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IN THE HIGH COURT OF MALAYA AT KUALA LUMPUR
(APPELLATE AND SPECIAL POWERS DIVISION)

APPEAL NO: WA-14-3-02/2016

BETWEEN

KETUA PENGARAH HASIL DALAM NEGERI ...APPELLANT

AND

KUALITI ALAM SDN BHD ...RESPONDENT

JUDGMENT

INTRODUCTION

1. This is an appeal by the Director General of Inland Revenue against a decision of the Special Commissioners of Income Tax dated 8 October 2015 to allow an appeal by Kualiti Alam Sdn Bhd (the *taxpayer*) against assessments made by the Inland Revenue Board. The issue in this appeal centres around the question of whether certain capital investments made by the taxpayer was eligible for relief as reinvestment allowance pursuant to section 133A of, and Schedule 7A to, the Income Tax Act 1967.

2. For ease of reference, the office of the Director General of Inland Revenue is referred to in this judgment as the *Revenue*.

Background

3. The taxpayer is in the business of collecting, storage, treatment and disposal of scheduled waste. Scheduled waste in this context refers to material that has been prescribed pursuant to the Environment Quality Act 1974 by the Minister of Environment by way of regulation and includes diverse matters such as contaminated soil, discarded medicine, pathogenic wastes and spent lubricants from industrial machinery (among many others).

4. The taxpayer had made certain capital investments for the purposes of upgrading its plant and machinery in order to expand, modernise and automate its business. The precise details of those investments need not detain us for the purposes of this case, as they do not affect the outcome of the appeal, but a brief summary of the capital expenditure will facilitate easy understanding of the facts. The investments made by the taxpayer related to four broad categories:

(a) the incineration plant: here the taxpayer acquired machinery to break down bulk solid and hardened waste and machinery that ran on recycled oil rather than diesel;

(b) the physical/chemical treatment plant: here the taxpayer introduced a reaction chamber to treat chromate waste, in order to increase the overall efficiency of the physical/chemical treatment plant;

(c) laboratory equipment/instruments: the taxpayer acquired equipment that allowed it to more quickly conduct waste analysis and to expand its business into gas cylinder treatment; and

(d) leachate treatment plant: the water tanks at one of its leachate treatment plants were converted to allow the collection and treatment of storm water. Various equipment were also installed to improve the aeration capabilities of its leachate treatment plant.

5. The taxpayer claimed reinvestment allowance in respect of the plant and machinery in which it had made investments, for the years of assessment 2005 to 2007. The Revenue conducted a tax audit on the taxpayer and disallowed its reinvestment allowance claim.

6. In respect of YA2011, the taxpayer did not claim reinvestment allowance in respect of the mini-incinerators, additional landfill cells, laboratory equipment

and leachate treatment plant when filing its tax return, but had immediately thereafter made an appeal to the Special Commissioners.

7. The Revenue had rejected the reinvestment allowance claims as it viewed the taxpayer as not manufacturing or processing any product that has value to be sold, and therefore the investments had not been made in connection with a "qualifying project" within the meaning of paragraph 8 of Schedule 7A of the Income Tax Act 1967. The Revenue was also of the view that the income of the taxpayer was not derived from the sale of treated scheduled waste, but from the provision of waste treatment and disposal services.[1]

8. Dissatisfied with the assessments made by the Revenue, the taxpayer appealed to the Special Commissioners.

Decision of the Special Commissioners

9. The Special Commissioners of Income Tax allowed the taxpayer's appeal.

10. The crux of the issue before the Commissioners (and before this court) was whether the taxpayer's claim for reinvestment allowance came within the meaning of the expression "qualifying project". It was common ground that the taxpayer satisfied all other requirements for reinvestment allowance, which would have amounted to 60% of the amount of its investment.

11. The expression "qualifying project" is defined in paragraph 8 of Schedule 7A to the Income Tax Act 1967. The relevant subparagraph in this case is subparagraph (a), which prior to 2009 provided as follows:

> 8. In this Schedule, "qualifying project" means—
>
> (a) a project undertaken by a company, in expanding, modernising or automating its existing business in respect of manufacturing or processing of a product or

[1] See subparagraphs (xxix) to (xxxii) at page 30 of the Case Stated

any related product within the same industry or in diversifying its existing business into any related product within the same industry;

12. This provision applied in respect of the years of assessment 2005 to 2007.

13. Subsequently, paragraph 8(a) was amended in 2009 in the following manner:

> 8. In this Schedule, "qualifying project" means—
>
> (a) a project undertaken by a company, in expanding, modernising or automating its existing business in respect of manufacturing ~~or 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;

14. The words "or processing" was deleted from subparagraph (a), and the word "manufacturing", which was previously undefined, was now defined in the following manner:

> "manufacturing" means—
>
> (a) conversion by manual or mechanical means of organic or inorganic materials into a new product by changing the composition, nature or quality of such materials;
>
> (b) assembly of parts into a piece of machinery or products; or
>
> (c) mixing of materials by a chemical reaction process including biochemical process that changes the structure of a molecule by the breaking of the intra molecular bonds or by altering the spatial arrangement of atom in the molecule,
>
> but does not include—
>
> (aa) the installation of machinery or equipment for the purpose of construction;
>
> (bb) a simple packaging operations such as bottling, placing in boxes, bags and cases;
>
> (cc) a simple fixing;
>
> (dd) a simple mixing of any products;
>
> (ee) a simple assembly of parts;
>
> (ff) any activity to ensure the preservation of products in good condition during transportation and storage;
>
> (gg) any activity to facilitate shipment and transportation;
>
> (hh) any activity of packaging or presenting goods for sale; or

(ii) any activity that may be prescribed by the Minister, notwithstanding the above interpretation;

15. In allowing the taxpayer's appeal, the Commissioners found that:

(a) in connection with the taxpayer's claim for reinvestment allowance for the years of assessment 2005 to 2007, the treatment and eventual transformation of hazardous and toxic waste into inert waste amounted to "processing" within the meaning of paragraph 8(a) of Schedule 7A;

(b) in connection with the taxpayer's claim for reinvestment allowance for the year of assessment 2011, the business activities of the taxpayer fully came within the definition of "manufacturing" in the amended Schedule 7A; and

(c) most importantly, the processes applied by the taxpayer to the scheduled wastes resulted in a "product" for the purposes of paragraph 8(a) as would entitle it to claim the reinvestment allowance.

16. The relevant passages in the Case Stated dealing with these issues bear setting out in full. The terms "Appellant" and "Respondent" in the excerpt below refer to the taxpayer and the Revenue respectively.

> 10.26 According to the Appellant, they treated the scheduled waste where the hazardous and toxic waste will undergo various stages of processes in the Appellant's factory and the character of these scheduled waste is altered and at the end will be transformed into inert waste safe for disposal in landfill. This fact was not disputed by the Respondent. Having considered the testimonies of AW1 and AW2 on the stages involved in the treatment of the scheduled waste and referring to the Appellant's business operations as a whole, we agree with the Appellant that treatment of the scheduled waste involves 'processing' to alter the form and character of the waste to inert waste.
>
> 10.27 The Respondent took the position that there is no product or end product, added value, marketable or be sold and that the Appellant business activity is

merely treating and disposing scheduled waste that has been altered to inert waste.

10.28 As stated above 'product' is not defined in Schedule 7A nor did para 8(a) states that the product must have value, marketable or be sold. Therefore it is incorrect of Respondent to state that there is no added value to Appellant's activity and that the processes merely altering the physical of the scheduled waste and therefore not a qualifying project under Schedule 7A para 8(a).

10.29 If the inert waste is to be taken as the product, the Appellant stated they are not allowed to sell the inert waste as the license prohibits them to do so. Referring to the note stated under the item 'product' in the license – *Menjalankan aktiviti "hazardous and toxic waste collection, storage, treatment and disposal"*, we are of the opinion that the Appellant is licensed to manage the activity of hazardous and toxic waste collection, storage, treatment and disposal only and not to sell the inert waste or the end product.

10.30 Considering that the Appellant's business activity is treatment and altering of scheduled waste to inert waste and the principal purpose of the whole service or operation is to protect the environment and create safe and healthy clean environment for all and the future, there is no benchmark on what monetary value that can be attached to such intangible product i.e. safe, clean and healthy environment.

10.31 In conclusion, based on the above findings, we hold that the Appellant has discharged the onus under para 13 of the Fifth Schedule to the Act. Accordingly, in respect of the YA 2005, YA 2006 and YA 2007 to which the para 8(a) of Schedule 7A (pre-amendment) applies, we allow the Appellant's appeal for its entitlement to RA claims for the disputed items in this case.

10.32 Further, in respect of the YA 2011 to which para 8(a) of Schedule 7A (post amendment) applies, having regard to the Appellant's business activity as per its manufacturing license of transforming scheduled waste through physical and chemical processes into inert waste and relatively non-toxic, we find this squarely fulfill the definition of the term 'manufacturing' provided in the post amendment provision which read as follows –

"(a) conversion by manual or mechanical means of organic or inorganic materials into a new product by changing the size, shape, composition, nature or quality of such materials;"

In other words, the Appellant's business activity fully coincides with the definition of the word 'manufacturing' enacted for para 8(a) of Schedule 7A (post amendment) and therefore the Appellant has accordingly fulfilled the requirement of the term 'qualifying project' in respect of manufacturing a product. Accordingly we will also allow the Appellant's RA claims for YA 2011.[2]

[2] see pages 49-51 of the Case Stated

17. The Revenue has now appealed against the decision of the Special Commissioners.

ANALYSIS AND DECISION

The applicable principles of statutory construction

18. It is well settled that statutes that impose any tax, duty levy or charge are to be read strictly, with any ambiguity to be construed in favour of a taxpayer. Thus for example in *Mangin v Inland Revenue Commissioner*[3], a decision of the Judicial Committee of the Privy Council on appeal from New Zealand, it was held that there were four applicable principles of construction of a taxing statute:

> First, the words are to be given their ordinary meaning. They are not to be given some other meaning simply because their object is to frustrate legitimate tax avoidance devices. As Turner J said in his (albeit dissenting) judgment in *Marx v Inland Revenue Comr* ([1970] NZLR 182 at 208), moral precepts are not applicable to the interpretation of revenue statutes.
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> Secondly,
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>> '... one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax. There is no presumption as to a tax. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used.'
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> (Per Rowlatt J in *Cape Brandy Syndicate v Inland Revenue Comrs* ([1921] 1 KB 64 at 71), approved by Viscount Simons LC in *Canadian Eagle Oil Co Ltd v Regem.*)
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> Thirdly, the object of the construction of a statute being to ascertain the will of the legislature, it may be presumed that neither injustice nor absurdity was intended. If therefore a literal interpretation would produce such a result, and the language admits of an interpretation which would avoid it, then such an interpretation may be adopted.
>
> Fourthly, the history of an enactment and the reasons which led to its being passed may be used as an aid to its construction.[4]

19. The strict precepts in *Mangin v Inland Revenue Commissioner* is tempered in Malaysia by virtue of section 17A of the Interpretation Acts 1948 and 1967,

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[3] [1971] AC 739

[4] per Donovan LJ

which requires a court to prefer a construction that would promote the purpose or object underlying the statute over one that does not. In the Federal Court decision of *Lembaga Pembangunan Industri Pembinaan Malaysia v Konsortium JGC Corporation & Ors*[5], Suriyadi FCJ observed that:

> The [general principles in *Mangin v Inland Revenue Commissioner*] of interpreting a tax imposing statute are still woven into the fabric of the principles of construction of taxing provisions despite the introduction of s. 17A of the Interpretation Acts 1948 and 1967. Section 17A of the latter Act enjoins a purposive reading to be undertaken when interpreting a statute; with such statutory backing, a literal and blinkered approach must now compete with the context and purpose of the Act as legislated by Parliament. With a litany of cases in abundance, it is now well established that taxing statutes like all other statutes must be given a purposive interpretation to fulfil the objective of the statute, unless the circumstances demand otherwise.

20. Gopal Sri Ram JCA (as his lordship then was) in the Federal Court decision of *Palm Oil Research and Development Board Malaysia v Premium Vegetable Oils Sdn Bhd*[6] explained the interaction between Lord Donovan's precepts in *Mangin v Inland Revenue Commissioner* and section 17A of the Interpretation Acts 1948 and 1967 in the following manner:

> In my respectful view, s. 17A of the Interpretation Acts 1948 and 1967 neatly fits into and is complementary with the third principle in the judgment of Lord Donovan. Hence, the governing principle is this. When construing a taxing or other statute, the sole function of the court is to discover the true intention of Parliament. In that process, the court is under a duty to adopt an approach that produces neither injustice nor absurdity: in other words, an approach that promotes the purpose or object underlying the particular statute albeit that such purpose or object is not expressly set out therein. Imposing a tax by means of subsidiary legislation on a person not identified in the parent Act produces an absurd and unjust result and therefore does promote its purpose or object.

21. The strictures of the foregoing rules of construction do not, however, apply where the provision to be construed is one that provides relief to the

[5] [2015] 9 CLJ 273
[6] [2004] 2 CLJ 265

taxpayer (rather than one that imposes upon the taxpayer a tax). In the English Court of Appeal case of *Littman v Barron*[7], Cohen LJ held that:

> [T]he principle that in case of ambiguity a taxing statute should be construed in favour of a taxpayer does not apply to a provision giving a taxpayer relief in certain cases from a section clearly imposing liability.

22. In my considered view, the rules of construction in *Mangin v Inland Revenue Commissioner* are to give effect to the principle that a taxing statute is to be construed in favour of a taxpayer. Hence, where the provision in question is one that provides relief, it would follow that, firstly, the court is not bound to construe any ambiguity in that provision in favour of the taxpayer and that secondly, the court is not constrained by Lord Donovan's four rules of construction. More specifically, the court would be permitted to examine the context of the legislation and to infer from it the true intent of the legislature.

23. In the present case, Schedule 7A of the Income Tax Act 1967 confers upon a taxpayer relief in the form of a reinvestment allowance. Hence where ambiguity exists as to the applicability or scope of the relief available, this court would be free to infer from the context of the legislation the true intent of parliament and to imply, where appropriate, requirements that would give effect to that intent.

24. For completeness, I would add that the Cohen LJ's principle in *Littman v Barron* does not mean that a provision giving relief must be construed *against* the taxpayer. Cases such as *OS(M) Sdn Bhd v Ketua Pengarah Dalam Negeri*[8] and *Opto Sensors Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri*[9] cite *Littman v Barron* as authority for this proposition. However, a close examination of *Littman v Barron* will reveal that the Court of Appeal did not go so far as to

[7] [1951] 2 All ER 393
[8] (2010) MSTC 10-005
[9] [2012] 1 MLJ 848

suggest that any ambiguity in a provision giving relief must be construed against the taxpayer. Of course, if a taxpayer appeals against a decision of the Special Commissioners of Income Tax, it would be for the taxpayer to satisfy the court that he or she comes within the scope of the relief or exemption. This was not the case in the present instance, as the Revenue is the appellant.

The availability of the reinvestment relief

25. The taxpayer's claim for its eligibility for reinvestment allowance turned on the issue of whether the capital investments undertaken by the taxpayer constituted a "qualifying project" within the meaning of Schedule 7A to the Income Tax Act 1967.

26. In my judgment, the capital improvements undertaken by the taxpayer was not done in relation to any "product" so as to allow the taxpayer to be able to claim reinvestment relief.

27. A deconstruction of paragraph 8(a) of Schedule 7A will reveal that there is envisaged three categories of qualifying projects:

(a) a project undertaken by a taxpayer in modernising or automating its existing business in respect of manufacturing or processing of a product;

(b) a project undertaken by a taxpayer in modernising or automating its existing business in respect of manufacturing or processing of a related product in the same industry. The expression "related product" must mean a product that is related to an existing product of the taxpayer; and

(c) a project undertaken by a taxpayer in diversifying its existing business into any related product in the same industry. Here, "related product" would have the same meaning as in paragraph (b), with the difference being that the investment here is not limited to only improvements made by modernising or automating an existing business. Thus, a new manufacturing process to produce a related product would be eligible as a "qualifying project".

28. In all cases, it is a prerequisite that the taxpayer either manufactures or processes a *product*.

29. In the hearing before the Special Commissioners, the business of the taxpayer was described in the following terms:

> The [taxpayer] processes scheduled waste whereby the [taxpayer] collects, tests, stores, treats and disposes scheduled waste. The [taxpayer] converts and scheduled waste into inert waste residue safe for final disposal at the secured landfill. In other words, the [taxpayer] processes the scheduled waste and changes the character of the waste from its hazardous and toxic state to relatively non-hazardous in nature for safe disposal at the secured landfill.[10]

30. The Commissioners accepted this explanation as a proved fact.

31. I am of the view that the taxpayer does not in fact manufacture or process any "product". Even though I accept that the business of the taxpayer involves "processing" (within the meaning of the pre-2009 provisions) and "manufacturing" (within the meaning of the post-2009 provisions), the activity undertaken by the taxpayer is essentially a *subtractive process*. The treatment plants operated by the taxpayer removes noxious and harmful substances from scheduled waste, producing output that may be safely discharged into the environment. The value of the activity undertaken by the taxpayer lies in the fact that potentially harmful substances have been *removed* from scheduled waste. In this sense, the activity undertaken by the taxpayer is to provide a *service*

[10] See page 10 of the Case Stated

rather than to manufacture or process any *product*. What remains at the end of this process cannot, in my view, constitute a *product* within the ordinary meaning of that word, in the context of its use in Schedule 7A.

32. I accept that the word *product* is wide enough to cover any thing that is produced by an action, operation or process. See for example, one of the meanings of "product" in the Shorter Oxford Dictionary:

> A thing produced by an action, operation, or natural process; a result, a consequence; *spec.* that which is produced commercially for sale.[11]

33. Despite this, the end result of the processing undertaken by the taxpayer in this case is not so much a *product* of its activities, but rather a *by-product*, a mere incidental end result.

34. By contrast, the word *product* used in paragraph 8(A) of Schedule 7A implies an *additive process*—where value is added to existing matter or substance, through the process undertaken by the taxpayer. That this is so can be seen from paragraph 8(a) itself, which refers to "any related product" within the same industry. Thus, the provision envisages a differentiation in value or utility between various "products". I cannot see that the filter cake that is the by-product of the taxpayer's physical/chemical treatment plant or the solid waste that is the by-product of the taxpayer's solidification plant or for that matter the exhaust gasses that are vented from the taxpayer's incineration plant provide any utility at all to the taxpayer's customers. The utility lies not in the by-product, but rather in the service provided by the taxpayer in disposing of the customers' scheduled wastes in accordance with the provisions of the Environmental Quality Act 1974 and its regulations.

[11] The New Shorter Oxford Dictionary, 4th edition (1993). It might also be observed that the dictionary meaning of the word "product" connotes something that has commercial value.

35. In addition, it may also be observed that the definition of "manufacturing" as introduced by the 2009 amendments, specifically excludes certain processes. Thus, where the process improvement involves, for example, simple packaging or assembly of a product, the investment into that process will not be eligible for reinvestment allowance (see the definition of manufacturing, reproduced at paragraph 14 *ante*). I surmise that the rationale for this exclusion is that there are certain processes that do not appreciably or significantly add value to the end-product, and hence improvements to such processes ought not be eligible for reinvestment allowance. If the legislature saw it fit to exclude certain process improvements from the definition of a qualifying project even where such process adds value to the product in question, it would follow that *a fortiori* processes that do not add value at all to the output should also be excluded.

36. In this connection, I would therefore agree with the submission of the counsel for the Revenue that it is therefore implied that the term "product" as used in the definition of "qualifying project" in Schedule 7A of the Income Tax Act 1967 connotes that the end-result of the activities, operations or processes must be something that has value and whose value may be realised by way of sale to customers.

37. Even though there is no express term in the legislation that requires a product to be something that is capable of being sold, this requirement exists by necessary implication, by reason of the construction of the provisions of Schedule 7A, as explained in the preceding paragraphs.

38. The finding of this court that the taxpayer does not manufacture or process any "product" within the meaning of the definition of "qualifying project" paragraph 8(a) of Schedule 7A to the Income Tax Act 1967 necessarily

means that the Revenue's appeal must be allowed. I would however like to reiterate that this court agrees with the Special Commissioners that:

(a) the business activities of the taxpayer would encompass "processing" within the meaning of the definition of "qualifying project" prior to the 2009 amendments to the Income Tax Act 1967; and

(b) the business activities of the taxpayer would encompass "manufacturing" for the purposes of the definition of "qualifying project" following the 2009 amendments.

39. I accordingly allow the Revenue's appeal with costs.

31 March 2017

Azizul Azmi Adnan
Judge
High Court of Malaya
Kuala Lumpur

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