

Judicial Committee of the
IN THE PRIVY COUNCIL

20 OF 1976

ON APPEAL
FROM THE FEDERAL COURT OF MALAYSIA
(APPELLATE JURISDICTION)

B E T W E E N :

INTERNATIONAL INVESTMENT CO. LIMITED

Appellant

- and -

THE COMPTROLLER-GENERAL OF INLAND
REVENUE

Respondent

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CASE FOR THE APPELLANT

RECORD

1. This is an appeal from the judgment and order dated the 13th June 1975 of the Federal Court of Malaysia (Gill, C.J., Malaya, Raja Azlan Shah F.J., and Wan Sulaiman, F.J.) dismissing an appeal from the judgment and order dated the 15th March 1973 of the High Court of Malaya (H.S.Ong, J.) whereby an appeal by the Appellant Company by way of Case Stated from the determination of the Special Commissioners of Income Tax made on the 7th June 1969 was dismissed. pp. 94-110
pp. 55-64
pp. 1-7
pp. 29-35
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2. The question that arose before the Special Commissioners was whether, on the facts before them which are hereinafter summarised, the Appellant Company derived income from the carrying on of a "trade" or "business", within the meaning of those words in Section 10(1)(a) of the Income Tax Ordinance 1947 ("the 1947 Ordinance" included in the pocket at the end of this Case), so that any profit therefrom would be assessable to income tax. pp. 8-13
- 30 The Special Commissioners decided that question in favour of the Respondent and the question in the present appeal is whether that determination was erroneous in law. pp. 29-35
p. 7

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3. The charge to income tax for the relevant years of assessment is found in Section 10(1)(a) of the 1947 Ordinance and applies to:

"the income of any person ... in respect of 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".

The said charge is not as extensive as that applying for the purposes of the corresponding United Kingdom statutes where "trade" is and has always been defined so as to include "every trade, manufacture, adventure or concern in the nature of trade" (Income and Corporation Taxes Act 1970, Section 526(5) deriving from Income Tax Act 1842, Section 100). It has been held by the Court of Appeal in Singapore (in D.E.F. v. Comptroller of Income Tax /1961/27 MLJ 55, in pocket at end) that the words "trade" or "business" in the 1947 Ordinance do not extend to an adventure or concern in the nature of trade and that decision has been expressly approved by the Federal Court of Malaysia in E. v. Comptroller General of Inland Revenue /1970/2 MLJ 117 (in pocket at end). The law has been subsequently amended (but not so as to apply to the years of assessment with which this case is concerned) so as to extend the definition to adventures or concerns in the nature of trade.

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pp. 8-28

4. The relevant facts as found by the Commissioners are as follows:-

p. 8

(1) The Appellant Company was incorporated on 16th January 1962 with an authorised share capital of \$500,000 in shares of \$100 each which subsequently, in 1963, was increased to \$5m. The issued share capital initially was \$300,000 fully paid which, as at 31st December 1963, had increased to \$500,000 fully paid and application and allotment moneys of a further \$500,000 had been received by the Appellant Company for shares which had not been finally allotted.

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pp. 8-9

(2) During the course of 1962 and 1963 the Appellant Company acquired four lots of land

situate in one area at Penang Road, Penang. It paid a total sum of \$8,300 to ten persons occupying old houses on part of the land as compensation for moving out of the land.

- (3) The Appellant Company demolished the existing houses on the land and, commencing on 31st March 1962, entered into various building contracts for the erection of a building on the land subsequently to be known as the International Building and described as a six-storey shopping arcade and hotel building including a banking hall. Part of the construction costs was financed by bank loans. p. 9
- 10 (3) The Appellant Company demolished the existing houses on the land and, commencing on 31st March 1962, entered into various building contracts for the erection of a building on the land subsequently to be known as the International Building and described as a six-storey shopping arcade and hotel building including a banking hall. Part of the construction costs was financed by bank loans. p. 9
- (4) In about June 1962 negotiations for renting the then unbuilt hotel section of the building took place but proved abortive since no agreement was reached on the amount of rent to be paid. In 1963 the Appellant Company received \$7,044 as rents of the arcade. p.10
- 20 (5) In 1962 the Appellant Company acquired shares having a total nominal value of \$175,000 in four Malaysian companies. pp.11-12
- (6) On 16th October 1963 a special resolution was passed for the reconstruction of the Appellant Company by transferring the incomplete building (subject to an obligation to complete it) to Island Hotels and Properties (Malaysia) Limited (the "Island Company"). The consideration for the said transfer was the issue by the Island Company, credited as fully paid, of 3,750,000 shares of \$1 each of which 2,846,300 shares were attributed to the site and the building and 903,700 shares were attributed to the Appellant Company's obligation to complete the building. The said resolution referred to the Appellant Company's decision "to expand its business of investment in and the holdings of securities". The accounts of the Appellant Company for the years 1965 and 1966 show this objective was achieved since it expanded its business from holding land and \$175,000 shares in other Malaysian companies into \$3,750,000 shares in the Island Company. pp.10-11
- 30 (6) On 16th October 1963 a special resolution was passed for the reconstruction of the Appellant Company by transferring the incomplete building (subject to an obligation to complete it) to Island Hotels and Properties (Malaysia) Limited (the "Island Company"). The consideration for the said transfer was the issue by the Island Company, credited as fully paid, of 3,750,000 shares of \$1 each of which 2,846,300 shares were attributed to the site and the building and 903,700 shares were attributed to the Appellant Company's obligation to complete the building. The said resolution referred to the Appellant Company's decision "to expand its business of investment in and the holdings of securities". The accounts of the Appellant Company for the years 1965 and 1966 show this objective was achieved since it expanded its business from holding land and \$175,000 shares in other Malaysian companies into \$3,750,000 shares in the Island Company. pp.27-28
- 40 (6) On 16th October 1963 a special resolution was passed for the reconstruction of the Appellant Company by transferring the incomplete building (subject to an obligation to complete it) to Island Hotels and Properties (Malaysia) Limited (the "Island Company"). The consideration for the said transfer was the issue by the Island Company, credited as fully paid, of 3,750,000 shares of \$1 each of which 2,846,300 shares were attributed to the site and the building and 903,700 shares were attributed to the Appellant Company's obligation to complete the building. The said resolution referred to the Appellant Company's decision "to expand its business of investment in and the holdings of securities". The accounts of the Appellant Company for the years 1965 and 1966 show this objective was achieved since it expanded its business from holding land and \$175,000 shares in other Malaysian companies into \$3,750,000 shares in the Island Company. pp.27-28
- (7) The Appellant Company subsequently transferred for no consideration all its shares in the p. 11

RECORD

- Island Company into the names of one of its principal shareholders and a company in which its other main shareholder was a principal shareholder. The accounts of the Appellant Company show that it retained beneficial ownership of the shares in the Island Company.
- pp.26-28
- p. 12 (8) By the end of 1963 the Appellant Company had disposed of the shares in Malaysian companies referred to in paragraph 4(5) above.
- p. 12 (9) Except for the above acquisitions and construction work the Appellant Company has not acquired any land or constructed any building. 10
- p. 10
pp.21-22 (10) On 27th April 1962 the Inland Revenue Department sent a standard form of enquiry to the Secretary of the Appellant Company asking, inter alia, for information concerning the nature of the business conducted by the Appellant Company and, on 16th August 1962, he replied that "the nature of the business conducted by the Company is dealing in immovable property and land development". 20
- pp.23-24
- pp.32-35
pp.61 and 63
pp.95-96
pp.102-104 (11) The Commissioners and both Courts below have relied on certain parts of both the Appellant Company's Memorandum of Association and its published accounts but it is part of the Appellant Company's case that, whatever relevance the parts so relied on may have, they should be judged in the light of all of the provisions of the said Memorandum and accounts. Further reference to these matters is made below. 30
- pp.13-21
pp.25-28
5. The Special Commissioners approached the matter by asking two questions:
- p. 30 (1) Whether, for income tax purposes, "the transfer of the property in exchange for shares can be treated as if it were a transaction of selling property for money". They held, as a matter of law, that that was so.
- pp.31-35 (2) Having so determined they then went on to hold that the excess of the value of the shares received over the cost of the property was a profit chargeable to income tax. They held 40

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that the facts pointed "to the conclusion that the Appellant Company has carried on the business of buying and selling property and that the profit in question has accrued to it from that business". The facts they referred to in support of that finding were:-

p. 32

(a) that the appellant Company was empowered amongst other things, by its Memorandum to traffic and otherwise deal in or turn to account immovable property;

p.32

(b) that since the shares acquired in the Island Company were subsequently transferred into the names of others (see paragraph 4(7) above) and that the shares in other Malaysian companies had likewise been transferred away (see paragraph 4(8) above) it was difficult to accept that the exchange was carried out for the purposes stated in the Appellant Company's resolution (see paragraph 4(6) above) at that time;

pp.32-33

(c) that in the Balance Sheet of the Appellant Company at 31st December 1962 the construction costs of the building were described as "work in progress" and classified amongst current assets;

pp.33-34

(d) that the reply of the Appellant Company's Secretary confirmed the classification in (c) and further supported the conclusion that the Appellant Company was carrying on the business of dealing in land.

p. 35

The Special Commissioners expressly rejected any reliance on the fact that the Appellant Company had borrowed moneys for the purposes of financing part of the construction costs.

p. 33

6. In the High Court of Malaya (H.S. Ong, J.) it was held that the Special Commissioners were justified in the determination they reached. The learned judge relied in particular on the fact that the Appellant Company erected the building together with the facts at paragraph 5(2)(a) to (d) above. He considered that the Scottish decisions in I.R.C. v. Livingstone (1927) 11 T.C. 532 and I.R.C. v. Reinhold (1953) 34 T.C. 389, concerned with whether or not a transaction constituted an

pp.55-63

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pp.61-63

pp.61-62

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adventure or concern in the nature of trade, supported this conclusion.

pp.94-107

7. In the Federal Court of Malaysia Raja Azlan Shah, F.J. (with whom Gill, C.J., Malaya, and Wan Sulaiman, F.J. agreed) delivered judgment dismissing the Appellant Company's appeal. In addition to the facts relied on by the Commissioners, Raja Azlan Shah F.J. appears to have considered that the following additional matters supported their conclusion:

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p. 101

(1) That the Appellant Company was a company with limited liability; and

pp.101-102

(2) that it had borrowed money to finance part of the construction costs, albeit that the Commissioners had expressly rejected reliance on this fact.

The learned Federal Justice appears to have considered that the facts established:

p. 105

"extensive series of dealings in immovable property over a period, and using for the purpose an organisation and methods such as are ordinarily adopted by property developers".

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8. The Appellant Company respectfully submits that, on the facts before them, the Special Commissioners were not entitled to come to the conclusion that they did and that both Courts below were wrong in upholding that determination. The Special Commissioners approached the matter

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p. 32

incorrectly by first asking the question whether an exchange could be treated as a sale (which is the wrong question) and, having answered that question in the affirmative, they went on to determine that the Appellant Company had carried on the business of buying and selling property. This is a non sequitur, and does not accord with the facts. In fact the Appellant Company sold no land whatsoever and the Commissioners disregarded this fact in determining that it had carried on the supposed business. The Commissioners relied on

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p.14. p.17

the fact that the Appellant Company had power to deal in land whilst disregarding the fact that it also had power to invest in land. The Commissioners relied on the Appellant Company's capacity to do

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something whereas they should have analysed what it in fact did. If what appears in the Appellant Company's accounts for the relevant period is relevant, those accounts, taken as a whole point to investment and not to the carrying on of a trade or business. Further, in view of the form in which the questions were posed, it is submitted that no reliance should have been placed on the reply given by the Appellant's Secretary to the standard form of enquiry made by the Inland Revenue Department. The Commissioners were not entitled to disregard the express purpose of the Appellant Company (as evidenced by its resolution) at the time of the exchange by reference to the fact that the shares in the Island Company were subsequently transferred into the names of others or, indeed, that the shares in other Malaysian companies originally acquired by it had also been transferred. These transfers were not sales, no consideration was received in respect of them, and the Appellant Company remained the beneficial owner of all the shares in the Island Company and thus achieved the purpose set forth in the resolution of 16th October 1963.

pp.25-28

pp.21-22

pp.23-24

pp.21-22

pp.10-11

pp.32-33

p. 11

pp.26-28

pp.10-11

9. The question the Commissioners should have asked is whether or not what the Appellant Company in fact did constituted the carrying on of a trade or business within Section 10(1)(a) of the 1947 Ordinance and not whether it had power to carry on a business or whether its accounts were consistent with such a business. Asking the question what the Appellant Company in fact did, it is submitted that there can be only one answer. The Appellant Company entered into one isolated transaction whereby it bought and developed land and exchanged that land for share capital of another company for the purposes of reconstruction and investment; and it retained beneficial ownership of the shares it acquired. Such a transaction cannot constitute the carrying on of a trade or business within the meaning of the 1947 Ordinance and accordingly there is no foundation in law for the proposition that the Appellant Company trafficked in immovable property. Alternatively, it is submitted that, if the facts before the Commissioners were equally consistent with the carrying on of a business, or not, the Respondent has failed to discharge the onus which lay on him to show that the Appellant Company's activities brought it within the charge to tax.

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10. It is further submitted that the words "trade" or "business" in Section 10(1)(a) of the 1947 Ordinance do not extend to an adventure or concern in the nature of trade so that, whether or not the transactions carried out by the Appellant Company could be regarded for United Kingdom tax purposes as such an adventure, they fell outside the scope of the 1947 Ordinance.

pp.61-62 11. None of the additional factors relied on in the Courts below to support the Commissioners' determination have any relevance. The fact, relied on by H.S. Ong, J., that the Appellant Company expended moneys in erecting the building is equally consistent with an intention to sell and an intention to hold as an investment by letting. pp.61-63 The authorities relied on by the learned judge, even in spite of the fact that they related to an adventure or concern in the nature of trade, nevertheless support the Appellant Company's case rather than that of the Respondent. The fact, relied on by Raja Azlan Shah, F.J., in the Federal Court, that the Appellant Company is a company incorporated with limited liability is irrelevant since limited liability companies can carry on a trade or business, or hold investments or do both. p.101 The fact that money was borrowed for the purposes of financing the construction is equally consistent with trading or investment and, furthermore, was expressly disregarded by the Commissioners. pp.101-102 20 p.33

p. 7 12. The Appellant Company humbly submits that the appeal should be allowed, that the judgments and order of the Federal Court upholding the determination of the Special Commissioners should be set aside, that both questions posed in paragraph 8 of the Case Stated should be answered in the negative and that the Respondent be ordered to pay to the Appellant Company its costs of this appeal, of the appeal in the Federal Court of Malaysia and of the appeal in the High Court of Malaya, for the following among other 30 40

R E A S O N S

(1) BECAUSE there were no facts on which the Special Commissioners could determine that the Appellant Company had carried on a trade or business within Section 10(1)(a) of the 1947 Ordinance so as to be liable to income tax on any profit therefrom.

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(2) BECAUSE even if, which is denied, the transaction in issue constituted an adventure or concern in the nature of trade, the same does not constitute the carrying on of a trade or business for the purposes of the said Section 10(1)(a).

(3) BECAUSE the Respondent failed to discharge the onus on him of bringing the Appellant Company within the said charge to income tax under the said Section 10(1)(a).

(4) BECAUSE the reasoning of the Special Commissioners, H. S. Ong, J., in the High Court and Raja Azlan Shah, F.J. in the Federal Court is not well founded.

BARRY PINSON

JOHN GARDINER

20 OF 1976

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ON APPEAL
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(APPELLATE JURISDICTION)

B E T W E E N:

INTERNATIONAL INVESTMENT
CO. LIMITED Appellant

- and -

THE COMPTROLLER-GENERAL
OF INLAND REVENUE Respondent

CASE FOR THE APPELLANTS

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