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Court Of Appeal Rules Waiver Of Debt Is Not Income

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The Court of Appeal delivered a significant ruling on the tax treatment of intercompany loan waivers, determining that forgiven debts are not taxable where the borrower has not previously claimed a deduction for the liability. The decision in *Multi-Purpose Credit Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* [2025] CLJU 2453 is expected to have wide implications for group financing structures and balance-sheet clean ups across corporate Malaysia.

The unanimous judgment turns on the interpretation of Section 30(4) of the Income Tax Act 1967 (ITA), which stipulates that a released liability becomes taxable only where it was previously deducted in arriving at adjusted income. The Court held that the provision is a self-contained charging rule that displaces the general business-income provision in Section 4(a).

The taxpayer was successfully represented by S. Saravana Kumar, a partner with the firm's the Tax, SST & Customs practice together with associate, Tan Jia Hua.

A Dispute Triggered By Intercompany Loan Forgiveness

The taxpayer, whose core business comprised credit leasing, hire-purchase and general loan financing, had taken intercompany borrowings amounting to roughly RM 78 million. When the related companies subsequently waived the loans, the Inland Revenue Board (IRB) treated the forgiven sum as taxable income on the basis that the company had realised a business gain when relieved of its repayment obligations.

During a tax audit, the IRB issued additional assessments covering several years of assessment, arguing that the waiver conferred an economic benefit equivalent to income arising from business activities. The taxpayer's appeals before both the Special Commissioners of Income Tax (SCIT) and the High Court failed, leading the taxpayer to escalate the matter to the Court of Appeal.

At the heart of the dispute lay a statutory question: can a debt waiver that does not fall within Section 30(4) nonetheless be taxed under the broad, catch-all provision in Section 4(a), which charges "gains or profits from a business"?

The Revenue's Argument: An Economic Gain Squarely Within Section 4(a)

Before the Court of Appeal, the IRB advanced an expansive interpretation of Section 4(a). The IRB argued that because the taxpayer dealt in money as its stock in trade, the release of its intercompany obligations effectively increased its net assets. This, the IRB maintained, amounted to a trading gain, akin to acquiring stock for free, which should be taxed as business income.

The IRB emphasised that although Section 30(4) did not apply in this case, the provision was not intended to be exhaustive. Instead, it should operate alongside Section 4(a), catching only the narrower category of previously deducted liabilities, while leaving the broader economic gains to be captured under the general income rule.

To support its position, the IRB relied heavily on the decision in *FT Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* (2016) MSTC 10-057, where the SCIT found that a loan waiver formed part of taxable trading income.

The Taxpayer's Case: Waiver Of Debt Is Not Income

The taxpayer took the opposite view, grounding its position in first principles of income tax law. It argued that for a receipt to fall within Section 4(a), it must first constitute "income" i.e. something that comes in rather than a mere saving from expenditure. Authorities from the United Kingdom, Australia and Malaysia were cited, including *Tennant v Smith* [1891-94] All ER Rep Ext 1851, *Federal Commissioner of Taxation v Cooke and Sherden* (1980) 29 ALR 202, and *The British Mexican Petroleum Company Limited v Jackson (H.M. Inspector of Taxes) & Anor* 16 TC 570, each drawing a clear distinction between economic inflows and the extinguishment of a liability.

The taxpayer stressed that a waiver does not bring new value into existence; it simply removes an obligation. As such, it cannot be classified as income unless Parliament expressly deems it so. That express treatment, counsel argued, is contained exclusively in Section 30(4), which taxes a waiver only where it reverses a deduction under Sections 33(1) or 42 of the ITA.

Since the taxpayer had claimed no such deduction, there was no statutory mechanism through which the waiver could be taxed.

The taxpayer further submitted that *FT Sdn Bhd* is not good law, arguing that the case was decided *per incuriam* because the SCIT failed entirely to consider Section 30(4), despite its central relevance to debt waivers.

The Court of Appeal's Ruling: Section 30(4) Is A "Complete Code"

The Court of Appeal accepted the taxpayer's submission, delivering a ruling that reasserts statutory clarity in a previously unsettled area of tax law.

The court described Section 30(4) as a comprehensive and exclusive charging provision governing the taxability of released liabilities. To allow Section 4(a) to operate in parallel, it observed, would effectively negate the purpose of Section 30(4) and render the provision redundant. Such an interpretation would run counter to legislative intent and the principle that tax charges must be clearly imposed.

Notably, the court downplayed the longstanding focus on whether a liability is "capital" or "revenue" in nature, calling the distinction a "red herring" in the context of debt waivers. The decisive question, the court held, is whether a deduction was previously claimed- nothing more.

The panel also expressly disapproved the ruling *FT Sdn Bhd*, concluding it had been decided *per incuriam* because the SCIT did not consider Section 30(4). In any event, the court distinguished the earlier case on the facts, noting that the taxpayer in *FT Sdn Bhd* had claimed deductions for expenditure funded with the borrowed sums, an element absent in the present appeal.

With the appeal allowed, the additional assessments were set aside. As a matter originating from the SCIT, the Court of Appeal's decision is final.

Implications For Businesses

The ruling provides substantial reassurance to businesses engaged in restructurings, rationalisations and post-pandemic remediation of intercompany balances. It confirms that debt forgiveness with no prior deduction sits firmly outside the tax net, reducing uncertainty for taxpayers who had previously faced inconsistent administrative positions.

The judgment also narrows the circumstances in which the IRB may rely on the general trading-income provision in Section 4(a). By holding that Section 30(4) displaces Section 4(a) in relation to debt waivers, the court has significantly curtailed a line of argument the IRB had increasingly advanced during audits.

Companies may now revisit ongoing or historic write-off exercises with renewed confidence, particularly where group-level loans are written off to streamline capital structures. Tax risk assessments for mergers, acquisitions and refinancing exercises where inherited intercompany mismatches often arise may also be materially rebalanced.

More broadly, the ruling underscores the judiciary's willingness to enforce the limits of the tax statute rather than permit economic concepts of "gain" to expand the tax base beyond Parliament's express wording.

Conclusion

The Court of Appeal's judgment re-establishes legal certainty in the taxation of debt waivers. By affirming that Section 30(4) is the sole provision capable of bringing a released liability into charge and only where a prior deduction has been claimed, the court has put an end to years of interpretive ambiguity. For taxpayers, the decision provides both clarity and comfort: absent prior deductions, a debt waiver is not taxable.

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