



CHARTERED TAX INSTITUTE OF MALAYSIA (225750 T)
(Institut Percukaian Malaysia)
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PROFESSIONAL EXAMINATION

FINAL LEVEL

REVENUE LAW

JUNE 2022

Student
Registration No.

Date

Desk No.

Examination Centre

Time allowed: 3 hours

INSTRUCTIONS TO CANDIDATES

1. This paper consists of **SIX** questions. **Candidates are ONLY REQUIRED TO ANSWER FIVE QUESTIONS.**
2. The income Tax Act 1967 (as amended) is referred to as ITA and the Real Property Gains Tax Act 1976 as RPGT.
3. Each answer should begin on a separate answer template.

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Question 1

- (a) It is generally accepted by the courts that there is no single, standard definition of the word 'income'; and for income tax purposes, it may be determined, according to the context in which the word is used. As the word 'income' can take multiplicity of forms, even the courts would not venture to define or codify it, much less, consider it wise to do so.

Required:

Discuss the concept of income in the context of 'gains or profits from a business for whatever period of time carried on' and 'rents' and the different tax treatment accorded to such income.

Note: Your discussion should make reference to the relevant provisions of the ITA, the salient features of the Public Ruling No. 12 of 2018 (Income from Letting of Real Property), as well as the facts, arguments and the decision of the *American Leaf Blending Co. Ltd. v Director General of Inland Revenue* [(1979) 1 MLJ 1] and the impact the different treatment of the income has on the tax liability.

(10 marks)

- (b) Mr Narendra Gupta ('Gupta'), an Indian citizen, is a postgraduate in marketing management, and a qualified aircraft engineer. He is the regional chief executive officer of an Indian company, The Bharat Aircraft Supplies Ltd. ('BAS') that supplies parts and components for various types of aircrafts operated in the South East Asian countries. BAS, incorporated in and operating from Chennai, India, is a subsidiary of the American Aviation Co. Inc., based in Seattle, United States of America.

BAS does not have an office in Malaysia but Gupta found Malaysia rather convenient and attractive and chose to operate from Kuala Lumpur from a rented office. He works on a work pass issued by the Malaysian Immigrations Department and uses the address of the rented office as his official correspondence in Malaysia. His job requires him to travel to the various South East Asian countries under his charge, meeting the aircraft operators, arrange for supplies, and provide technical and management support in respect of the utilisation of these aircraft parts and components. Gupta's job requirements in each of the different territories are qualitatively different and specific to the problems facing each of the aircraft operators in those territories. These works performed in the various territories have no nexus to the duties he performed in Malaysia.

During the three (3) years i.e., 2019 - 2021, that he was in Malaysia, his duties included compiling and preparing various detailed reports on the supply and sale of the aircraft parts including reports on the dynamics of the aviation industry in the region to assist marketing and planning. The reports are sent to BAS monthly. The reports are to be prepared in the country where the parts are supplied but sometimes, owing to work overload and time pressure he will bring the work to Kuala Lumpur, complete it and submit it to BAS.

Gupta has a daughter studying in New Zealand. He used two of the paid leave of three (3) weeks each in the years 2020 and 2021 in New Zealand, to be with his daughter. Gupta is entitled to three (3) weeks fully paid leave under his contract of employment with BAS, signed in Chennai, and he can choose to spend it wherever he wishes.

In filing his tax returns for the years of assessment 2019 to 2021, Mr Gupta did not report the income from work performed outside Malaysia. However, when the notices of assessment for those years were issued to Gupta, he was surprised to note that the Inland Revenue Board [IRB] has included the income for the whole period both *in* Malaysia *and* outside Malaysia as income derived from an employment in Malaysia.

Gupta is very much puzzled and has approached you for some clarification.

Required:

- (i) What do you think are the possible reasons Mr Narendra Gupta completed his Malaysian income tax return by not including the income from his employment for the period he was outside Malaysia?**
- (ii) Explain to Mr Narendra Gupta the possible basis for the Malaysian Inland Revenue Board to have assessed his income, from the exercise of his employment both in Malaysia and outside Malaysia for the years of assessment 2019 - 2021.**

Note: You are required to make reference to the relevant provisions of the ITA and applicable case law or laws (stating briefly the facts, arguments and decisions in those case or cases) in your discussion and explanation. You should disregard any provisions of the double tax agreements between Malaysia and the relevant countries, if any.

(10 marks)

[Total: 20 marks]

Question 2

- (a) Mohan & Tan Construction Sdn Bhd ('the Company') is a Malaysian incorporated resident company carrying on business as highway infrastructure contractors.**

The Company is heavily dependent on bank facilities (e.g., overdraft, short term credits and bank guarantees), for the smooth financing of its business. To provide these facilities, particularly the bank guarantees, the bank requires the Company to place specified sums of money with the bank in fixed deposits on stated terms, as collateral. The Company complies with these requirements and keeps large amount of cash in fixed deposits with the bank.

Failure to obtain a guarantee from a bank will seriously affect the chances of the Company being awarded any construction project, and successfully carrying on its business.

The sources of funds for these deposits are made up of cash from advance payments made by developers, construction companies and other traders as well as cash from deferred payments – essentially, the monies are internally generated and 'rolled' over (i.e., meticulously managed in relation to receipts and payments, while maintaining financial credibility, for which the Company has a special department to handle this).

The monies placed in fixed deposits with the bank earn an average interest of 2% per annum. The interest charged by the bank on the financial facilities it provides to the Company, on the other hand, ranges from 8% to 12% per annum.

For the years of assessment 2019, 2020 and 2021 the balance of the fixed deposits in the relevant basis year for the year of assessment, the interest earned from the deposits, and the total interest expenses incurred in the production of gross income from business were as follows:

Year of assessment	Balance of fixed deposits as at 31 December for the basis year for the year of assessment (RM)	Fixed deposit interest earned (RM)	Interest expenses incurred (RM)
2019	10,000,000	200,000	1,224,000
2020	24,000,000	480,000	2,939,000
2021	16,000,000	320,000	1,959,000
Total	50,000,000	1,000,000	6,122,000

The company's accounts are closed to 31 December each year.

Required:

- (i) Based on the decision of the Special Commissioners in the case of *I (M) Sdn Bhd v KPHDN* [(2005) MSTC 3609], what would have been the income tax treatment in respect of the fixed deposit interest earned by Mohan & Tan Sdn Bhd for the years of assessment 2019, 2020 and 2021, highlighting the key elements in the treatment.

Note: You are required to state briefly the facts, arguments and the decision in the case of *I (M) Sdn Bhd v KPHDN* [(2005) MSTC 3609 (also known as the 'Isyoda' case)].

(7 marks)

- (ii) How would the Director General of Inland Revenue treat the interest income from the fixed deposit, and the interest expenses incurred in the production of gross income from the business, following the amendments to the ITA from the year of assessment 2013 onwards, particularly with reference to sections 4B and 24(5).

(3 marks)

- (b) In the case of *Constantinesco v Rex* [11 TC 730] the House of Lords held that the payments made to the taxpayer, Mr Constantinesco by the British government in respect of the use of his patent during World War I was royalty, properly chargeable to income tax, and not a capital sum not liable to income tax.

Required:

Briefly discuss the facts, and the arguments of the Revenue authorities, and that of the taxpayer, in the case of *Constantinesco v Rex* [11 TC 730] and the grounds of the decision by the House of Lords. Further, discuss the taxability of 'royalty' income under the provisions of the Malaysian ITA.

(10 marks)

[Total: 20 marks]

Question 3

(a)

'... there is a clear distinction between the carrying on of a lawful business in the course of which acts prohibited by statute may, or may not, be committed, and the setting up of an enterprise every act and step of which is a criminal offence.'

Per Murnaghan, J
C. Hayes v R. J. Duggan [(1927) AC 193]

Required:

Discuss the above *dicta* in the context of the taxation of income with reference to sections 3 and 4 of the ITA 1967 and the case of *C. Hayes v R. J. Duggan* [(1927) AC 193].

Note: You are required to state briefly, the facts, arguments and the decision in the case of *C. Hayes v R. J. Duggan* [(1927) AC 193] in your discussion.

(10 marks)

(b) Mr Ah Long was laid off in 2020 when his employer closed down his business owing to the Covid-19 epidemic. Unable to find a job, he decided to go into a business venture.

He imported from Taiwan a few used units of 'fruits' or 'diddler' gaming machines. These are automatic coin-operated machines with revolving drums bearing representation of various kind of fruits. When a coin is inserted and a lever is pulled to activate the drums in the machine, the combination of fruits appearing when the drums come to a stop will determine whether the patron loses the coin he inserted or is lucky to win between two (2) to twenty (20) coins. While the combinations that give a winning position are entirely a matter of chance, the odds are usually not in the player's favour – and therein the possibility of gains to be made by the owner of the machine.

The paper works and the legal requirements for a license to start a business using the gaming machine was exceedingly tedious. Mr Ah Long was put off by this, and he decided to go ahead without the license. He contacted various pubs, clubs and massage parlour operators in Kuala Lumpur and made arrangements to place these machines in a discrete corner, at their business premises. The premise owner and Mr Ah Long will share the takings from the machine in the ratio of 30:70. Mr Ah Long made substantial gains from these machines, and he imported more machines, this time from the United States and placed it in several locations in the country, in the later part of the year 2021.

In filing his tax returns for the year of assessment 2021, he did not report the gains from the operation of these machines because he figured that since their operation is illegal the income too is illegal, and should not be taxable. He also did not want to alert the authorities in any way on his illegal operations by declaring the income in his tax returns.

Required:

With reference to the ITA and the relevant case laws, discuss the taxability of the income from the gaming machines by Mr Ah Long, including the issue of the illegality of the operations on its assessability for income tax.

(10 marks)

[Total: 20 marks]

Question 4

Babyway Ltd ('BL') is a company incorporated in United Kingdom. BL manufactures baby products such as milk bottles, pacifiers, napkins and wet wipes. All the manufacturing activities are carried out in the United Kingdom. In order to expand its business globally, BL incorporated a subsidiary, Babyway Sdn Bhd ('BSB') in Malaysia in 2019 to carry out the sale of its baby products in Malaysia.

In 2019, BSB's Board of Directors comprised of four (4) British nationals. Mr Johan, a Malaysian citizen and resident was employed by BSB as a general manager to assist in the day to day management of the business in Malaysia. However, he was not involved in any of the major decision makings while he was a manager. All major decisions of BSB were made by the Board of Directors during their meetings held in London. The accounts are closed to 30 April each year.

In May 2020, Mr Johan was appointed to join the board of directors of BSB. All of the board of directors' meetings were still held in London, except for one which was held on 20 November 2020 in BSB's office in Kuala Lumpur where a number of important strategic business decisions were made.

BL is BSB's parent company. As BL's business operations are in London, shareholders' meetings of BSB are typically held in London. Due to unsatisfactory performance of Mr Johan recently, BL intends to exercise its voting powers to remove Mr Johan as a director from the board of directors during the next shareholders' meeting.

At the same time, the directors of BSB wanted to minimise BSB's tax liability in Malaysia. They decided to engage a top tax consultant firm in Malaysia to assist them in their tax planning and to reduce BSB's tax liability.

Required:

- (a) **Advise Babyway Sdn Bhd on its resident status in Malaysia in YAs 2019, 2020 and subsequent years, specifically elaborating on the following matters:**
- (i) **To identify the relevant provisions of the ITA on corporate residence status.** (2 marks)
 - (ii) **To identify and discuss the basis year for a year of assessment on corporate residence status.** (1 mark)
 - (iii) **To identify and discuss the key factor in determining corporate resident status in Malaysia.** (2 marks)
 - (iv) **To identify and discuss whether place of physical operations will affect a company's corporate resident status with reference to relevant case laws.** (2 marks)
 - (v) **To identify and discuss whether the place of residence of the directors will affect a company's corporate resident status, with reference to case laws.** (2 marks)
 - (vi) **To identify the resident status of Babyway Sdn Bhd in Malaysia in YA 2019, 2020 and subsequent years.** (3 marks)
 - (vii) **To discuss and elaborate on control by shareholders in the context of corporate resident status.** (2 marks)

(b) Advise Babyway Sdn Bhd on tax avoidance position in Malaysia, specifically elaborating on the following matters:

(i) Identify briefly the relevant anti-avoidance provisions of the ITA.

(1 mark)

(ii) Discuss the case of *IRC v Duke of Westminster* [1936] AC 1 and the tests and factors that should be considered in tax avoidance and planning with reference to relevant case laws.

(5 marks)

Note: Candidates are required to support their answers with reference to the relevant Public Rulings, case laws and provisions of the ITA.

[Total: 20 marks]

Question 5

(a) Kilimanjaro Tea Sdn Bhd ('the Company') is in the business of growing tea leaves in Sabah. In the year 2020, the Company transferred its tea plantation in Sabah to its wholly owned subsidiary ('the Subsidiary') and ceased its operations in Malaysia. The Subsidiary is a non-resident that does not carry on business in Malaysia. The Company claimed agriculture allowance and capital allowance on qualifying assets used in the business before the transfer. Subsequently, the Subsidiary leased the plantation to a third party which continued the business of growing tea leaves.

Required:

Discuss whether the provisions relating to disposals subject to control under the ITA would apply to Kilimanjaro Tea Sdn Bhd's transfer of the tea plantation to its subsidiary.

Note: Support your answer with reference to the relevant provisions of the ITA and related case laws.

(5 marks)

(b) Palmy Oil Sdn Bhd ('the Company') is in the business of growing, processing, refining and selling oil palm and their by-products. In the year 2020, the Company incurred capital expenditure on the construction of a building complex and other construction expenditures as in (i) to (iii) below:

(i) RM250,000.00 on Building A which was to be used for the cleaning, servicing and repairing of the Company's machines which are used to process palm oil.

(ii) RM300,000.00 on Building B where the oil palm fresh fruit bunches are received, graded, sorted, sterilised and separated from their stalks, before going through the next stage in the milling process.

(iii) RM50,000.00 on an internal road system linking up the various buildings in the complex, including Building A and B.

Required:

Discuss briefly whether the expenditures in (i) - (iii) incurred by Palmy Oil Sdn Bhd would qualify for industrial building allowance under the ITA.

Note: Support your answer with reference to the relevant provisions of the ITA and related case laws.

(9 marks)

(c) Maida Furniture Sdn Bhd ('the Company') is in the business of manufacturing household and office furniture since 1985. In 2020, the Company decided to expand its business by constructing a new factory next to its existing factory. The taxpayer incurred construction expenditures totalling RM750,000 as in (i) and (ii) below.

(i) RM500,000.00 on the production area of the new factory which resulted in an increase in the production capacity of the Company;

(ii) RM250,000.00 on the rest of the building consisting of a lobby area, meeting rooms, office space and staff lounge.

Required:

Discuss briefly whether the expenditures incurred by Maida Furniture Sdn Bhd would qualify for reinvestment allowance under Schedule 7A of the ITA in the relevant years of assessment.

Note: Support the answer with reference to the relevant provisions of the ITA and related case laws.

(6 marks)

[Total: 20 marks]

Question 6

- (a) i-Shares Sdn Bhd ('i-Shares') is an investment holding company and closes its financial accounts on 31 December each year. i-Shares submitted its income tax return form ('ITRF') for the year of assessment ('YA') 2011 on 30.6.2012. i-Shares disagreed with certain guidelines published by the Director General of Inland Revenue ('DGIR') in preparing its tax computation for the YA 2011. Sometime in 2021, a director of i-Shares approached you for advice on filing an appeal to the Special Commissioners of Income Tax.

Required:

Discuss whether i-Shares Sdn Bhd may file an appeal to the Special Commissioners of Income Tax and the timeline for doing so.

(4 marks)

- (b) Floorworks Sdn Bhd ('Floorworks') is in the business of manufacturing tiles and closes its financial accounts on 31 December each year. Floorworks did not furnish its ITRF for the year of assessment ('YA') 2019. A best judgment assessment was made by the DGIR. A civil action was pursued to recover the amount of income tax payable for YA 2019. In an application for summary judgment against Floorworks, the DGIR claimed that the relevant notice of assessment had been posted to the last known address of Floorworks. Floorworks has denied receiving the notice of assessment. There was no evidence adduced by the DGIR that the said notice of assessment was actually posted.

Required:

With reference to the ITA and relevant case laws, advise Floorworks Sdn Bhd on the following:

- (i) **Its potential liability for failing to submit the ITRF for YA 2019; and**

(6 marks)

- (ii) **Whether there is any basis for challenging the service of the assessment as claimed by the DGIR.**

(6 marks)

- (c) New Valley Sdn Bhd ('New Valley') commenced business on 1.1.2015 and closes its financial accounts on 31 December each year. New Valley submitted its ITRF for the YA 2016 on 30.6.2017. Subsequently, New Valley realised that the ITRF for YA 2016 was submitted without claiming a deduction of business expenses incurred in 2015.

In January 2022, New Valley approached you for advice on claiming the deduction of business expenses which it incurred in 2015.

Required:

With reference to the ITA and relevant case laws, advise New Valley Sdn Bhd on whether it may claim the deduction of business expenses which it incurred in 2015 and the procedure for doing so.

(4 marks)

[Total: 20 marks]

(END OF QUESTION PAPER)