

LHAG Insights



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TRSB v KPHDN: High Court's Grounds of Judgment

The High Court has recently issued its grounds of judgment for TRSB v KPHDN (see our previous alert titled TRSB v KPHDN: Duty to Give Reason for Imposition of Penalty under Income Tax Act 1967 [here](#)).

To recap, in this case, the taxpayer overpaid its taxes because it had filed its tax returns based on its management accounts, as its audited accounts were not finalised at the time of filing. Despite having overpaid its taxes, the Director General of Inland Revenue (“**DGIR**”) penalised the taxpayer under subsection 112(3) of the Income Tax Act 1967 (“**ITA**”), for not filing its tax returns based on its audited accounts. The Special Commissioners of Income Tax (“**SCIT**”) dismissed the taxpayer’s appeal. Subsequently, the High Court reversed the SCIT’s decision and set aside the penalties imposed on the taxpayer.

The High Court gave several reasons for its decision. Some of these reasons were specifically related to the now-amended legislation. However, some of the reasons were of general importance and have a profound impact on the approach that should be taken for imposition of penalties. Whilst the decision is related to section 112 ITA, the Court’s reasoning should equally apply to penalties imposed under section 113 of the ITA:

- (a) For subsection 112(3) of the ITA to apply, it must be established that a criminal offence has been committed under subsection 112(1). A civil penalty can only be imposed under subsection 112(3) where no prosecution is brought for the offence under subsection 112(1). As criminal legislation, subsection 112 should be strictly construed in favour of the taxpayer;
- (b) The Revenue argued, amongst others, that it was entitled to impose the penalties because the taxpayer in this case had failed to comply with the *Nota Iringan* and *Peringatan* in the tax return form (Form C). However, the DGIR is not empowered to create a criminal offence under section 112(1) through the use of *Nota Iringan* and *Peringatan*. The *Nota Iringan* and *Peringatan*, being merely a guideline issued by the DGIR has no force of law. At best, it is just the DGIR's opinion of best practice; and
- (c) It may be that in some cases, the rationale for the imposition of a penalty is self-evident. However, in the instant case, the DGIR must justify imposing penalties in a case where the taxpayer had overpaid its taxes.

Significance of High Court's Decision

In this case, the Court sent a clear message that the DGIR cannot usurp the powers of the Parliament by creating new law through the issuing guidelines or practice notes, holding, amongst others, that:

- a. Penalty provisions such as section 112 [and by analogy section 113], which entail a criminal sanction, must be strictly interpreted and not extended beyond their plain meaning;



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- b. Failure to comply with the DGIR's guidelines cannot justify the imposition of penalties, which should only be imposed for non-compliance with the legislation; and
- c. The DGIR's discretion to impose penalties is not unfettered. In some cases, where the reason for imposing the penalty is unclear, the DGIR must explain and justify the exercise of his discretion.

The taxpayer was successfully represented in this appeal by Dato' Nitin Nadkarni and Ivy Ling Yieng Ping from the firm's Tax, Customs & Trade Practice. A copy of the High Court's Grounds of Judgment can be accessed [here](#).

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If you have any queries, please do not hesitate to contact Partners [Ivy Ling Yieng Ping](#) or [Dato' Nitin Nadkarni](#) at tax@lh-ag.com.