

SECTION 33(1) INCOME TAX ACT 1967

SSB

v.

DIRECTOR GENERAL OF INLAND REVENUE

PKCP(R) 1035-1036/2017, PKCP(R) 693/2017,
PKCP(R) 12/2018, PKCP(R) 223/2018, PKCP(R) 50/2019,
PKCP(R) 90/2019 & MOF.PKCP.700-7/1/536



BY LEGAL DEPARTMENT



SPECIAL COMMISSIONERS OF INCOME TAX



PUAN NIK SERENE BINTI NIK HASHIM



09 FEBRUARY 2023

The Taxpayer's principal activity involves generation, transmission, distribution and sale of electricity. Pursuant to a license vested on the Taxpayer, the Taxpayer has rights to use, work or operate any

installations which among others grid power stations and system supply voltages. The Taxpayer claimed for deduction on the expenses for the years of assessment ("YA") 2011 and 2012 including the expenses for feasibility studies ("FS"). The Taxpayer explained the FS expenses relates to a hydropower project and according to the Director Circular Resolution No.15/2011, the expenditure for the FS is for exploring, identifying and developing new hydroelectric sites and dams. Dissatisfied with the DGIR's decision to disallow the FS expenses as deductible expenses, the Taxpayer appealed to the Special Commissioners of Income Tax ("SCIT").

The Taxpayer submits that the expenses incurred in respect of the FS were carried out wholly and exclusively in the production of the Taxpayer's business income. The phrase "*in the production of income*" provides for an evaluation of the closeness or remoteness between an expenditure incurred and the earning of income of the business. However, the test is not strict that only expenditure directly connected to the earning of income is allowed as a deduction. The Taxpayer avers that FS are not limited to hydro, but also includes gas or coal generation potential project to increase business as well as revenue opportunity. It is meant to also increase business opportunities through international investors and local investors. The FS conducted by the Taxpayer in its usual business practice or operations were to fulfill the continuing demand.

While, the DGIR asserts that the hydroelectric sites or dams are not the Taxpayer's stock-in-trade but are their physical assets. The FS expenses incurred by the Taxpayer are for the purpose of exploring and developing hydroelectric sites and dams which is capital in nature, therefore falling within the ambit of the exception in Section 39(1)(c) Income Tax Act 1967 ("ITA 1967"). The deductibility of the expenditure on the FS must not only fulfill the requirement of wholly and exclusively incurred in the production of gross income under Section 33(1) ITA 1967, but must also not be prohibited under Section 39 ITA 1967. As such, the expenses in relation to the FS claimed by the Taxpayer is not deductible by virtue of Section 39(1)(c) ITA 1967.

Further, the DGIR submits that based on the documentation evidence furnished by the Taxpayer including various agreements entered into between SE Berhad and relevant consultants, the FS expenses claimed by the Taxpayer were incurred by SE Berhad and not by the Taxpayer.

The Taxpayer's appeal (Appeal No. PKCP(R) 1035/2017 and PKCP(R) 1036/2017) was decided on 15.09.2022 where the SCIT agreed with the DGIR and ruled that the Taxpayer's claim related to FS expenses are for the purpose of exploring and developing hydroelectric sites and dams are capital in nature and therefore the appeal was dismissed. The Notification of Non-Chargeability to Tax dated 09.12.2016 for YA 2011 and the Notice of Additional Assessment dated 07.12.2016 for YA 2012 are conclusive and upheld.

This decision shall bind the Taxpayer's appeals for YA 2013 to YA 2020 (Appeal No. PKCP(R) 12/2018, PKCP(R) 50/2019, PKCP(R) 693/2017, PKCP(R) 223/2018, PKCP(R) 90/2019 and MOF.PKCP.700-7/1/536) on the issue of FS expenditure.

Editorial Note:

- *The Taxpayer has filed an appeal against the decision by the Special Commissioners of Income Tax.*