at a cost of RM 420,000. After living there for about 4 years, she decided to move to another area in Subang Jaya and purchased a semidetached house from a developer at a cost of RM 650,000. As a result she sold the condominium to a friend at a market value of RM 710,000 on 31 October 2006. She would like to know how much RPGT that she has to pay as a result of the disposal.

Disposal Price	RM 710,000
Acquisition Price	RM 420,000
Chargeable Gain	RM 290,000
(-) Sch 4 Exemption RM 5000 or 10% of chargeable gain, take the higher	
(5000 or 10% x 290,000)	(29,000)
Chargeable Gain	RM 261,000

RPGT payable = RM 261,000 @ 15% (sold in 4th year after acquisition) = RM 39,150

Example 3 :

Using facts in example 2, let's say Ms Yeoh disposed the property on 13 February 2007, what will be the tax payable?

Chargeable gain after exemption is RM 261,000, and disposal took place in the 5th year.

∴ RPGT payable = 5% x 261,000 = RM 13,050.

Q6. What is Schedule 4 Exemption?

Ans. *Schedule 4 Exemption is given to an individual (resident or non resident) upon disposal of the real property. The amount exempt is calculated by taking the higher of RM 5000 or 10% of chargeable gain, on the particular asset.*

However this exemption will not be given where the chargeable asset is part of a bigger chargeable asset at the time of disposal.

Q7. Will there be a real property gains tax payable if the disposal price is lower than the acquisition price?

Ans. *If the disposal price is lower than the acquisition price, an allowable loss will arise, and there is no tax payable.*

Q8. It is possible to claim the allowable loss against the chargeable gain of another asset, if the owner disposed more than one chargeable assets.

Ans. *An allowable loss is allowed to be set off against the real property gains tax payable on another chargeable asset. However, the loss has to be converted to a tax relief for losses before any set off is given. The tax relief for losses is ascertained by multiplying the amount of an allowable loss by the same tax scale rate applicable to chargeable gain as prescribed by the Act.*

Example 4 :
Mr. Fauzi disposal the following properties in 2006.

Property A
It was disposed to Mr. Yap on 31 October 2006 at a price of RM 310,000. This property was purchased on 4 July 2002 at a cost of RM 390,000.

Property B
It was disposed to Miss Elisa on 24 November 2006 as a market value of RM 430,000 and it was purchased on 29 March 2004 at a cost of RM 240,000.

Mr. Fauzi would like to know whether he needs to pay any RPGT an both disposal.

Property A: Disposal Price	RM 310,000
Acquisition Price	RM390,000
Allowable Loss	80,000

∴Tax relief for losses= 80,000 x 5% = RM 400
∴RPGT payable is NIL

Property B: Disposal Price	RM430,000
Acquisition Price	RM240,000
Chargeable gain	190,000
(-) Exemption under Sch 4 [5000 or 10% x 190,000] ∴ the higher	(19,000)
Chargeable Gain	171,000
RPGT = 171,000 x 20% (3rd year)	= RM 34,200
Less : Tax relief for losses from Property A =	(400)
Real Property Gains Tax Payable	RM 33,800

Q9. How will an acquisition price is being determined in relation to buying a chargeable asset?.

Ans. *The acquisition price of an asset is the consideration paid to the seller (disposer) plus any incidental costs or expenses . Examples of the incidental costs are fees, commissions, remuneration paid for professional services of accountants, lawyers, surveyors, architects, costs of transfer including stamp duty and costs of advertising to find sellers.*

Example 5 :
Mr. Albert acquired a shophouse on 24 March 2004 for a consideration of RM 820,000. He also incurred other costs incidental to the acquisition such as legal fees RM 20,500, valuer's fees RM 1,200, advertisement fees to find a seller RM 1500 and stamp duty of RM 8,200. What will be Mr. Albert's acquisition price to the shophouse?

Consideration Paid		RM 820,000
(+) Incidental Costs :		
Legal fees	RM20,500	
Valuer's fees	RM 1,200	
Advertisement fees	RM 1,500	
Stamp fees	RM 8,200	RM 31,400
Acquisition price		RM 851,400

Q10. Is interest incurred on money borrowed to buy the asset is treated as part of acquisition price?

Ans. *If the asset is bought from a developer, the interest incurred from the date of signing the sale and purchase agreement until the property can be used by the buyer (such as when CF is obtained) is included as part of the acquisition price. Once the asset is fit to be used, any*

interest incurred can not be taken into account. However if this property is being let out, then it can be deducted from the rental income under income tax.

Q11. If there is any capital receipts derived by the owner of the asset, can they be claimed/deducted in determining the acquisition price?

Ans. Schedule 2 Para 4 has stated that, if the owner of the property has received any capital receipt such as compensation (for qny damages, injury, destruction, etc), payment under insurance policy for any damage etc and deposits forfeited by an intended buyer, these receipts must be deducted in arriving at the acquisition price.

Example 6 :

Using facts in example 5, let's say Mr. Albert received some money relating to the shophouse, as follows :

- Compensation from a neighbour who accidentally damaged the wall of the shophouse while doing a renovation to his property, amounting to RM 51,200.
- Insurance claim from insurance company due to the same damage, amounting to RM 32,900.
- A deposit forfeited from an intended buyer, Mr. Khoo, who called off the deal amounting to RM 75,000.

What is the acquisition price of the shop house for Mr. Albert?

Consideration Paid		RM 820,000
(+)Incidental Costs :		
Legal fees	RM20,500	
Valuer's fees	RM 1,200	
Advertisement fees	RM 1,500	
Stamp fees	RM 8,200	RM 31,400
Acquisition price		RM 851,400

(-) Incidental Costs :		
Insurance Claim	RM32,900	
Compensation	RM51,200	
Deposit forfeited	RM75,000	(RM159,000)
Acquisition price		RM 692,300

Q12. How will a disposal price being determined in relation to selling a real property?

Ans. A disposal price of an asset is the consideration received from the buyer less all incidental costs incurred in disposing the asset, expenses wholly and exclusively incurred in enhancing or preserving the value of the asset, expenses incurred in preserving or defending the asset's title after it is acquired. Such costs include legal fees, stamp duty, advertisement to find a buyer and professional fees (such as valuer and accountant).

Example 7 :

Puan Kaur sold her semidetached house which she bought four years ago for RM 732,000 to Mr. Singh on 31 October 2006. In the process of disposing the house, she incurred the following expenses :

- Stamp duty RM 1,732
- Advertisment to find a buyer RM 2,500
- Legal fees RM 8,200
- Valuer's fees RM 1,600

What will be Puan Kaur's disposal price after taking into account the expenses incurred by her:

Consideration Received		RM 732,000
Less: Incidental Costs :		
Stamp Duty	RM1732	
Advertising	RM2500	
Legal fees	RM8200	
Valuer's fees	RM1600	RM(14,032)
Disposal price		RM717,968

Q12. It a owner of the property did some extension or renovation to his property before disposing off, can he make some claim with regard to the costs incurred?

The capital expenditures incurred by the owner of the property can be considered as part of the costs incurred in determining the disposal price. These expenditures will be deducted from the consideration received by the seller (disposer).

Example 8 :

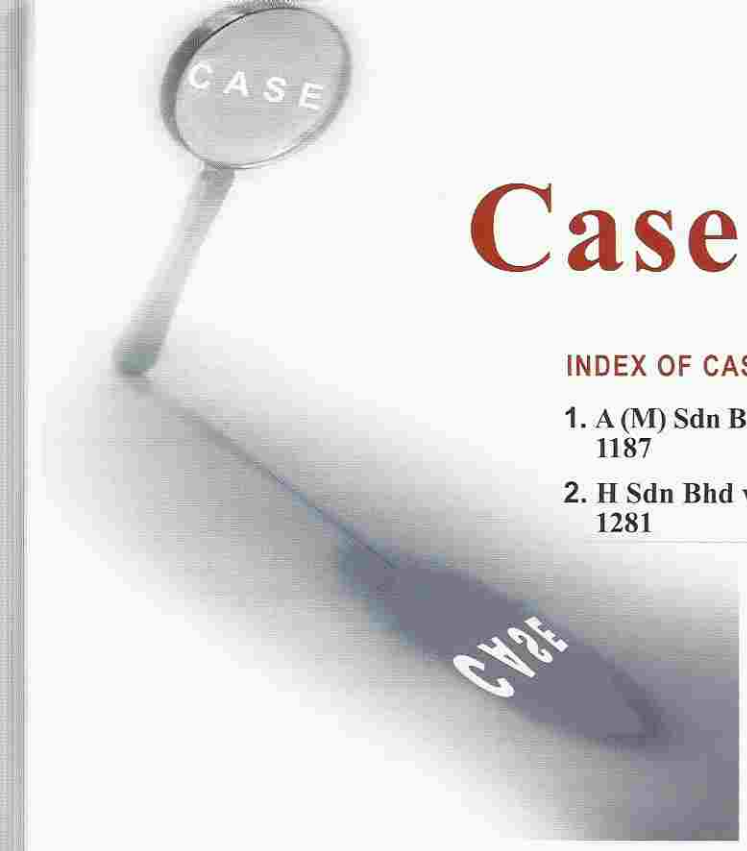
On 2 June 2006, Mr. Wong sold his bungalow which he bought three years ago for RM 970,000. In 2004, he did some renovation to the house which cost him RM 120,000. Incidental costs were also incurred such as stamp duty RM 4,800, advertisement to find buyer RM 1300 and valuation fees of RM 2,100. What is the disposal price to Mr. Wong.

Consideration Received		
Less: Permitted expenses:		RM970,000
Renovation		(RM120,000)
Less: Incidental cost:		
Stamp duty	RM4,800	
Advertisement	RM1,300	
Valuation fees	RM2,100	(RM 8,200)
Disposal Price		RM841,000

Author's Profile

*A academician of repute, **Puan Faridah Ahmad** is an Associate Professor at the Faculty of Accountancy, UiTM specialising in Malaysian Taxation. She has also taught the various levels of professional courses of ACCA, MICPA and ICSA.*

She is a Fellow Member of the Chartered Certified Accountants (FCCA, UK), a Fellow of the Malaysian Institute of Taxation (FTII) and a Chartered Accountant of the Malaysian Institute of Accountants (CA). She also holds a diploma in Accountancy (DIA) from the University Teknologi MARA (UiTM). Besides teaching, she is involved in providing consulting services for taxation and cash flow management to small and medium enterprises (SME) and has also conducted various workshops and seminars organised jointly by ACCA Malaysia, SMEDEC, JELITA and FELDA.



Case Summaries

Ms Audrey Quay

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A (M) Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri [2006] AMTC 1187

The principal activities of the appellant consist of steel and aluminium fabrication and trading in building materials, electrical and electronic products. In 2000, the appellant had several banking facilities for its trade and business purposes. On February 20, 2002 the respondent treated the fixed deposits of RM936,580 placed by the appellant as security for banking facilities as an investment, and assessed the interest of RM46,757 earned from the fixed deposits as an investment income under s 4(c) of the Income Tax Act 1967. The appellant appealed against that assessment.

The appellant submitted that the fixed deposits were placed as security for its banking facilities and for the purpose of producing gross income from the appellant's business. It was argued that the placements of the fixed deposits and the banking facilities obtained were closely connected with its business operation and could not be described as investments. Further, it was contended that the interest income of RM46,757 should be assessed as business income under s 4(a) of the Act, and therefore the interest restriction applicable under s 33(2) of the Act would not apply to the said interest income.

The respondent contended that the interest income received by the appellant was derived from investment and was therefore chargeable under s 4(c) of the Act. It was maintained that since the placing of the fixed deposit was described as an investment, the income therefrom would be restricted under s 33(2) of the Act.

The issues were –

(1) Whether the respondent is correct in assessing the interest earned from the fixed deposits placed by the appellant under s 4(c) of the Act or whether the said interest from the fixed deposits should be assessed under s 4(a) of the Act.

(2) Whether the respondent is correct in treating the fixed deposits placed by the appellant as investments otherwise than for the purpose of producing gross income from the business, and taking into account the same when calculating interest restriction applicable under s 33(2) of the Act.

Held, dismissing the appeal:

Since there was no evidence to show that the appellant's business involved any financial activities or dealing with money, the interest from the fixed deposits cannot be treated as business income under s 4(a) of the Act. There was also insufficient evidence to support the appellant's contention that the placing of the fixed deposits was ancillary to the appellant's business activity and formed part of the whole of the appellant's business operation. Unlike *Isyoda (M) Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* (2005) MSTC 3609, there was no evidence to show that the failure to place a fixed deposit will prejudice the appellant from being awarded any projects. Therefore the income derived from the placing of the fixed deposits is an investment income which ought to be assessed under s 4(c) of the Act. Since the fixed deposit is an investment, the interest restriction as prescribed under s 33(2) of the Act is applicable.

H Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri [2006] AMTC 1281

The appellant, H S Sdn Bhd, was an investment holding company. The controlling shareholder and governing director of the appellant company was Dr. S. In 1996, the appellant, who had never undertaken any prior activity of trading in shares, acquired shares in another company (NKB) as a long term investment. The appellant had not organised itself in terms of employees and resources in such a way as to indicate that it intended to carry out share trading activities. On June 9, 1997 NKB was listed on the stock exchange. On June 26, 1997 the appellant entered into an agreement for the sale of its shares in NKB. This sale was triggered by deterioration in the economy and fears that further deterioration may result in total loss. When the appellant entered into a members voluntary liquidation in 1999, Dr. S was appointed as the liquidator. The respondent raised two notices of assessment for the years of assessment 1998 and 1999 and assessed the appellant twiceon the same disposal of the shares in NKB. The appellant appealed against those assessments.

It was the appellant's contention that the acquisition of shares in NKB was an isolated investment in shares and that the shares were not acquired as part of the trade.

The respondent contended that the appellant's object clause indicated that the appellant intended to purchase the shares for trading. In support of this the respondent relied on the fact that the appellant, with a paid-up capital of RM100, had no financial ability to acquire the shares for a long term investment. The appellant sold its shares immediately after the shares were listed on the second board in the KLSE, evidencing that the appellant had an intention to resell at a profit.

The issue was whether the proceeds on the disposal of the shares in NKB constitute capital gains which are not taxable, or business income chargeable to income tax under s 4(a) of the Income Tax Act 1967.

Held, allowing the appeal:

The objects of the appellant as stated in the memorandum and articles of association state are not conclusive evidence of the fact that the appellant's principal activity was trading in shares. The intention of the appellant at the time when it purchased the shares in NKB is an important consideration. The appellant maintains that it purchased the shares in NKB as a long term investment. This is supported by the audited accounts of the appellant for the financial years 1997 and 1998 which describe the principal activity of the appellant as that of an investment holding company and classify the shares in NKB as an investment in the balance sheet. Trading requires an intention to trade and generally implies repetition and organisation but the appellant only had a single investment namely the shares in NKB throughout its corporate existence. Moreover, it did not have any other commercial characteristics that would suggest that it intended to trade in shares.

Although one single sale and purchase can constitute trading the other factors to indicate badges of trade need to be present. In the appellant's case, none of these conditions as laid out were present. As such, based on the available evidence and an analysis of the badges of trade, the appellant's investment in NKB cannot be said to be an adventure in the nature of trade.

Author's Profile

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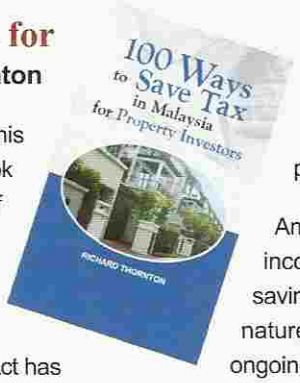
Book Review by

Mr Kalisewaran Sinniah
LLB(Hons) University of Wolverhampton, CLP

100 Ways to Save Tax in Malaysia for Property Investors by Mr Richard Thornton



Written by the same author, Mr. Richard Thornton, in his detailed and characteristically methodical style, this book provides a well rounded look at the tax implications of property investment.

Although the real property gains tax has been granted a blanket exemption as from 1 April 2007, this book still refers to it as one of the topics. After all the RPGT Act has not been repealed. Who is to say when RPGT may be revived?!

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Among the topics covered are rents and other incomes from real estate, tax deductions, tax saving ideas, IHC's, Adventure or concern in the nature of trade, REITS and the ever fresh and ongoing Stamp Duty issues.

This is a simple, inexpensive and easy to read book not to be missed by anyone with an interest in Property Income. To this reviewer, the book's simplicity simply adds to its usefulness.

Disclaimer

The views and opinions expressed herein are those of the reviewer personally and made in good faith. They are not necessarily views endorsed or expressed by MIT.

THOMSON
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100 Ways to Save Tax in Malaysia for Property Investors

by Richard Thornton

100 Ways to Save Tax in Malaysia for Property Investors is a comprehensive guide to the tax implications of property investment. As a work that collects together in one source all of the tax issues relevant to property investment, it is an invaluable tool to help investors in their vital decision-making processes. It is a companion work to **100 Ways to Save Tax in Malaysia for Individuals** and **100 Ways to Save Tax in Malaysia for Small Businesses** by the same acclaimed tax author. The book covers the specifics of the taxation of property income, which is in many ways distinct from the taxation of other kinds of income. The availability of deductions against rental income is discussed with clear examples. In addition to dealing with the taxation of property income, the book covers other areas of taxation including investment holding companies and real estate investment trusts which have relevance for the property investor. Tax-saving strategies which include tax deferment, tax reduction and elimination of tax liability are explored with practical illustrations.

Although real property gains tax is not to be imposed from April 1, 2007, it seems likely that the tax will not be repealed altogether and this tax is still discussed in the book. For the unwary investor who might otherwise stray over the line by dealing with properties in such a way that a profit on sale becomes liable to income tax, useful guidelines are provided. Stamp duty which is still in force and continues to be a significant cost for property investors is also covered by the book.

Whether you are a new property investor or an experienced one, a Malaysian or a foreign investor, this book contains a wealth of ideas to help you to minimise the taxes you have to pay and to plan your future actions so as to pay as little tax as possible. This book aims to make the understanding of tax issues affecting property investment easy by using simple everyday language and practical examples to illustrate them. It is certainly a book not to be missed by property investors, tax consultants, real estate consultants, landlords and anyone with an interest in property income.

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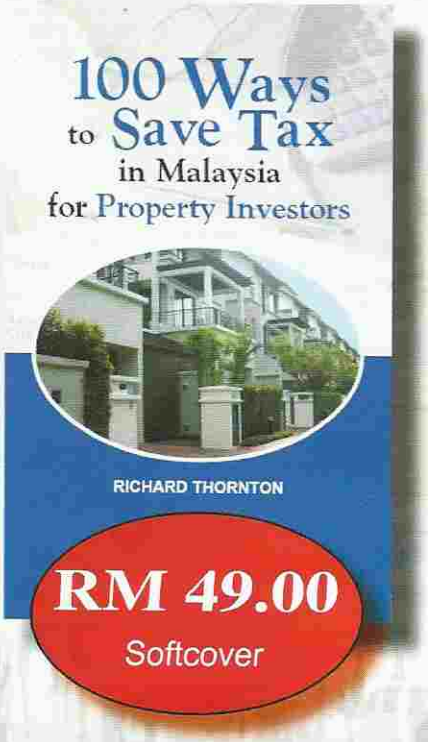

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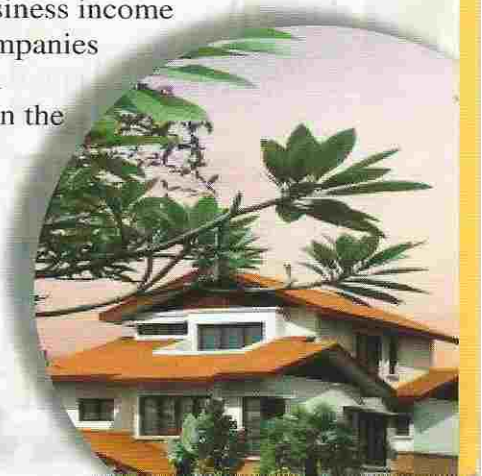
- REITs
- Stamp duty



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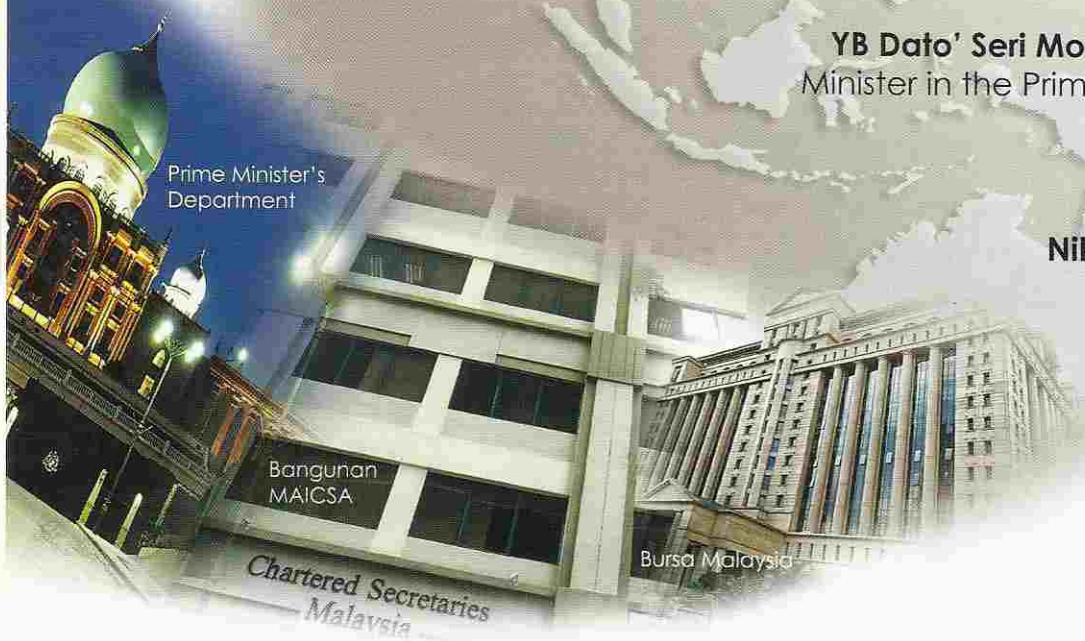

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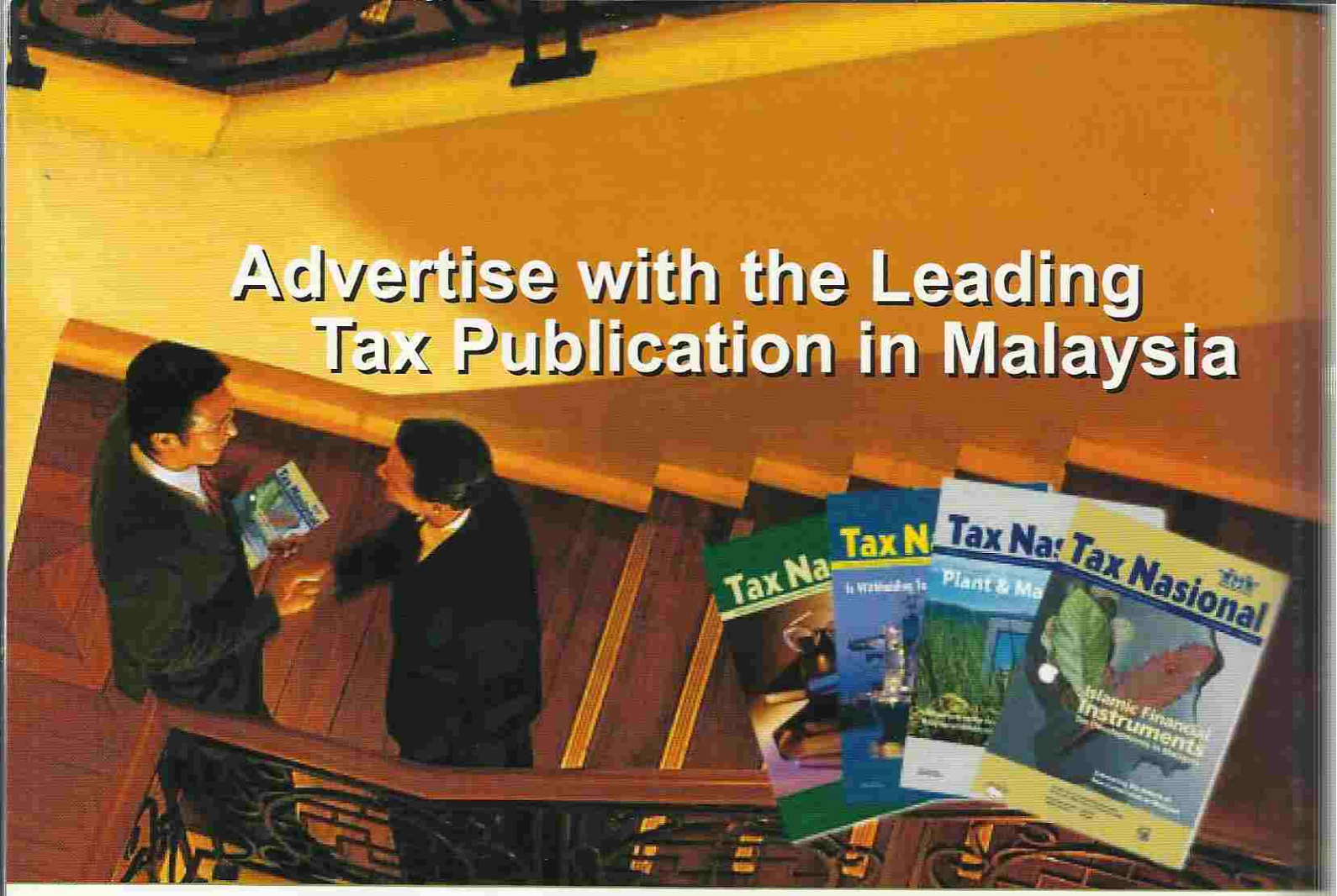

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