

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

O N A P P E A L

FROM THE FEDERAL COURT OF MALAYSIA

(APPELLATE JURISDICTION) CIVIL APPEAL No. X50 OF 1973

B E T W E E N:

INTERNATIONAL INVESTMENT LIMITED

Appellants

- and -

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THE COMPTROLLER-GENERAL OF INLAND
REVENUE

Respondent

CASE FOR THE RESPONDENT

Record

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1. This is an appeal from the judgment of the Federal Court of Malaysia (Gill C.J., Raja Azlan Shah F.J., and Wan Suleiman F.J.) dismissing an appeal by the Appellant against the judgment of Ong F.J. dismissing an appeal by the Appellant by way of Case Stated from an Order of the Special Commissioners of Income Tax that in transferring its property known as The International Building, Penang, to Island Hotel & Properties (Malaysia) Limited in exchange for shares in the said Company, the Appellants were carrying on the business of trafficking in immovable property and that the profits obtained from the transfer of the property were profits from business assessable to income tax under Section 10(1)(a) of the Income Tax Ordinance 1947.

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2. The primary facts are not in dispute. The Appellants were incorporated in 1962 with the objects, inter alia, of trafficking and otherwise dealing in or turning to account buildings and

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immovable property of the description (Clause 3(i)); developing and turning to account any land acquired and carrying out works of building and construction thereon (Clause 3(ii)); and investing and holding shares, securities or investments or selling realising and dealing in the same and reinvesting the proceeds (Clause 3(xvi)). In 1962 and 1963 the Appellants purchased several pieces of land in Penang Road, Penang, which together formed a block (hereinafter referred to as "the property") for a total price of \$337,273.71. The Appellants entered into contracts to erect a six-storey building with a shopping arcade and hotel on the said land. The building was to be completed by the 30th October 1963 at a cost of \$585,000. In order to finance the purchase and building costs the Appellants obtained a bank overdraft of \$491,365.44 from Malayan Banking. P. 25 The ground, first and second floors were completed and were let to tenants. In June 1962 there were negotiations concerning the letting of the hotel rooms but these negotiations fell through. In 1963 a loan of \$400,000 was made by Tan Sim Hoc to the Appellants and a further loan of \$422,500 was made by Disco Limited. In October 1963 it was resolved to reconstruct the business and undertaking of the Appellants with the alleged view of expanding its business of investment in securities. The property was transferred to Island Hotels and Properties (Malaysia) Limited, on an undertaking to complete the building in exchange for 3,750,000 shares of \$1 each in the said Company. In December 1963 and January 1964 all these shares were transferred to Disco Limited and Tan Sim Hoc. Other than this building the Appellants have constructed no building of a similar nature. P. 26

3. Before any dispute arose between the parties a letter dated 27th April 1962 was sent to the Appellants' Company Secretary by the Inland Revenue Department asking him to specify the nature of the business conducted by the Company. The Company Secretary, a qualified Accountant, replied on behalf of the Appellants on 16th August 1962 stating that: "The nature of the business conducted by the Company is dealing in immovable property and land development." In the Appellants' account for the year 1962 the costs of the construction of the building were described as "work in progress" under "Current Assets". By Notice of Amended Assessment dated 25th May 1967 the Comptroller of Income Tax raised assessment P. 26

10 of income tax on the Appellant Company for the year of assessment 1964 and included in the income upon which this tax was assessed an amount of \$1,704,061 which the Comptroller alleged was the net profit after deduction of certain expenses derived by the Appellant Company from the transfer of The International Building erected on the property in exchange for the shares in Island Hotels & Properties (Malaysia) Limited, and which the Comptroller alleged was assessable to income tax as being income from business carried on by the Appellants. The Appellants appealed to the Special Commissioners against the inclusion of this amount in the assessment.

20 4. The issue which arises upon this Appeal is whether there was evidence upon which the Special Commissioners could find that the profit realised by the Appellants on the sale of the property was chargeable to income tax within the meaning of Section 10(1)(a) of the Income Tax Ordinance 1947 as being a gain or profit from a trade or business.

5. The statutory provisions which have been considered relevant in the Court below are as follows :

Income Tax Ordinance 1947

Section 10

30 (1) Income tax shall, subject to the provisions of this Ordinance, be payable at the rate or rates specified hereinafter for each year of assessment upon the income of any person accruing in, derived from or received in, the Union in respect of -

(a) gains or profits from any trade, business, profession or vocation, for whatever period of time such trade, business, profession or vocation may have been carried on or exercised;

Section 2

40 In this Ordinance unless the subject or context otherwise requires:-

...

"person" includes a company, ...

Companies Ordinance 1940 - 46

Section 125

(1) Every balance sheet of a company shall contain a summary of the authorised share capital and of the issued share capital of the company, its liabilities and its assets, together with such particulars as are necessary to disclose the general nature of the liabilities and the assets of the company and to distinguish between the amounts respectively of the fixed assets and of the floating assets, and shall state how the values of the fixed assets have been arrived at. 10

(2) There shall be stated under separate headings in the balance sheet, so far as they are not written off -

(a) the preliminary expenses of the company; and

(b) any expenses incurred in connection with any issue of share capital or debentures; and 20

(c) if it is shown as a separate item in or is otherwise ascertainable from the books of the company, or from any contract for the sale of purchase of any property to be acquired by the company, or from any documents in the possession of the company relating to the stamp duty payable in respect of any such contract or the conveyance of any such property, the amount of the goodwill and of any patents and trademarks as so shown or ascertained. 30

(3) Where any liability of the company is secured otherwise than by operation of law on any assets of the company, the balance sheet shall include a statement that that liability is so secured, but it shall not be necessary to specify in the balance sheet the assets on which the liability is secured. 40

(4) The provisions of this section are in addition to other provisions of this Ordinance requiring other matters to be stated in the balance sheets."

6. The Special Commissioners in their Grounds for Decision came to the following conclusions: p. 35
p. 52

(a) "We find that the facts in the Appellant Company's case point to the conclusion that the Appellant Company has carried on the business of buying and selling property and that the property in question has accrued to it from that business."

10 (b) "...We conclude that when the Appellant Company disposed of its land together with The International Building on it in exchange for the shares, it did so with this object of trafficking or dealing in or turning to account the property with a view to profit. Although there was only one such transaction it was a business transaction carried out with the intention of carrying on the business of dealing in property..."

20 On the question of whether the true intention of the Appellant Company was to expand its business of investments in securities as stated in the Resolution, the Special Commissioners concluded at page 26 :

30 "...We find it difficult to accept that the true object of acquiring those shares was in order to expand its investment. That the true object was not to expand to hold investment in shares is confirmed by the fact that all the \$175,000 shares in four other companies held by the Appellant Company in 1962 were transferred away by the end of 1963." p.53

The Special Commissioners further found:

40 "Hence we find that the Appellant Company was not only empowered by Clause 3(i) and (ii) of its Memorandum of Association to traffic and deal in lands, houses and buildings, but it had also the intention to traffic and deal in buildings which it did by the transfer of the land and buildings to Island Hotels & Properties (Malaysia) Limited in exchange for shares in that Company. In other words the Appellant Company was empowered by its Memorandum of Association to carry on the business of trafficking in lands and buildings,

it had that intention and it had carried out that intention. The classification of the construction costs as work in progress under current assets in the financial account seem to be consistent with the description by the Appellant Company's Secretary (a firm of Accountants holding professional qualification) in Exhibit R.17 of the nature of its business as dealing in immovable property and land development, and we are further urged by this consideration to come to that conclusion."

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By their deciding order dated 19th September 1968 the Special Commissioners found that in transferring the said property to the said Company in exchange for shares the Appellants were carrying on the business of trafficking in immovable property pursuant to its declared objects stated in Clause 3(i) of its Memorandum of Association and that the profits obtained from the transfer of the property were profits from business assessable to income tax; and ordered that the assessment of income tax in respect of the Appellant Company for the year of assessment 1964 as per Notice of Amended Assessment dated 25th May 1967 should be and was thereby confirmed.

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p. 60

7. Upon appeal by way of Case Stated to the High Court of Malaysia Ong F.J. held:

That, following Copper Syndicate v. Harris, 5 T.C. 159, the excess of the value of the shares over the cost of the property could be treated as a profit chargeable to tax in a proper case. The facts of the case justified the decision of the Special Commissioners. Although this was an isolated transaction the building operations involved were of a kind, and were carried on in the same way as those which characterised ordinary trading in the line of business in which the venture was made. Following Commissioner of Inland Revenue v. Livingston & Ors., 11 T.C. 358 and Commissioner of Inland Revenue v. Reinhold, 34 T.C. 389, the Learned Judge rejected the argument that the transaction was not business because it was isolated. He distinguished the case of E. v. Comptroller-General of Inland Revenue [1970] 2 M.L.J. 118, because it dealt with the case of an individual, not a company formed with the declared object of trafficking and dealing in land and buildings.

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8. Upon appeal by the Appellants to the Federal Court of Malaysia, Raja Axlan Shah F.J. delivering and Judgment of the Court held:

10 That the question to be decided was whether there was evidence capable of justifying the finding of the Special Commissioners that the facts revealed a realisation of income from the business of trafficking in immovable property carried on by the Appellants. The answer depended, in the final analysis, on all the surrounding circumstances. Following D.E.F. v. The Comptroller of Income Tax /1961/ M.L.J. 55 and The Commissioner of Inland Revenue v. The Korean Syndicate Limited, 12 T.C. 181, the case of E. v. Comptroller-General of Inland Revenue /1972/ M.L.J. 118 should be distinguished. There was a fundamental distinction between an individual and a limited company. The company had been formed to carry on business and the fact that a transaction was an isolated one did not prevent it from being business. Considering the stated objects of the Memorandum, the Company Secretary's letter, statements in the accounts, the fact that the Appellants were a limited company, the quick sale of the shares in Island Hotels & Properties (Malaysia) Limited, and the other facts found by the Special Commissioners "the overwhelming material of the evidence was consistent with 'carrying on business in immovable property' and the Special Commissioners could reasonably decide, and were entitled to decide, as they did." The Federal Court rejected the Appellants' argument that the ownership of the property never changed hands because the persons constituting the Appellant Company continued to hold it through Island Hotels & Properties (Malaysia) Limited. The quick transfer of the shares to two distinct legal persons "let the cat out of the bag". There was no admissible or sufficient evidence to suggest that the transferees held the shares on trust for the said Company. The Appellants' appeal was dismissed.

9. The Respondent first submits that the Appellants can only succeed in this appeal if they show that the only reasonable conclusion that can be reached on the evidence contradicts the decision of the Special Commissioners: (Edwards (HM Inspector of Taxes) v. Bairstow and Harrison /1956/ A.C. 14.) The Respondent further submits that there was overwhelming evidence to justify the conclusion

of the Special Commissioners:

- (a) The objects of the Company including trafficking and otherwise dealing in buildings and immovable property of any description and the development of land and property. These were not subsidiary object but the primary objects of the Appellants. The Special Commissioners were entitled to rely on this evidence. Scottish Investment Limited v. Forbes (Surveyor of Taxes) 3 T.C. 231. 10
- (b) The Appellants are a limited company and it is a proper presumption that a company is formed with the intention of carrying on business. Commissioner of Inland Revenue v. Eccentric Club, 12 T.C. 689.
- (c) The letter from the Appellants' Company Secretary is powerful evidence in that it was written by the responsible officer of the Company who was a qualified Accountant well before any dispute arose. 20
- (d) The accounts show that the Appellants have borrowed large sums of money to finance the purpose of the land and building operations. Rental income would have been insufficient to repay those borrowings. This is strong evidence that the Appellants must have intended to sell the property and not to retain it as capital.
- (e) The 1962 accounts describe the construction costs of the building as "work in progress" under "Current Assets". The accounts were audited by an independent auditor. By Section 125 of the Companies Ordinance 1940-1946 the Company was obliged to distinguish between its fixed assets and floating or current assets. The said statement was again made by the Appellants well before any dispute arose. 30
- (f) The building was sold before it was completed. 40
- (g) The shares received as consideration for such sale were themselves sold on within a short period.

The word "buisness" has a broad meaning. St. Aubyn

Estates Limited v. Strick, 17 T.C. 412, 419.
Commissioner of Inland Revenue v. The Korean
Syndicate Limited, 12 T.C. 181. In the
Respondent's submission the conclusion of the
Special Commissioners that the Appellants were
carrying on a business of trafficking in immovable
property was not merely amply supported by the
evidence but was irresistible.

10 10. The Respondent therefore submits that
the Order of the Federal Court of Malaysia
was right and should be affirmed for the following
among other

R E A S O N S

- (i) BECAUSE the only reasonable conclusion
to be drawn from the evidence is that the
Appellants were carrying on the business of
trafficking in immovable property.
- (ii) BECAUSE the profits realised from the sale
of the property were rightly held to be
taxable under Section 10(1) (a) of the
Income Tax Ordinance 1947.

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NICHOLAS LYELL

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