



 Kuching High Court

 September 13, 2019

 Tax Litigation Division,
Legal Department

INCOME HAS TO BE RECOGNISED FIRST BEFORE A BAD AND DOUBTFUL DEBT CAN BE CLAIMED FOR DEDUCTION

—— QCHB v. KETUA PENGARAH HASIL DALAM NEGERI

FACTS

CGM awarded a contract for site-clearing, earth filling and levelling works to QCHB ("the Appellant") on 15.10.1997 for a contract sum RM3.4million payable progressively within 6 months. On 18.10.1997, the Appellant subcontracted the works to CCD for a contract amount of RM3.2million and the completion date was fixed on 18.1.1998.

CCD submitted its claim of RM900,000 for the first interim payment to the Appellant for the work done. The Appellant paid CCD RM700,000. Subsequently, the Appellant submitted its payment claim to CGM in the amount of RM950,000 and CGM failed to pay the same which was claimed for year ended 31.1.1998 (Y/A 1999). The works were not completed on 18.1.1998 and were suspended and abandoned since then.

The Appellant reported the claim amount of RM950,000 under the Trade Debtors Account in the Balance Sheet as at 31.1.1998 for YA 1999. The amount of subcontractor's charge of RM900,000 incurred was also reported under the Trade Creditors Account for the balance of RM200,000 (RM900,000 less RM700,000 paid).

The Appellant recovered a total amount of RM341,268.75 from CGM by way of contra between year ended 31.1.1998 to 31.1.2000 through contra of accounts of the other related companies of CGM, leaving a balance of RM608,731.25 outstanding as 31.1.2003.

The Appellant made a provision for bad and doubtful debt in the Income and Expenditure Statement for year ended 31.1.2004 and claimed for tax deduction for the balance of trade debt of RM608,731.25 in YA 2004.

JUDGE

Y.A. Datuk Supang Lian

REVENUE COUNSELS

Ashrina Ramzan Ali
Kwan Huey Shin
Amir Syafiq Abdul Karim

Upon audit, it was found that in the basis year ended 31.1.1998 for YA 1999, both the value of works done at the amount of RM950,000 and the amount of RM900,000 incurred were not taken up and recognised as income and expense in the Income and Expenditure Statement for the year ended 31.1.1998 (YA 1999) and up to year ended 31.1.2004 (YA 2004). Thus, KPHDN disallowed the deduction of RM608,731.25 and imposed penalty under S.113(2) of the Income Tax Act 1967 ("ITA").

The Appellant appealed to the SCIT on the issues as follows:

- A) Whether the provision of bad and doubtful debt of RM608,731.00 arising from the contract of earth filling project is allowable for deduction under section 34(2) of the ITA 1967;
- B) Whether the imposition of penalty under section 113(2) of ITA 1967 is justified, bad and wrong in law?

The SCIT heard the appeal and dismissed the appeal on issue (A) being the deductibility of the provision of bad and doubtful debt and allowed the appeal on issue (B) being the penalty imposed.

The Appellant appealed to High Court on issue (A) and KPHDN cross-appealed on issue (B).

APPELLANT'S CONTENTIONS

The contract works has not been completed and there was no profit, thus the Appellant is not required to recognize the amount of RM950,000.00 as gross income for Y/A 1999.

The amount of RM950,000 was also reported under the Trade Debtors Account in the Balance Sheet for YA 1999 and the balance of the subcontractor's charge was also reported under the Trade Creditors Account.

Penalty should not be imposed because there is no intention to evade tax.

RESPONDENT'S CONTENTIONS

KPHDN contended that S.34 of the ITA reading together with S.24 of the ITA clearly spell out that in order for the Appellant to claim deduction for a debt under S.34(2) of the ITA, such debt has to be first included in the gross income the Appellant for the basis period for a year of assessment prior to the year of assessment to which the relevant period relates.

Strict interpretation has to be applied in construing the provisions and it is a mandatory requirement to be fulfilled that the amount claimed as provision for doubtful debt has to be treated as gross income in the relevant period when the debt owing to the Appellant arose in Y/A 1999. As the result of the failure to comply with S.34 of the ITA, the amount of RM608,731 does not fall under the definition of 'debt' and not eligible for deduction for provision of doubtful debt.

The Appellant had filed incorrect return and gave incorrect information when they claimed deduction for the sum of RM608,731. Therefore, the penalty was correctly imposed under S.113(2) of the ITA. The language used in S.34 and S.24 of the ITA is clear and there is no technical interpretation involved herein which negates the imposition of the penalty.

COURT'S DECISION

The High Court dismissed the Appellant's appeal and allowed KPHDN's cross appeal. The High Court decided that the Appellant had failed to comply with S.34 of the ITA and there is no issue of technical interpretation in this case.