18/81

No.28 of 1978

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

O N A P P E A L

FROM THE FEDERAL COURT OF MALAYSIA

B E T W E E N :

LAHAD DATU TIMBER SENDIRIAN BERHAD — Appellant

- and -

THE DIRECTOR-GENERAL OF INLAND REVENUE — Respondent

RECORD OF PROCEEDINGS

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No.28 of 1978

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

ON APPEAL

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BETWEEN:

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INDEX OF REFERENCE

EXHIBITS

DOCUMENTS TRANSMITTED TO PRIVY COUNCIL
BUT NOT RE-PRODUCED

Description of Document	Date
Memorandum of Appeal to the Federal Court	1st September 1976
2 Notices of Appeal to the Special Commissioners of Income Tax	7th August 1971 7th January 1974
Notes of Yusoff J.	18th March 1975
Appellant's submission	Undated
Respondent's submission	Undated
Respondent's supplementary written submission	Undated
Appellant's further submission	Undated
Notice of Appeal to the Federal Court	24th July 1976
List of Exhibits	Undated
Exhibits (excepting those parts re-produced)	-
Notes of argument of Lee Hun Hoe, C.J. Borneo	3rd October 1977 29th December 1977
Notes of argument of Ong Hock Sim,F.J.	3rd October 1977
Notes of argument of Ho, J.	3rd October 1977
Appellant's submission	Undated
Respondent's submission	Undated
Reply to cross-appeal	Undated
Notice of Motion for Leave to Appeal	22nd February 1978
Affidavit of S Woodhull	19th January 1978
Order for conditional leave to appeal	21st March 1978

No.28 of 1978

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

ON APPEAL

FROM THE FEDERAL COURT OF MALAYSIA

BETWEEN:

LAHAD DATU TIMBER SENDIRIAN BERHAD — Appellant

- and -

THE DIRECTOR-GENERAL OF INLAND REVENUE — Respondent

RECORD OF PROCEEDINGS

In the High Court in Borneo at Kota Kinabalu

No.1

Case Stated by Special Commissioners of Income Tax

22nd November 1974

No. 1

CASE STATED BY SPECIAL COMMISSIONERS OF INCOME TAX

IN THE HIGH COURT IN BORNEO AT KOTA KINABALU

LAHAD DATU TIMBER SENDIRIAN BERHAD — Appellants

vs.

DIRECTOR GENERAL OF INLAND REVENUE — Respondent

CASE STATED by the Special Commissioners of Income Tax for the opinion of the High Court pursuant to paragraph 34 of Schedule 5 to the Income Tax Act, 1967

The appellants appealed to us, the Special Commissioners of Income Tax, in respect of two additional assessments on the appellants for the year of assessment 1969 dated 17th July, 1971, and 8th December, 1973.

2. Two questions were in issue for our determination

in this appeal. The first issue was whether the sum of $303,313.66, described by the appellants as "agency fee", was chargeable to timber profits tax under the Supplementary Income Tax Act, 1967 (Act 54). The second issue was whether the three sums of $158,000.00, $201,000.00 and $140,175.54, described by the appellants as "development cost", "planting payments" and "commission" respectively, were allowable deductions in the ascertainment of the adjusted income of the appellants from timber operations.

3. We heard the appeal on 30th and 31st May, 1974, and gave our decision on 11th July, 1974.

4. Encik M.K. Mathai, accountant, appeared for the appellants. Encik Mohammed bin Haji Said, Federal Counsel (Inland Revenue), appeared for the Director General of Inland Revenue.

5. Encik M.K.Mathai called Encik Abdul Majid Khan vin Haji Kalakham, Chairman and Managing Director of Lahad Datu Timber Sendirian Berhad, to give evidence for the appellants. Encik Philip Chong Kui Phin, Acting Assistant Director of Inland Revenue, was also called by Encik Mathai to give evidence.

6. The following documents were submitted to us, during the hearing, by the parties :-

(i) Agreed Bundle of Documents (Exhibit A1).

(ii) Letter dated 30.11.71 from T.M. Luk & Co. to Revenue (Exhibit A2(A)).

(iii) Letter dated 12.6.72 from Voon, Liew & Co. to Revenue (Exhibit A2(B)).

(iv) Letter dated 29.12. from Voon, Liew & Co. to Revenue (Exhibit A2(C)).

(v) Certificate of Incorporation of Private Company dated 10.12.66 (Exhibit A3).

(vi) Letter dated 24.11.71 from Revenue to T.M.Luk & Co. (Exhibit A4).

(vii) Letter dated 12.3.66 from District Officer, Lahad Datu (Exhibit A5).

(viii) Development Plan from Tungku Land Development Co-Op. Society (Exhibit A5(A)).

(ix) Letter dated 17.8.73 from Voon, Liew & Co. to Revenue (Exhibit R6).

(x) Cost of Timber Extraction from 1.3.68 (Exhibit R7).

(xi) Proceeds, Sale of Logs per Yong Bros. Co. Ltd., from 1.1.68 (Exhibit R8).

(xii) Profit & Loss Account for period ended 31.12.67 (Exhibit R9).

(xiii) Profit & Loss Account for period ended 31.12.69 (Exhibit R10).

(xiv) Profit & Loss Account for period ended 31.12.70 (Exhibit R11).

(xv) Profit & Loss Account for period ended 31.12.71 (Exhibit R12).

7. The following facts were admitted or proved :-

(a) State land, consisting of an area of approximately 4364 acres, was originally alienated to the Ulu Tungku Co-operative Land Development Society Limited of Lahad Datu (hereinafter referred to as the Society). It was for the purpose of agricultural development (folio 51 and 56 of Exhibit A1).

(b) At the same time, the Society was granted a timber licence by the State government with the rights to extract timber from the said land and thereafter remove and sell the timber (folio 51 and 56 of Exhibit A1).

(c) The Society did not, however, carry out the agricultural development of the land; nor did the Society undertake the timber extraction itself.

(d) Subsequently on 6th September, 1966, the Society entered into an agreement, described as "the timber extraction contract" (folio 13 of Exhibit A1) with Dato Donald Stephens and Abdul Majid Khan bin Haji Kalakhan.

(e) The said agreement, unfortunately, was not produced before the Special Commissioners during the hearing of this appeal. It was just not available.

(f) Subsequently, on 10th December, 1966, the Lahad Datu Timber Sendirian Berhad (hereinafter referred to as the appellants) was incorporated. Dato Donald Stephens and Abdul Majid Khan bin Haji Kalakhan were the only two subscribers to the Memorandum and Articles of Association of the appellant company (both undated enclosed in folio 4 to

44 of Exhibit A1).

(g) The objects of the appellant company, inter alia, were :

(i) To carry on business as forest operators, fellers, loggers and growers of timber and other forest products, and for these purposes to own, acquire, purchase, sell, lease, sub-lease, clear, plant, exploit, and work in any manner and for any consideration forest, land, timber estates, timber felling and forest clearing rights of any kinds, sawmills, plywood and veneer plants, workshops, factories and timber yards.

(ii) To carry on business as timber merchants, sawmill proprietors and timber growers, and to buy, sell, grow, prepare for market, manipulate, import, export, and deal in timber and wood of all kinds, and to manufacture and deal in veneers and plywood and articles of all kinds in the manufacture of which timbers or wood is used, and to carry on business as general merchants, and to buy, clear, plant and work timber estate, and to carry on any other business which may seem to the Company capable of being conveniently carried on in connection with any of the above or calculated directly or indirectly to render profitable or enhance the value of the company's property or rights for the time being.

(iii) To acquire and take over the timber extraction contract now being carried in Mukim TUNGKU, LAHAD DATU by virtue of an Agreement dated 6th September, 1966, and made between the ULU TUNGKU CO-OPERATIVE LAND DEVELOPMENT SOCIETY of Tungku, Lahad Datu of one part AND DATO DONALD STEPHENS AND ABDUL MAJID KHAN BIN HAJI KALAKHAN of the other part with a view thereto to adopt that Agreement and all or any of the assets and liabilities therein (sub-clause (MM) of clause 3 at folio 13 of Exhibit A1).

(h) The said agreement dated 6th September,

1966, was not produced. But witness, Abdul Majid Khan bin Haji Kalakhan, testified during the hearing that the appellants were incorporated solely for the purpose of adopting the said agreement. Nevertheless, the appellants did not make any formal resolution adopting the said agreement.

(i) Simultaneously on 13th June, 1967, the appellants entered into two agreements with the Society (folio 51 to 52 of Exhibit A1). One was merely described as "agreement for timber extraction" whereby the appellants undertook to fell and cut timber from blocks 1, 2, 3, 4, 5, 6 and 7 as indicated in the development plan (Exhibit A5(A)) and remove the timber to the log pond at the rate of $1.00 per cubic foot to be paid by the Society. The other was described as "agreement for timber export and execution of certain works" whereby the appellants undertook to sell and export the timber delivered to the log pond, to pay royalties due to the State government in respect of the timber and also to pay planting fees and fixed commission to the Society. In addition, the appellants undertook to execute certain works specified in the schedule to the latter agreement at a total cost of not exceeding $632,000.00 (folio 61 and 62 of Exhibit A1). Both the said agreements were specified for a period of four years and expired on 13th June, 1971.

(j) The appellants did not, however, intend to carry out the extraction, sale and export of the timber themselves. Consequently, on 28th June, 1967, the appellants entered into yet another agreement with Yong Brothers of Lahad Datu (folio 64 to 66 of Exhibit A1). There is no period stipulated in this agreement.

(k) In the agreement with the appellants dated 28th June, 1967, Yong Brothers undertook to fell the timber from the specified blocks and remove it to the log pond at a fee of 82 cents per cubic foot. In addition, Yong Brothers undertook to sell the timber and would receive a commission of 2% of the proceeds of sale.

(l) Letters of Credit were opened in favour of Yong Brothers by the buyers. The proceeds

of sale were collected by Yong Brothers and after deducting the extraction charges of 82 cents per cubic foot due to them plus the sales commission of 2%, the balance was paid to the appellants.

(m) In his evidence before the Special Commissioners, witness Abdul Majid Khan bin Haji Kalakhan testified that the appellants had not got the knowledge nor the expertise to carry out the undertakings. Hence, the services of Yong Brothers had to be employed. All the felling, transporting and selling of timber were actually undertaken by Yong Brothers.

(n) In the accounts for the year ended 31st December, 1968, (year of assessment 1969) the profit and loss account of the appellants shows the following income (folio 85 of Exhibit A1) :-

(i) Agency fee	$303,313.66
(ii) Extraction charges received	686,775.70
(iii) Interest received	8,157.82
	$998,247.18

(o) The said agency fee of $303,313.66 is derived as follows (folio 91 of Exhibit A1) :

Proceeds from the sale of 686,775.7 cubic foot of timber		$1,789,645.59
LESS:		
Royalty	$300,380.69	
Fixed Commission paid to the Society	140,175.54	
Extraction fee at $1.00 per cubic foot	686,775.70	
Planting payments	201,000.00	
Development cost	158,000.00	$1,486,331.93
Agency fee earned		$ 303,313.66

(p) The said proceeds of sale of $1,789,645.59 were, in fact, arrived at after deducting the sum of $36,651.52 which was paid to Yong Brothers and shown as "Commission paid - sub-contractor" (folio 85 of Exhibit A1). The said sum of $36,651.52 was incorrectly deducted and should, therefore, be added back to the said agency fee of $303,313.66.

8. The Director General of Inland Revenue decided to include the said agency fee of $303,313.66 in the computation of timber profits tax in respect of the appellants' adjusted income for the year of assessment 1969. The said agency fee was treated as income from timber operations. Likewise, the Director General of Inland Revenue disallowed as deductions the three sums of $158,000.00 (development cost), $201,000.00 (planting fees) and $140,175.54 (fixed commission) in computing the appellants' adjusted income for the relevant year of assessment.

9. It was contended on behalf of the appellants that :-

(a) the agency fee of $303,313.66 was income derived from the appellants' agency business by virtue of the "agency agreement";

(b) the two agreements concluded between the appellants and the Society on 13th June, 1967, should be construed as two separate and independent agreements. One was the "extraction agreement", specifically for the extraction of timber and onward delivery to the log pond. The other, referred to as the "agency agreement", was for the sale and export of timber from the log pond, and the execution of certain works for the development of the land;

(c) in other words, the said agreements should be treated as two separate contracts for the performance of different functions and not treated as contracts providing for one continuous process of activities;

(d) the "extraction agreement" and the "agency agreement" were independent of each other. The termination of one

would not automatically result in the termination of the other;

(e) either party could terminate the "agency agreement" without in any way affecting the operations of the "extraction agreement". Likewise, the "extraction agreement" could be terminated and the Society could still appoint some other persons to undertake the timber extraction so as to ensure that the "agency agreement" continue to be operative;

(f) by appointing the appellants as agents for the sales of timber and stipulating an obligation on the appellants to pay certain sums of money in return, as well as to carry out certain construction works at the specified cost, the Society was insuring itself against adverse fluctuations in the price of timber. The risk, if any, was passed on to the appellants by the Society. If the price of timber had fallen substantially then the appellants would have suffered a loss without any recourse to the Society for reimbursement;

(g) the said two agreements were not artificial or fictitious. They were entered into by the appellants with the Society in the course of an ordinary business dealing and not with the intention of avoiding tax. Hence, the respondent could not properly invoke the provisions of section 140 of the Income Tax Act, 1967, in this respect;

(h) It was wrong for the respondent to imply that the three sums of $158,000.00, $201,000.00 and $140,175.54, described as "development cost", "planting payments" and "commission" respectively, paid to the Society were 'Ali Baba' payments (folio 72 and 79 of Exhibit A1), and to have disallowed the said three sums for the purpose of income tax under the provisions of section 39(1)(g) of the Income Tax Act, 1967;

(i) there is nowhere in the said section or anywhere else in the said Act, any reference made to 'Ali Baba' payments;

(j) if the said sums are to be disallowed under the said section, the sums in question must clearly fall within the

meaning of the said section;

(k) in order to come within the meaning of the said section, the respondent must prove that the said sums were paid for the use of a licence or permit to extract timber from a forest in Malaysia;

(l) the sum of $158,000.00, namely "development cost", was in reality expenditure involved in connection with the construction works as stipulated in Schedule 5 of the "agency agreement" (folio 61 and 62 of Exhibit A1);

(m) it was a proper charge and, therefore, deductible in arriving at the adjusted income of the appellants, and was not a mere contingent liability as implied by the respondent (folio 77 of Exhibit A1);

(n) the two other sums of $201,000.00 and $140,175.45, viz. "planting payments" and "commission" respectively, were paid to the Society under clause 9(1) and (2) of the "agency agreement" (Folio 59 of Exhibit A1);

(o) the said "agency agreement" had nothing to do with the extraction of timber from a forest in Malaysia. The appellants, under the terms of the said "agency agreement", were merely acting as agents of the Society to sell the timber. As such, the said sums paid were not in any way connected with the use of a licence or permit to extract timber.

10. It was contended on behalf of the Director General of Inland Revenue that :-

(a) the purpose of the agreement dated 6th September, 1966, described as the timber "extraction contract", was to confer the rights under the licence to cut, remove and sell the timber to Dato Donald Stephens and Abdul Majid Khan bin Haji Kalakhan by the Society;

(b) the assignment of these rights and privileges was taken over by the appellants when it was incorporated on 10th December, 1966;

(c) the appellants would not have entered into the two agreements dated 13th June,

1967, with the Society if the Society did not have the rights and privileges under the licence to cut, remove and sell the timber;

(d) Yong Brothers too would not have entered into the agreement dated 28th June, 1967, with the appellants if the rights or privileges were not assigned to the appellants by the Society;

(e) since the word "extraction" is not defined under the Supplementary Income Tax Act, 1967, it must be given its ordinary meaning. The said word, in this case, arose from the phrase "income from timber extraction";

(f) the meaning to be attributed to the word "extraction" must be construed in relation to the words "timber" and "income";

(g) the sum of $303,313.66 described as "agency fee", therefore, constituted income from timber operations;

(h) alternatively, the respondent would invoke the provisions of section 140 of the Income Tax Act, 1967, in that the two agreements dated 13th June, 1967, entered into between the appellants and the Society, were artificial or fictitious. The said agreements were designed solely for the purpose of avoiding tax liability. Both agreements were executed on the same day and by the same parties for exactly the same considerations, viz. the rights and privileges under the licence;

(i) in all other respects, the appellants did not draw any distinction between cutting and selling. For all intents and purposes both these functions in the said two agreements should be treated as one continuous process of activities;

(j) only the two agreements draw that distinction. There is no such distinction shown in the appellants' accounts or records;

(k) the three sums of $158,000.00, $201,000.00 and $140,175.54, described as "development cost", "planting payments" and "fixed commission" respectively, were not outgoings or expenses wholly and exclusively incurred in the production of gross income

of the appellants within the meaning of section 33(1) of the Income Tax Act, 1967;

(l) in order to come within the ambit of section 33(1) of the said Act, the appellants must prove that the said sums were outgoings or expenses wholly and exclusively incurred in the production of income;

(m) the appellants have not proved that the said sums were outgoings or expenses wholly and exclusively incurred in the production of their gross income;

(n) even if the said sums were allowable deductions under the provisions of section 33(1) of the said Act, the appellants still must prove that the said sums are not disallowed under the provisions of section 39(1)(g) of the said Act;

(o) the said sums were paid by the appellants to the Society specifically for the use of the timber licence;

(p) the onus of proving that payments of the said sums were not made for the use of the timber licence is on the appellants.

11. The following authorities were cited to us :-

(i) Mangin v. Comrs. of I.R. (N.Z.), 70 A.T.C. 1001.

(ii) Ormond Investment Co. v. Betts, 13 T.C. 400.

(iii) Munro v. Comr. of Stamp Duties (1933), 34 S.R. (N.S.W.), 1, p.7.

(iv) Russell (Inspector of Taxes) v. Scott (1948), 2 All E.R. 1, p.5.

(v) Duke of Westminster v. I.R. Comr. 19 T.C. 490.

(vi) Henricksen v. Grafton Hotel Ltd., 24 T.C. 460.

(vii) Tariff Reinsurances Ltd. v. C. of T. (Vic) (1938) 1 A.I.T.R. 280.

(viii) Lord Vestey's Executors v. I.R.Comrs. (1949) 1 All E.R. 1120.

(ix) Wolfson v. I.R.Comrs. (1949), 1 All E.R.865, p.868.

(x) Lord Howard de Walden v. I.R. Comrs. (1948) 2 All E.R. p.829.

(xi) Graddock v. Zevo Finance Co. 27 T.C. 267.

(xii) Comr. of I.R. (N.Z.) v. Europa Oil (N.Z.) Ltd., 70 A.T.C. 6012.

(xiii) Newton v. F.C. of T. A.I.T.R. 298.

(xiv) Clarke v. F.C. of T. (1932), 48 C.L.R. 56.

(xv) Griersen v. I.R. Comr (N.Z.), 3 A.I.T.R. 3.

(xvi) Southern Railway of Peru Ltd. v. Owen (1956), 2 All E.R. 728.

(xvii) F.C. of T. v. James Flood Pty.Ltd., 5 A.I.T.R. 579.

(xviii) No.297 v. Minister of National Revenue, 55 D.T.C. 611.

(xix) Cape Brandy Syndicate v. I.R.Comrs. 12 T.C. 358.

(xx) Hutchinson v. Ripeka Te Peehi (1919) N.Z.L.R. 373.

(xxi) Supplementary Income Tax Act, 1967 (Act 54).

(xxii) Income Tax Act 1967 (Act 53)

(xxiii) Forest Enactment No.2 of 1968 (Sabah).

(xxiv) Forest Rules 1954 (Sabah)

(xxv) Shadford v. Fairweather 43 T.C. 291 at 299.

(xxvi) Eames v. Stepnell Properties Ltd. 43 T.C. 678.

(xxvii) Evidence Act (Act 56).

(xxviii) Leong Poh Chin v. Chin Thin Sin 1959 M.L.J. 246.

(xxix) Tan Bing Hock v. Abu Samah 1967 2 M.L.J. 148.

(xxx) Lo Su Tsoon Timber Depot v. Southern Estate 1971 2 M.L.J. 161.

(xxxi) Director-General of Inland Revenue v. Lee Thean Seng; originating motion 19/72, judgment of Chang Min Tat J., Penang.

12. We the Special Commissioners of Income Tax, who heard the appeal, after giving due consideration to the evidence adduced, the facts and submissions made to us by the parties,

agreed with the contention advanced on behalf of the respondent. We were of the opinion that the submissions put forth on behalf of the appellants were mere conjectures devoid of merit.

13. We were unanimously of the view that the sum of $303,313.66, described by the appellants as "agency fee", was liable to timber profits tax under section 20 of the Supplementary Income Tax Act, 1967 (Act 54). The said sum represents income derived by the appellants from timber operations within the meaning of the said section. The said sum, therefore, forms part of the gross income of the appellants from timber operations and should be taken into account in the computation of the gross income of the appellants for the year of assessment 1969.

14. We found that the gross income of the appellants from timber operations, for the relevant year of assessment should be $1,026,740.88. It was made up as follows:-

(i)	"agency fee"	$303,313.66
(ii)	Extraction fee (paragraph 7(n) above)	686,775.70
(iii)	Commission paid - sub-contractor (paragraph 7(p) above)	36,651.52
		$1,026.740.88

15. We were also unamimously of the view that in the ascertainment of the adjusted income of the appellants from timber operations, for the relevant year of assessment, the following three sums, namely :

(i)	Development cost	$158,000.00
(ii)	Planting payment	$201,000.00
(iii)	Commission	$140,175.54

paid by the appellants to the Society, were not outgoings or expenses wholly and exclusively incurred in the production of gross income of the appellants, under the provisions of section 33(1) of the Income Tax Act, 1967. The said sums were, in fact, paid for the use of the licence or permit to extract timber within the meaning of section 39(1)(g) of the

said Act and should not, therefore, be allowed as deductions.

16. We were unanimously of the opinion that the said three sums were paid to the Society as consideration for the assignment of the rights and privileges under the timber licence. These rights and privileges to extract and sell timber were, in fact, the sole consideration in both the agreements between the appellants and the Society. This is amply evident from the two preambles to the said two agreements. The process of extraction and sale of the timber would, therefore, be one continuous operation, as evidenced by the agreement dated 28th June, 1967, between the appellants and Yong Brothers (folio 64 to 66 of Exhibit A1). In effect, the agreement between the appellants and Yong Brothers is for the same purpose (except for the payment of the so-called "development expenditure") as contained in the two agreements between the appellants and the Society.

17. We accordingly ordered that the assessment of income tax in respect of the appellants for the year of assessment 1969, as contained in the notice of additional assessment dated 17th July, 1971, be amended accordingly, and we also decided that the assessment of income tax in respect of the appellants for the relevant year of assessment, as contained in the notice of additional assessment dated 8th December, 1973, be confirmed.

18. The appellants, by notice dated 13th July, 1974, required us to state a Case for the opinion of the High Court pursuant to paragraph 34 of Schedule 5 to the Income Tax Act, 1967, which Case we have stated and do sign accordingly.

19. The question of law for the opinion of the High Court is whether, on the evidence before us, our unanimous decision was correct in law.

Dated this 22nd day of November, 1974

Sgd: (M.C.Schubert)
Presiding Special Commissioner of Income Tax

Sgd: (Lee Kuan Yew)
Special Commissioner of Income Tax

Sgd: (Tan Sri Hj. Wan Hamzah bin Hj.Wan Mohamed)
Special Commissioner of Income Tax

No. 2

DECIDING ORDER OF SPECIAL COMMISSIONERS

In the High Court in Borneo at Kota Kinabalu

No.2

Deciding Order of Special Commissioners

11th July 1974

DECIDING ORDER

1. We, the Special Commissioners of Income Tax, find and decide that :-

(a) the sum of $303,313.66, described by the appellants as "agency fee", was an income derived by the appellants from timber operations, within the meaning of section 20 of the Supplementary Income Tax Act, 1967 (Act 54);

(b) the said sum of $303,313.66, therefore, forms part of the gross income of the appellants from timber operations and should be taken into account in the computation of the gross income of the appellants from timber operations for the year of assessment 1969;

(c) the sum of $36,651.52, paid by the appellants to Yong Brothers as sales commission, was part of the gross income of the appellants from timber operations and should, therefore, be taken into account in the computation of the gross income of the appellants from timber operations for the year of assessment 1969;

(d) the gross income of the appellants from timber operations, for the year of assessment 1969, was $1,026,740.88, made up of the three sums of

(i) $686,775.70, extraction charges received,

(ii) $303,313.66, described as "agency fee", and

(iii) $36,651.52, described as "commission paid - sub contractor";

(e) in the ascertainment of the adjusted income of the appellants from timber operations, for the year of assessment

1969, the following three sums of

(i) Development cost $158,000.00,

(ii) Planting payments $201,000.00 and

(iii) Commission $140,175.54,

paid by the appellants to the Ulu Tungku Co-operative Land Development Society Limited of Lahad Datu, are not outgoings or expenses wholly and exclusively incurred in the production of gross income of the appellants, under the provisions of section 33(1) of the Income Tax Act, 1967. The said sums were, in fact, paid for the use of the licence or permit to extract timber within the meaning of section 39(1)(g) of the said Act and should not, therefore, be allowed as deductions.

2. We, therefore, order that :-

(i) the assessment of income tax in respect of the appellants for the year of assessment 1969, as per notice of additional assessment dated 17th July, 1971, be amended to give effect to our findings as per paragraph 1(a), (b), (c) and (d) above; and

(ii) the assessment of income tax in respect of the appellants for the year of assessment 1969, as per notice of additional assessment dated 8th December, 1973, be confirmed.

Dated this 11th day of July, 1974.

Sgd: M.C.Schubert
Presiding Special Commissioner of Income Tax

Sgd: Lee Kuan Yew
Special Commissioner of Income Tax

Sgd: Tan Sri Hj.Wan Hamzah bin Hn.W.Mohd.
Special Commissioner of Income Tax

No. 3

LIST OF EXHIBITS BEFORE SPECIAL COMMISSIONERS

In the High Court in Borneo at Kota Kinabalu

No.3

List of Exhibits before Special Commissioners

Undated

LIST OF EXHIBITS

Exhibit No.	Particulars
A1	Agreed Bundle of Documents.
A2(A)	Letter dated 30.11.71 from T.M.Luk & Co. to Revenue.
(B)	Letter dated 12.6.72 from Voon Liew & Co. to Revenue
(C)	Letter dated 29.12.72 from Voon, Liew & Co. to Revenue.
A3	Certificate of Incorporation of Private Company dated 10.12.66
A4	Letter dated 24.11.71 from Revenue to T.M.Luk & Co.
A5	Letter dated 12.3.66 from District Officer, Lahad Datu
A5(A)	Development Plan for Tungku Land Development Co-Op. Society.
R6	Letter dated 17.8.73 from Voon, Liew & Co. to Revenue.
R7	Cost of Timber Extraction from 1.3.68.
R8	Proceeds, Sale of Logs per Yong Bros. Co.Ltd., from 1.1.68.
R9	Profit & Loss Account for period ended 31.12.67.
R10	Profit & Loss Account for period ended 31.12.69
R11	Profit & Loss Account for period ended 31.12.70.
R12	Profit & Loss Account for period ended 31.12.71.

EXHIBITS

A1 (part)

(i)

AGREEMENT DATED 13th June 1967 for timber extraction

C O P Y

AGREEMENT FOR TIMBER EXTRACTION

AGREEMENT made between the ULU TUNGKU COOPERATIVE LAND DEVELOPMENT SOCIETY LIMITED of Lahad Datu (hereinafter referred to as the Society) of the one part and the LAHAD DATU TIMBER SENDIRIAN BERHAD, Lahad Datu (hereinafter referred to as the Contractor) of the other part:

WHEREAS the Society has been granted State land of approximately four thousand three hundred and sixty-four (4,364) acres for the purpose of agricultural development with rights to extract and sell the timber on the land and apply the proceeds thereof for development of the land and the Society is desirous of entering into an Agreement with the Contractor for the extraction of timber for part of the land:

WHEREBY IT IS AGREED as follows -

1. The Society shall permit the Contractor to fell and cut timber from blocks 1, 2, 3, 4, 5, 6 and 7 as indicated and numbered on the Development Plan initialled by the parties and attached to this Agreement and to remove the timber to such log pond as shall be agreed between the parties.

2. The Contractor shall be paid for the timber so felled, cut and removed at the rate of one dollar ($1) per cubic foot, and such payment shall be made by the Society as soon as the timber has been measured for royalty by the Forest Department and delivered in the log pond.

3. The Contractor shall, in so far as it is always practicable to do so, give preference to members of the Society for work in the felling, cutting and removal of timber either on a contract basis or on any other basis on such terms as the Contractor may think fit.

4. The Society shall for the purpose of the

Contractor's operations under this Agreement give full and uninterrupted access to the Contractor, its servants and agents and where access is required to or on State lands the Society will seek such access from Government.

5. The Contractor's operations under this Agreement shall be conducted with due regard to the law, the conditions of the grant of the land to the Society and of the timber licence for the extraction of timber and any instructions given by the Conservator of Forests or his officers, and the Contractor shall indemnify the Society against any breaches thereof and against any claims for damage or injury done to any person or property in the undertaking of its operations under this Agreement.

6. The Contractor shall keep proper books of accounts which shall show the number of logs and volume of timber measured and removed and monies paid, and such accounts shall be open to inspection by any Committee member of the Society or by the Registrar of Cooperative Societies and his authorised officers.

7. It shall be the duty of the Contractor when sawing trees into logs to ensure good trading by avoiding as far as practicable bends, holes and other defects.

8. This Agreement may be terminated -

(a) by either party upon the breach of any condition of this Agreement,

(b) by the Contractor giving one month's written notice to the Society,

provided that in either case such termination shall be without prejudice to any rights, obligations and liabilities that may have accrued prior to the termination.

9. Any dispute under this Agreement shall be referred to arbitration by a single arbitrator to be agreed between the parties and failing agreement by three arbitrators, two of whom shall be appointed by the parties independently and the other by the two arbitrators so appointed.

10. The Contractor shall commence work as soon as may be after the signing of this Agreement and shall complete extraction within

four (4) years of the date of this Agreement.

Provided that if any delay has been occasioned to the Contractor's operation which could not have been reasonably avoided by the Contrator such extension of the completion date as may be reasonable in the circumstances shall be permitted.

11. The Agreement entered into by the Society and the Contractor dated the 6th day of September, 1966 is hereby cancelled.

Dated at Jesselton this 13th day of June, 1967.

The Seal of the Society is affixed in the presence of :-

Sgd:
Chairman (A.Kangan)

Sgd:
Vice Chairman
(Abdullah Kome)

Sgd:
Secretary (Abdul Razak)

Signed by Dato Donald Stephens and Majid Khan for and on behalf of the Contractor

Sgd:
Dato Donald Stephens

Sgd:
Majid Khan

Witness

"Certified True Copy"

I hereby certify that this 16th day of June, 1967 I have at Lahad Datu registered this document and numbered it as No.69/67 in the Register.

Stamp duty on original:	$1.00
Stamp duty on duplicate	1.00
Attestation fee	1.00
Registration fee	2.00
	$5.00

Sgd:Tony Chong
REGISTRAR
LAHAD DATU

Rt.K211331-32 of 16.6.67

EXHIBITS

A1 (part)

(ii)

AGREEMENT DATED 13th June 1967 FOR TIMBER EXTRACTION AND EXECUTION OF CERTAIN WORKS

C O P Y

AGREEMENT FOR TIMBER EXPORT AND EXECUTION OF CERTAIN WORKS

AGREEMENT made between the ULU TUNGKU COOPERATIVE LAND DEVELOPMENT SOCIETY LIMITED of Lahad Datu (hereinafter referred to as the Society) of the one part and the LAHAD DATU TIMBER SENDIRIAN BERHAD, Lahad Datu (hereinafter referred to as the Contractor) of the other part:

WHEREAS the Society has been granted State land of approximately four thousand three hundred and sixty-four (4,364) acres for the purpose of agricultural development with rights to extract and sell the timber on the land and apply the proceeds thereof for development of the land and the Society is desirous of entering into an Agreement with the Contractor for the sale of the timber on the Society's behalf and for certain works to be undertaken in the development of the land:

WHEREBY IT IS AGREED as follows -

1. The Society shall permit the Contractor to sell and export on behalf of the Society all the timber extracted from Blocks 1, 2, 3 4, 5, 6 and 7 as indicated and numbered on the Development Plan initialled by the parties and attached to this Agreement and delivered at such log pond as shall be agreed between the parties.

2. The Contractor shall -

(1) provide and keep in good order the log pond and be responsible for receiving and the custody of timber therein and for the transport of the timber to and on ships;

(2) pay for the timber extracted and delivered to the log pond as may

be due to any contractor from the Society;

(3) pay any royalty due to Government in respect of the timber.

3. It shall be the duty of the Contrator to find the best markets for the sale and export of the timber and to negotiate with buyers for the best price either in the name of the Society or in the name of the Contractor.

4. The Contractor shall keep proper books of account which shall show the number of logs and volume of timber held in the log pond, sold and exported, and the price and amount for the sale of timber, and such accounts shall be open to inspection by any Committee member of the Society or by the Registrar of Cooperative Societies and his authorised officers.

5. (1) The Contractor shall execute the works specified in the Schedule hereto at the costs not exceeding the amounts specified in the Schedule hereto.

(2) The location at which the works shall be executed shall be in accordance with the development plan hereto or otherwise as may be agreed between the parties.

(3) The date for the commencement and completion of any such works shall be as may be agreed from time to time by the parties.

6. The Contractor shall, in so far as it is always practicable to do so, give preference to members of the Society for work under this Agreement either on a contract basis or on any other basis and on such terms as the Contractor may think fit.

7. The Society shall for the purpose of the Contractor's operations under this Agreement give full and uninterrupted access to the Contractor, its servants and agents and where access is required to or on State lands the Society will seek such access from Government.

8. The Contractor's operations under this Agreement shall be conducted with due regard to the law, the conditions of the grant of the land to the Society and of the timber licence for the extraction of timber and any instructions given by the Conservator of Forests

or his officers, and the Contractor shall indemnify the Society against any breaches thereof and against any claims for damage or injury done to any persons or property in the undertaking of its operation under this Agreement.

9. The Contractor shall pay to the Society -

(1) a sum of Dollars Five Hundred and eighty seven thousand ($587,000) being the sum assessed and required for the planting of approximately one thousand seven hundred and twenty-four (1,724) acres with coconuts and cover crops, for maintenance of the planted area for six (6) months and for approximately twelve (12) miles of fencing, which amount may be paid to any contractor authorised by the Society and approved by the Director of Agriculture to undertake the works; payment shall be made by instalments and as may from time to time be requested by the Society provided that the total payment in any one year shall not exceed Dollars One hundred and ninety-eight thousand ($198,000).

(2) twenty-one (21) cents per cubic foot in respect of lots of six (6) feet girth or more, sold and exported, and five (5) cents per cubic foot in respect of logs less than six (6) feet girth, sold and exported; payment shall be made within one month from the date of the timber being sold and exported.

10. This Agreement may be terminated -

(a) by either party upon the breach of any condition of this Agreement or

(b) by the Contractor giving one month's notice in writing to the Society,

provided that in either case such termination shall be without prejudice to any rights, obligations and liabilities that may have accrued prior to the termination.

11. The Bank Guarantee of Dollars One hundred Thousand ($100,000) that has been furnished to

the Society by the Contractor shall continue but shall be released at any time after six (6) months from the date of this Agreement if the Society is satisfied that the Contractor is faithfully discharging its obligations under this Agreement.

12. Any dispute under this Agreement shall be referred to arbitration by a single arbitrator to be agreed between the parties and failing agreement by three arbitrators, two of whom shall be appointed by the parties independently and the other by the two arbitrators so appointed.

13. This Agreement shall be for a period of four (4) years from the date of this Agreement

Provided that if there is delay in the extraction and delivery of timber at the log pond and in the execution of any work under this Agreement, which could not have been reasonably avoided by the Contractor, such extension as may be reasonable in the circumstances shall be permitted.

SCHEDULE

(Clause 5)

Items	Amount
1. Construct approximately eight miles of road at $30,000 per mile as indicated in the Development Plan	$240,000
2. Construct 170 houses at $2,000 per house (including water tank and latrine) as indicated in the Development Plan and in accordance with standard specifications for such houses approved by the District Officer, Lahad Datu	$340,000
3. Construct a school with three class rooms (including latrine and basic furniture), as indicated in the Development Plan to be approved by the District Officer, Lahad Datu	$ 6,000
4. Construct one teacher's quarters (including water tank, latrine and standard furniture), capable of housing at least two teachers, as indicated in the Development Plan and in	

accordance with a plan to be approved by the District Officer, Lahad Datu $ 5,000

5. Construct a community centre with a floor space of 3,000 square feet (including a 2,000 gallon water tank and two latrines) as indicated in the Development Plan $13,000

6. Construct a staff quarters including water tank and latrine, as indicated in the Development Plan and in accordance with a plan to be approved by the District Officer, Lahad Datu $ 5,000

7. Level and construct a padang 110 yards x 132 yards as indicated in the Development Plan $ 5,000

8. Construct a rest house on a site to be selected by the Society $16,000

Dated at Jesselton this 13th day of June, 1967.

The Seal of the Society is affixed in the presence of -

Sgd: ??
Chairman (A.Kangan)

Sgd: ??
Vice Chairman
(Abdullah Kome)

Sgd: ??
Secretary
(Abdul Razak)

Signed by Dato Donald Stephens and Majid Khan for and on behalf of the Contractor

Sgd:
Dato Donald Stephens

Sgd:
Majid Khan

Witness

"Certified True Copy"

In the High Court in Borneo at Kota Kinabalu

No.3

EXHIBITS

(ii)

Agreement dated 13th June 1967 for timber extraction and execution of certain works

(continued)

I hereby certify that on this 16th day of June, 1967, I have at Lahad Datu Registered this document and numbered it as No.70/67 in the Register.

Stamp duty on original:	$1.00
Stamp duty on duplicate:	1.00
Attestation fee	1.00
Registration fee	2.00
	$5.00

Sgd: Tony Chong
REGISTRAR,
LAHAD DATU

Rt. K211331-32 of 16.6.67

EXHIBITS

(iii)

Agreement dated 28th June 1967

EXHIBITS

A1 (part)

(iii)

AGREEMENT dated 28th June 1967

AGREEMENT made between Lahad Datu Timber Sendirian Berhad of Lahad Datu (hereinafter referred to as the Contractor) of the one part and Yong Brothers of Lahad Datu (hereinafter referred to as the Sub-Contractor) of the other part

WHEREAS the Contractor has a contract to extract and sell timber from certain lands at Tungku Lahad Datu belonging to Ulu Tungku Land Development Co-operative Society Limited of Lahad Datu and the Contractor is desirous of entering into a sub-contract with the Sub-Contractor for the extraction and sale of timber from the said lands:

WHEREBY it is agreed as follows :-

1. The Contractor shall permit the Sub-Contractor to fell and cut timber from Blocks 1, 2, 3, 4, 5, 6, 7, as specified in the Development Plan attached hereto of the said lands and remove the timber to a log pond to be notified by the Contractor.

2. (1) The sub-Contractor shall at his own expense fell, cut and remove the timber

to the log pond.

(2) Upon the receipt by the Contractor of the timber in the long pond, the Contractor shall pay the sub-Contractor 82 (eighty-two) cents per cubic foot. Payment shall be made within one week from the receipt of the timber in the log pond.

(3) The cubic content of the logs shall be ascertained in accordance with the scale or method used by the Forest Department in the measurement of logs for royalty.

3. The Contractor shall provide for the log pond and shall be responsible for its maintenance and the custody of the timber in the log pond upon its receipt therein by the Contractor.

4. The Contractor shall be responsible for the payment of royalties due to Government.

5. No timber shall be removed from the felling area without prior notification of the Contractor, and the logs shall be measured either in the felling area prior to removal or at such other place, and in either case it shall be subject to agreement of the Contractor.

6. (1) The Contractor shall permit the sub-Contractor to sell the timber in the log pond to such market and at such prices as may be agreed from time to time between the parties, and the Contractor shall pay the sub-Contractor a commission of 2 (two) per cent of the proceeds of the sale of timber.

(2) The sub-Contractor shall be responsible for obtaining payment for the sale of timber and after deducting the commission aforesaid shall pay the balance to the Contractor, and every payment shall be made within one week from the date the timber is sold.

7. The Contractor shall be responsible at his own expense for the removal of the timber from the log pond to shipping points and on ships.

8. If any timber is lost in the course of removal from the felling area to the log pond

or from the log pond to ships, the sub-Contractor shall pay to the Contractor the amount that the timber would fetch if sold under this Agreement less the payments in clause 2 that the sub-Contractor would have received in respect of that timber.

9. The sub-Contractor's operations under this Agreement shall be conducted with due regard to the law, the conditions of the Licence to extract and remove timber and any instructions that may be given by the Conservator of Forests or his officers, and the sub-Contractor shall indemnify the Contractor against any breaches thereof or against any damage or injury done to any person or property in the undertaking of its operations under this Agreement.

10. The sub-Contractor shall keep proper books of accounts which shall show the number of logs and volume of timber felled, cut and removed and sold and the value of the sale, and such accounts shall be open to inspection by the Contractor.

11. It shall be the duty of the sub-Contractor when sawing trees into logs to ensure good grading by avoiding as far as practicable bends, holes and other defects.

12. This Agreement may be terminated by either party upon the breach of any condition of this Agreement by the other party or by giving one month's written notice to the other party provided that in either case such termination shall be without prejudice to any rights, obligations and liabilities that may have accrued prior to the termination.

IN WITNESS whereof the parties hereto have hereunto set their hands and seals the day and year first hereinabove written.

Signed on behalf of the sub-Contractor Yong Brothers.

YONG BROTHERS & CO.
Sgd. Illegible
Managing Partner

Signed on behalf of the Contractor Lahad Datu Timber Sendirian Berhad

Sgd. Illegible
Sgd. Illegible

Dated Jesselton 28th June 1967

I hereby certify that on this 30th day of June, 1967 I have at Lahad Datu registered this document and numbered it as No.78/67 in the Register.

Stamp duty on original:	$1.00
Stamp duty on duplicate:	1.00
Registration fee	2.00
Attestation fee	1.00
	$5.00

Sgd: Illegible
REGISTRAR
LAHAD DATU

K.211554-55
30.6.67

EXHIBITS

A1 (part)

(iv)

ACCOUNTS TO YEAR ENDED
31st December 1968

Office Copy

LAHAD DATU TIMBER SDN. BHD.

BALANCE SHEET

and

PROFIT AND LOSS ACCOUNT

year ended 31st December 1968

T.M. LUK & CO.
SABAH.

In the High Court in Borneo at Kota Kinabalu

No.3
EXHIBITS
(iv)
Accounts to year ended 31st December 1968
(continued)

LAHAD DATU TIMBER SENDIRIAN BERHAD

REPORT OF THE DIRECTORS

The Directors have pleasure in submitting herewith the Balance Sheet and Profit and Loss Account of the Company for the year ended 31st December, 1968.

After meeting all charges and providing Depreciation and Income Tax, the net profit for the year ended 31st December, 1968 amounted to $104,976.25 to be carried forward.

No dividend was paid during the year nor do the Directors recommend any amount to be paid by way of dividend.

In the opinion of the Directors, the results of the Company's operation for the year have not been materially affected by items of an abnormal character.

No circumstances have arisen which rendered adherence to the existing method of valuation of the assets or liabilities of the Company misleading or inappropriate.

Details of Directors' shareholdings in the Company during the year were as follows :-

	31.12.68
Abdul Hakin Khan	1
Abdul Majid Khan	1
	2

Messrs. T.M. Luk & Company, Kota Kinabalu, have indicated their consent to act as auditors of the Company for the ensuing year.

By Order of the Board
of Lahad Datu Timber Sdn.Bhd.

Sgd. Abdul M. Khan

Abdul Majid Khan
Chairman

INITIALS DATE

TYPED BY L.O.F. 20-10-69

ADDITIONS

Called Over

PASSED BY

Date:

LAHAD DATU TIMBER SENDIRIAN BERHAD

BALANCE SHEET AS AT 31ST DECEMBER 1968

1967			1967			
	AUTHORISED CAPITAL			**FIXED ASSETS**		
500,000	50,000 Ordinary shares of $10 each	500,000.00		Furniture & Fittings at cost - 1.1.68	5,606.11	
				Additions during year - at cost	3,222.75	
	ISSUED CAPITAL		4,999		8,828.86	
				Less Provision for Depreciation	1,429.29	7,399.57
20	2 ordinary shares of $10.00 each fully paid	20.00		Marine Vehicles - at cost - 1.1.68	2,900.00	
				Additions during year - at cost	1,926.46	
19,441	Profit and Loss Appropriation A/c	124,617.76			4,826.46	
				Less Disposal during year - at cost	2,900.00	
19,461	Shareholders Fund	124,837.76	2,610		1,926.46	
				Less provision for Depreciation	192.65	1,733.81
	CURRENT LIABILITIES			Motor Vehicles at cost 1.1.68	4,000.00	
				Additions during year - at cost	12,000.00	
					16,000.00	
46,942	Sundry Creditors and Accrued charges 265,358.44		3,000	Less Provision for Depreciation	4,750.00	11,250.00
32,509	Trade Creditors 99,135.31			Air Conditioners - at cost 1.1.68	885.40	
			750	Additions during year - at cost	986.00	
15,000	Provision for Income Tax 91,000.00				1,871.40	
				Less - provision for Depreciation	395.80	1,475.60
94,451		455,493.75		Office Equipment at cost - 1.1.68	39.00	
				Additions during year - at cost	1,065.00	
			33		1,104.00	
			6,250	Less provision for Depreciation	170.70	933.30
			17,642	Log Pond at cost - 1.1.68	6,941.27	
				Additions during year - at cost	821.96	
					7,763.23	
				Less provision for Depreciation	1,398.47	6,364.76
						29,157.04
	CONTINGENT LIABILITIES			**CURRENT ASSETS**		
			40,000			
	1. Developmental works amounted to $474,000.00 at the Ulu Tungku Lahad Datu		2,920	Deposit - The Chartered Bank - Lahad Datu	-	
			14,414	Staff Loan Advances	83,215.17	
	2. Crops planting cost for $1,724 acres at Ulu Tungku Lahad Datu amounted to $377,000.00		9,009	Trade Debtor	1,839.80	
				Cash on Hand	88.65	
				The Chartered Bank - Kota Kinabalu	185,553.46	
				The Chartered Bank - Lahad Datu	12,802.79	
				Deposit	250.00	
			66,343			283,749.87
			29,927	AMOUNT OWING BY MANAGING DIRECTOR		216,560.60
				INTANGIBLE		
				Exploratory & Preliminary Expenses		
113,912		580,331.51	113,912			580,331.51

LAHAD DATU TIMBER SENDIRIAN BERHAD

PROFIT AND LOSS ACCOUNT FOR YEAR ENDED 31ST DECEMBER, 1968

1967				1967		
	EXPENDITURE				**INCOME**	
131,326	Extraction cost - Sub-contractor		561,078.76	108,686	Agency Fee - per attached Statement	303,313.66
-	Tallyman and Hookman Charges		1,470.55	161,376	Extracted Charges Received	686,775.70
-	Boats & Launches Hire		2,231.50	-	Interest Received	8,157.82
-	Stevedoring		17,087.69			
-	Towing and Rafting		16,345.24			
-	Fuel & Oil		1,549.35			
-	Sundry Transport		663.08			
-	Repair Maintenance & Replacements		2,934.40			
-	Surveying Fee		250.00			
-	Penalty		574.70			
-	Logpond Expenses		6,136.72			
-	Evinrude 60 H.P. Out Board-Scrapped		2,610.00			
	ADMINISTRATIVE EXPENSES					
-	Secretarial & Consultation fees	1,110.50				
1,750	Audit Fees	3,000.00				
8,164	Commission paid - Sub-Contractor	36,651.52				
-	Donation	2,000.00				
8,256	Interest paid	-				
-	Advertising	479.00				
-	Legal Expenses	500.00				
365	Stationery Newspapers & Postages	2,158.75				
-	Bank Charges & Exchange	990.04				
-	Staff Requisite	826.35				
6,604	Entertainment	5,558.35				
5,167	Hotel Accommodation	6,606.55				
17,410	Travelling Air Fare	14,275.80				
-	Travelling Expenses & Allowance	3,126.90				
3,150	Telephone, Telegram & Trunk call	6,673.10				
-	Electricity, water & gas	2,507.40				
35,600	Salary & Wages	81,148.12				
712	Payroll Tax	1,560.00				
12,150	Rental Charges	12,263.00				
-	Medical Expenses	2,788.50				
2,037	Sundry Expenses	218.73				
2,730	Depreciation	5,897.13	189,338.94			
235,621			802,270.93			
15,000	Provision for Income Tax		91,000.00			
19,441	Net Profit after tax		104,976.25			
270,062			998,247.18	270,082		998,247.18

L'AHAD DATU TIMBER SENDIRIAN BERHAD

DEPRECIATION SCHEDULE FOR YEAR ENDED 31ST DECEMBER 1968

	ORIGINAL COST	W. D. V. 1.1.68	Considera-tion	DISPOSAL Profit	DISPOSAL Loss	ADDITIONS DURING YEAR	ACCOUNT FOR DEPRECITATION	RATE %	DEPRECIATION	W. D. V. 31.12.68
Furniture & Fittings	5,606	4,999				3,223	1,222	10	822	7,400
Marine Vehicles - 60 H.P. outboard	2,900	2,610	Scrap		2,610					
Speed Board (1)						1,428	1,428	10	142	1,286
Outboard Engine						498	498	10	50	448
Motor Vehicles -	4,000	3,000					3,000	25	750	2,250
1 Volvo car						12,000	12,000	25	3,000	9,000
Air Conditioners -	885	750					750	15	113	637
1 Philco conditioner						986	986	15	148	838
Office Equipment -										
1 electric kettle	39	33					33	15	5	28
1 calculating machine						365	365	15	55	310
1 adding machine						350	350	15	53	297
1 adding machine						350	350	15	52	298
Log Pond	6,941	6,250				822	7,072	10	707	6,365
	20,371	17,642			2,610	20,022	15,054		5,897	29,157

LAHAD DATU TIMBER SENDIRIAN BERHAD

INCOME TAX RETURN

ASSESSMENT YEAR 1969

	W. D. V. 1.1.68	ADDITIONS AT COST	I.A. 20%	TOTAL VALUE FOR ANNUAL ALLOWANCE	ANNUAL ALLOWANCE Rate	Amount	TOTAL ALLOWANCE	W. D. V. 31.12.68
Furniture & Fittings	4,205	3,223	645	7,428	5	372	1,017	6,411
Marine Vehicles		1,926	385	1,926	10	193	578	1,648
Motor Vehicles	2,400	12,000	2,400	14,400	20	2,880	5,280	9,120
Air Conditioners	620	986	197	1,606	10	161	358	1,248
Electric Kettle	27			27	10	3	3	24
Office Equipments:								
2 Adding Machines		700	140	700	10	70	210	490
1 Calculating Machine		365	73	365	10	36	109	256
Log Pond	6,247	822	164	7.069	10	707	871	6,198
	13,499	20,022	4,004	33,521		4,422	8,426	25,095

Marine Vehicle - 60 H.P. Outboard

Written down	due at 1st January 1968	2,030
Scrapped during	year	-
	Balancing Allowance	2,030

In the High Court in Borneo at Kota Kinabalu

No.3

EXHIBITS

(iv)

Accounts to year ended 31st December 1968

(continued)

LAHAD DATU TIMBER SDN. BHD

ASSESSMENT YEAR 1969 — INCOME TAX RETURN

SUMMARY OF DONATION ACCOUNT

	DEDUCTIBLE	NON-DEDUCTIBLE	TOTAL
St.Patrick School - Tavau	50.00	-	50.00
St.Joseph Convent-Penampang	200.00	-	200.00
Ursula's convent School	150.00	-	150.00
K.K.Mosque Building Fund	-	1,500.00	1,500.00
Govt.Primary School	50.00	-	50.00
Women's Institute	-	50.00	50.00
	450.00	1,550.00	2,000.00

LAHAD DATU TIMBER SDN. BHD.

PROFIT AND LOSS APPROPRIATION ACCOUNT FOR YEAR ENDED 31ST DECEMBER 1968

Transferred from 1967 Profit & Loss A/c	19,441.51
Add Excess provision for 1967 tax - written back	400.00
Transferred from 1968 profit and loss account	104,976.25
OR Balance carried forward	124,817.76

LAHAD DATU TIMBER SDN. BHD.

INCOME TAX COMPUTATION FOR ASSESSMENT YEAR 1969

Net Profit - per profit and loss account		195,976
Add:		
Depreciation	5,897	
Marine Vehicle Scrapped	2,610	
Travelling air fare	14,275	
Donation	2,000	24,782
		220,758
Less:		
Initial Allowance	4,004	
Annual Allowance	4,422	
Balancing Allowance	2,030	
Donation	450	
Travelling - air fare	7,980	18,886
Adjusted net profit		$ 201,872

2. STATEMENT SHOWING AGENCY FEE CALCULATION AT 31.12.1968

Proceeds from Timber sales 686,775.7 cu.ft.		1,789,645.59
Less		
Royalty	300,380.69	
Fixed Commission due to Ulu Tungku Co-op Society	140,175.54	
Extraction fee at $1.00 per cu.ft.	686,775.70	
Planting Payments	201,000.00	
Development Cost	158,000.00	
		1,486,331.93
Agency Fee transferred to General Profit & Loss Account		$ 303,313.66

3. EXTRACTION CHARGES RECEIVED $686,775.70

This amount was received from Ulu Tungku Developments Society, Lahad Datu. The rate is $1.00 per cu.ft. based on the number of cu.ft. exported during the year.

The volume exported for year ended 31st December, 1968 was 686,775.7 cu.ft.

Hence, Amount received = 686,775.7 x $1.00

$686,775.70

In the High Court in Borneo at Kota Kinabalu

No.4

Judgment of Mr.Justice Yusoff

30th June 1976

No. 4

JUDGMENT OF MR. JUSTICE YUSOFF

IN THE HIGH COURT IN BORNEO

KOTA KINABALU REGISTRY

ORIGINATING MOTION NO.7 of 1974

BETWEEN

Lahad Datu Timber Sendirian Berhad — Appellant

AND

Director-General of Inland Revenue — Respondent

Datuk Thomas Jayasuriya for Appellant Company

Encik Zulkifli bin Mahmood (Senior Federal Counsel) for Respondent

JUDGMENT

This is an appeal by case stated against the deciding order of the Special Commissioners of Income Tax in confirming the assessment of the appellant company's income for the year of assessment 1969 in respect of :

(1) the sum of $303,313.66, described by the appellant company as "agency fee" was an income derived by the appellant company from timber operations, within the meaning of section 20 of the Supplementary Income Tax Act, 1967 (Act 54), and

(2) the three sums variously described as Development cost $158,000.00 Planting payments $201,000.00 and Commission $140,175.54 paid by the appellant company to the ULU Tungku Cooperative Land Development Society Ltd. of Lahad Datu, were not outgoings or expenses wholly and exclusively incurred in the production of gross income within the scope of section 33(1) of the Income Tax Act, 1967 (Act 53).

The facts as found by the Special Commissioners are as follows :-

A forest area consisting of 4364 acres was

alienated to the Cooperative Society (Society) by the state government for agricultural purposes. At the same time the Society was granted with a timber licence with the rights to extract timber from the land. On 6th of September 1966 the Society entered into an agreement described as "the timber extraction contract" with the promoters of the appellant company. On 10th of December 1966 the appellant company was formed and on 13th of June 1967 the appellant company entered into two agreements with the Society one for timber extraction and the other for timber export and execution of certain works. As the appellant company had no expertise to do the work themselves, they entered into another agreement with Yong Brothers of Lahad Datu for the extraction of timber at a lesser fee than they had obtained from the Society. In addition Yong Brothers undertook to sell the timbers on a commission basis.

In the accounts for the year ended 31st December, 1968 for the year of assessment 1969, the profit and loss account of the appellant company shows the following income:

Agency fee	$303,313.66
Extraction charges received	686,775.70
Interest received	8,157.82
	$997,247.18

The agency fee was arrived at as follows:

Proceeds from timber sale of 686,755.7 cubic feet		$1,789,645.59
LESS		
Royalty	$300,380.69	
Fixed commission paid to the Society	140,175.54	
Extraction fee at $1/- per cubic ft.	686,775.70	
Planting payments	201,000.00	
Development cost	158,000.00	1,486,331.93
Agency fee earned		$ 303,313.66

On these facts the Special Commissioners found, on the first issue, that the "agency fee" represented income derived from timber operations and therefore, formed part of the gross income of the appellant company. No reason was given for this finding but the Special Commissioners indicated that they had agreed with the contention advanced on behalf of Revenue. In this respect, Revenue's contentions are :

1) the first agreement dated 6th September 1966 described as "extraction contract" was to confer rights under the licence to the promoters of the appellant company;

2) these rights were assigned to the appellant company when it was incorporated on 10th of December 1966;

3) proper construction must be given to the phrase "income from timber extraction" in section 20 of the Supplementary Income Tax Act 1967 (Act 54);

4) alternatively Revenue invoked section 140 of the Income Tax Act 1967 (Act 53) in that the two agreements dated 13th of June 1967 were artificial or fictitious and were designed solely for the purpose of avoiding tax;

5) in all intent and purposes the function of cutting and selling in the two agreements were not distinguished and should be treated as one continuous process of activities.

On the second issue, in the three sums variously described as Development Cost; Planting payments and Commission, the Special Commissioners found as a fact that they were paid for the use of the licence or permit to extract timber within the meaning of section 39(1)(g) of Act 53. The reasons advanced are:

1) these three sums were paid to the Society as consideration for assignment of rights under the licence;

2) the process of extraction and sale of timber was one continuous operation as evidenced by agreement dated 28th June 1967, between the appellant company and Yong Brothers.

It appears to me that the main contention by Revenue which was accepted by the Special Commissioners was that the two agreements dated 13th June 1967 were, designed for the purpose of avoiding tax and should, in that event be treated as one as providing for one continuous process of activity of cutting and selling timber.

This contention is also reflected in the Special Commissioners finding in respect of the three sums, Development cost, Planting payments and Commission, paid by the appellant company to the Society.

In my view and with due respect, to the Special Commissioners whether this was an inference of fact or law, it cannot be right. To construe that the two agreements as providing for one continuous activity of extracting and selling timbers, presupposes in this case, the existence of the timber licence granted by the government to the Society and that the rights under the licence had been assigned to the appellant company.

In this appeal, it is contended on behalf of the appellant company that the existence of this timber licence was not admitted by the appellant company at the hearing before the Special Commissioners. The reference by the Special Commissioners to the preamble of both agreements at Exhibit A1 at folios 51 and 56 is misleading. There is no mention of timber licence there. The preamble to these agreements merely state that "the Society has been granted State land.....for the purpose of agriculture development with rights to extract and sell timber on the land."

It seems that the contention of the appellant company has substance and on examining the original approval of the land by the government to the Society at Exhibit A5 it appears that the land was alienated expressly for cultivation of crops - para. (1) - andthat for the purpose of development, timber would be extracted from specified blocks - para.(5). No timber licence was granted. Further, conditions imposed on the Society by the government were: that all income from such timber extraction would be placed on deposit to be used for cultivation of crops, building of houses at certain locality in the area and for maintenance of the areas - paras (4) and (10).

On proper construction of both those two

agreements, it would appear that each agreement provides for different contract of service in line with the rights and obligation of the Society and the appellant company. They are not inter-related and each is capable of existing by itself.

The first agreement at Exhibit Al folio 51, is for the extraction of timber from part of the Society's land and among other things it provides that the Society would permit the appellant company to fell and cut timber from certain blocks on the land and remove them to a log pond to be agreed by the parties. The Society would pay the appellant company at the rate of $1.00 per cubic foot and such payment would be made when the timbers were delivered to the log pond. The agreement could be terminated by either party upon breach of any condition or by the appellant company on one month's written notice.

The second agreement at Exhibit Al folio 56 is for the sale of timbers on the Society's behalf and for certain works to be undertaken in the development of the land by the appellant company. This agreement among other things provides that the appellant company was to sell timbers extracted from the land on behalf of the Society at the best market price to be negotiated by the appellant company. Appellant company was to keep a log pond and be responsible for the custody of those timbers and to transport them to and load them on the ship; to pay any contractor for such timbers and pay royalties due to the government on those timbers; to make planting payment of a sum assessed at $587,000.00 by instalment not exceeding $198,000.00 a year, for a period of four years; and to pay a commission to th Society at the rate of 21 cents or 5 cents per cubic foot for timbers having 6 feet girth or less respectively, which had been exported by the appellant company. In addition the appellant company was to execute certain works specified in the schedule of the agreement comprising the construction of roads, houses, school, community centre, staff quarters, playing field and a rest house..... This is described by the appellant company as development cost.

This second agreement also provides for termination thereof by either party on breach of any condition or by the appellant company on one month's notice.

In view of those provisions it would not,

with respect, be right, to construe that both the agreements provide for one continuous process of activity.

On the question of assignment it is contended by Revenue that the original agreement dated the 6th of September 1966 conferred rights under the licence to the promoters of the appellant company. Further, it is contended that these rights were assigned to the appellant company by its promoter when the company was incorporated.

It is already shown that there was no such timber licence in existence and that it is wrong to assume that there was. Even assuming that there was such a licence there is no evidence to show that rights under the licence was conferred on the promoters of the company by the agreement. The agreement referred to was not in evidence. The only evidence available is that one of the objects of the appellant company, showing that it intended to adopt this timber extraction agreement - (Exhibit A1 folio 13 clause 3 (MM)). Nevertheless there are other evidence to show that the agreement was never acted upon. The appellant company did not even pass a formal resolution adopting the said agreement.

From these it would again appear that the inference drawn by the Special Commissioners on the assignment of rights under the licence is not supported by evidence.

Now, the basis for a charge of timber profit tax on which the income of the appellant company described as "agency fee" was assessed is provided in section 20 of the Supplementary Income Tax Act 1967 (Act 54) which says :

> "A supplementary income tax (to be known as timber profit tax) shall be charged for each year of assessment upon the income of any person derived from timber operations at the rates specified in this Part and shall be additional to the income tax (if any) charged in respect of that person for that year of assessment under the principal Act."

Section 19 defines those words underlined:

> "income derived from timber operations" includes all premiums, rents and tributes (by whatever name called) derived from timber operations, or from the granting or assignment of any rights, privileges,

licences, or concessions (by whatever name called) for the extraction of timber from a forest in Malaysia;"

"timber operations" means the extraction of timber from a forest in Malaysia or the granting or assignment of any rights, privileges, licences or concessions(by whatever name called) for the extraction of such timber but does not include the processing, milling, sawing or manufacturing of the timber."

In the interpretation of this provision Revenue had contended and accepted by the Special Commissioners that the word "extraction" appearing in the phrase "income from timber extraction" must be given its ordinary meaning and that the meaning to be attributed to this word must be construed in relation to the word "income" and "timber".

It is urged on behalf of the appellant company to which I quite agree that the quoted phrase is wrong. The proper phrase is "income derived from timber operations" and the word "extraction" is to be found in the definition of "timber operations" in section 19 of the Act.

In repeating Revenue's contention the learned Senior Federal Counsel urged that the word "income" in section 20 of the Act implies that there must be a sale and without sale there would be no income. That the word "timber" as defined in the Forest Enactment, 1968 (Sabah) gave a wide meaning as to include trees which had been felled and sold.

With respect, I think the method used by Revenue in construing this provision of the Act is indeed very strange and foreign to the rules of interpretation. To my mind there is no rule allowing the interpolation of words from one section of an Act into another, and similarly to employ the word defined in another statute not in pari materia, as an aid to construe a provision of an Act.

The difficulty encountered and attempted to overcome by Revenue seems to be the existence of the timber licence issued to the Society and that there was an assignment of the rights under the licence to the appellant company within the meaning of sections 19 and 20 of the Act; and that since there is no direct evidence on these facts they were presumed or inferred from other evidence. It should not be forgotten that in

construing a tax Act, there is no room for such presumption. The relevant maxim is "In a taxing Act clear words are necessary to tax the subject." This means that, in the words of Rowlatt J. in The Cape Brandy Syndicate v. The Commissioner of Inland Revenue 12 TC 358 at p. 366 :

> "It does not mean that words are to be unduly restricted against the Crown or that there is to be any discrimination against the Crown in such Acts....it means that in taxation you have to look simply for any intendment; there is no equity about a tax: there is no presumption as to a tax; you read nothing in; you imply nothing, but you look fairly at what is said and at what is clearly and that is the tax."

It would be necessary, in my view, to reassert this maxim on certain occasion and this is an appropriate occasion.

Further, in construing sections 19 and 20 of Act 54 Revenue gave strained and unnatural meanings to the words which have already been defined in the Act and employed a method of construction not known to the rules or interpretation of statutes. To that I would say as Lord Simonds emphasised in Wolfson v. Commissioners of Inland Revenue 31 TC at p.169 that :

> "It is not the function of a court of law to give to words a strained and unnatural meaning because only thus will a taxing section apply to a transaction which, had the Legislature thought of it, would have been covered by appropriate words."

It is also urged by the appellant company's counsel that Revenue was trying to revive the supposed doctrine of "substance and form" in tax cases in construing the two agreements dated 13th June, 1967, together. This is a cogent argument. This doctrine has been ruled inapplicable by the decision in the Duke of Westminster v. Commissioners of Inland Revenue 19 TC 490 H.L. and as said by Lord Russel of Killowen at p.524:

> "If all that is meant by the doctrine is that having once ascertained the legal rights of the parties you may disregard mere nomenclature and decide the question of taxability or non-taxability in accordance with the legal rights, well and good..... If, on the other hand,

> the doctrine means that you may brush aside deeds, disregard the legal rights and liabilities arising under a contract between parties, and decide the question of taxability or non-taxability upon the footing of the rights and liabilities of the parties being different from what in law they are, then I entirely dissent from such a doctrine."

In that case the Court had to decide whether certain payments made by the appellant Duke, under several deeds of covenant, constitute annual payments which were deductible in computing his income for Surtax. The deeds provided for payments to his ex-employees in consideration for past services and it was explained that in the event of their being re-engaged they would be expected to be content with the provision and addition of such sum as would bring the total payments to the amount of salary or wages they had been receiving before. It was decided that "the substance of the transaction was to be found and to be found only by ascertaining the respective rights of the parties under the deeds," at p.524 and held that these were annual payments and were admissible deductions in computing the appellant's income for Surtax purpose.

In the present case, it is argued by learned counsel for the appellant that Revenue had only looked at the substance and not the form of those agreements. This simply means that the true legal position of the parties is disregarded and a different legal right and liability substituted in the place of the legal right and liability which the parties had created.

I accept that argument and would quote Lord Greene, M.R. in Craddock (H.M. Inspector of Taxes) v. Zevo Finance Co.Ltd. 27 TC 267 at p.279 on similar attempt to revive this doctrine:

> "The argument, so far as it deals with the facts of the present case, is, as it appears to me, nothing but an attempt to revive the "supposed doctrine" of substance and form. That argument, one had hoped, had been decently interred by the decision in Commissioners of Inland Revenue v. Duke of Westminster. But its ghost still walks on occasions, and this, it appears to me, is one of them."

Lastly, Revenue invoked section 140 of the Income Tax Act, 1967 (Act 53) and contended

that the two agreements were "artificial or fictitious". With respect, there are no such words in the section. The section merely provides that:

> "140(1) The Director General, where he has reason to believe that any transaction has the direct or indirect effect of -
>
> (a) altering the incidence of tax which is payable or suffered by or which would otherwise have been payment or suffered by any person;
>
> (b) (c) & (d) not applicable.
>
> may, without prejudice to such validity as it may have in any other respect or for any other purpose, disregard or vary the transaction and make such adjustments as he thinks fit with a view to counter-acting the whole or any part of any such direct or indirect effect of the transaction."

With respect, I cannot follow the argument advanced by the learned Senior Federal Counsel that because, both these agreements were executed on the same day, by the same parties and for the same consideration they were in effect designed solely for the purpose of avoiding tax. Nevertheless, I do not think that this argument would go to show that the transaction has 'the direct or indirect effect of altering the incidence of tax' as provided in section 140, of the Act.

In my opinion, in order to see that the transaction in this case had the effect of altering the incidence of tax, it must be shown that the transaction is not capable of explanation by reference to ordinary business dealing without necessarily being labelled as a means to avoid tax. In the words of Lord Denning in Newton v. Federal Commissioner of Taxation (1958) 2 All E.R. P.C.759 at p.764 :

> "In order to bring the arrangement within the section, you must be able to predicate- by looking at the overt acts by which it was implemented - that it was implemented in that particular way so as to avoid tax. If you cannot so predicate, but have to acknowledge that the transactions are capable of explanation by reference to ordinary business or family dealing, without necessarily being labelled as a

means to avoid tax, then the arrangement does not come within the section."

Newton's case was a decision of the Privy Council resting of section 260 of the Australian (Commonwealth) Income Tax Assessment Act 1936-1960 which is in pari materia with our section 140 of Act 53.

In explaining this passage Lord Donovan in delivering majority judgment of the Judicial Committee in Mangin v. Commissioner of Inland Revenue (1971) 2 WLR 39 at p.47, His Lordship said :

> "....this passage, properly interpreted, does not mean that every transaction having as one of its ingredients some tax saving feature thereby becomes caught by a section such as section 108. If a bona fide business transaction can be carried through in two ways, one involving less liability to tax than the other, their Lordships do not think section 108 can properly be invoked to declare the transaction wholly or partly void merely because the way involving less tax is chosen..... The clue to Lord Denning's meaning lies in the words "without necessarily being labelled as a means to avoid tax." Neither of the examples above given could justly be so labelled. Their Lordships think that what this phrase refers to is, to adopt the language of Turner J. in the present case,
>
> > "a scheme.....devised for the sole purpose, or at least the principal purpose, of bringing it about that this taxpaper should escape liability on tax for a substantial part of the income which, without it, he would have derived."

Mangin's case is a decision of the Privy Council on the application of section 108 of the New Zealand Land and Income Tax Act 1954 which is similar in context with the Australian Income Tax Assessment Act 1936-1960, section 260 ibid.

In applying these principles to the present case and by looking at the two agreements, in my opinion, it cannot be said that the transaction was done to avoid tax.

The question to be asked is, what was

the purpose of the arrangement for the appellant to enter into two agreements with the Society, instead of one. It is not difficult to see that the appellant company's purpose was to separate their income derived from the extraction of timber and those income from the sales of timbers on behalf of the Society. Their income from timber extraction fees as contracted in the first agreement for the year was $686,775.70; and their income from the sales of those timbers namely, the agency fee was $303,313.66, according to the terms of the second agreement. This arrangement brings about the result that the appellant company escapes liability for timber profit tax on their income derived from the sales of those timbers; but not their income from timber extraction fees.

Now, whether this was or was not an ordinary business dealing, it is argued by the appellant company that both agreements were independent of each other and that termination of one would not automatically result in the termination of the other; that both agreements were made in consistent with the rights and obligation of the parties.

Revenue did not contend that these agreements were not made in the course of ordinary business dealing but question the purpose of the agreements mainly on the ground that they were entered into on the same date.

In my opinion, there is nothing unusual in this type of business for one person to contract for the cutting and extracting of timbers from the forest and for another person to contract for selling of those timbers in the market; or for that matter, for one person or company to contract for both of these services. Equally the concession owner has the right to contract out one aspect of the business, that is for example, the cutting and extracting of timbers only and retain the other that is, selling those timbers himself. These are matters for the decision of each business dealing. In these circumstances it would be difficult to say that the arrangement adopted by the appellant company was not an ordinary business dealing.

Finally, what was the effect of the arrangement? The appellant company had conceded that their income derived from the first agreement was liable to timber profit tax. This income was substantial compared to the

income derived from the second agreement which is now under appeal. What the appellant company has established by entering into this second agreement - Exhibit A1 folio 56, with the Society was, not only to provide for their services in selling the timber but more so, as the agreement at Clause 5 and the Schedule shows, to execute major development works on the land by constructing roads, building houses, school, teachers quarters, community centre, staff quarters, playing field and a rest house. These services and cost of development were required of the appellant company, to meet from the income derived from the sales of those timbers. This is in addition to various payments they had to make such as payment to contractors for timber extracted, payment of royalty due to Government (Clause 2); cost of planting coconuts on 17724 acres of land and its maintenance for six months, cost of 12 miles of fencing and to pay certain commission to the Society (Clause 9). It may well be argued that these terms could be drafted into the first agreement, but there seem to be no objection to a choice of a method more convenient to the parties.

From these facts it could not be said that the principal purpose of the arrangement was designed to avoid tax or in the words of Lord Denning - "necessarily being labelled as a means to avoid tax." This is more so when the substantial income from this arrangement had already been conceded to be taxable. In my view, the principal purpose of the scheme or transaction designed by the appellant company was to facilitate the development of the land and the execution of works of building houses, school and other facilities relating to such development. The tax saved by the appellant company in this respect was not substantial. With due respect I do not think that in this case, section 140 of Act 53 can properly be invoked.

On the second issue with regard to the three sums :

(i)	Development Cost	$158,000.00
(ii)	Planting Payment	$201,000.00
(iii)	Commission to the Society	$140,175.54

the Special Commissioners held that they were not outgoing or expenses wholly and exclusively incurred in the production of gross income within the provision of section 33(1) of the Income Tax Act, 1967 (Act 53). They went further

to say that they found as a fact that these three sums were paid for the use of the licence or permit to extract timber within the meaning of section 39(1)(g) of the Act and should not therefore be allowed as deductions.

With respect to the Special Commissioners, in my view, that is not a correct interpretation of the law. Following Chang Min Tat J's decision in Director General of Inland Revenue v. L T.S. (1974) 1 MLJ 189, the Federal Court in Federal Court Civil Appeal No.64 of 1974 (not reported) referred favourably to the construction of section 33 and 39 of Act 53 by the Judge in that :

> "Section 33(1) deals with deductions which are allowed. Section 39 refers to deductions which are not allowed ..... what is relevant is section 39(1)(g) which speaks of 'any sum, by whatever name called, payable (otherwise than to a State Government) for the use of a licence or permit to extract timber from a forest in Malaysia.' Section 39 (2), provides as follows :-

Section 39(2) was quoted and the Court went on to say that :

> "The learned Judge interpreted section 39(2) to mean that the deductions allowed by section 33 in respect of expenses wholly and exclusively incurred in the production of gross income do not extend to the expenses mentioned in section 39(1)(a) to (g)..... Against that part of the learned Judge's judgment there is no appeal."

To my mind that is the correct interpretation of sections 33 and 39 of Act 53. The disallowing provision in section 39(1)(g) would only apply if the outgoings or expenses claimed by the appellant company fell within section 33(1) of the Act. If not section 39(1)(g) would have no application. A taxpayer cannot be held to be liable for his tax twice, once under section 33(1) and again under section 39(1)(g) of the Act.

The reasons advanced by the Special Commissioners in arriving at the decision again, as in the first issue rested on the existence of timber licence and the application of

"substance and form" doctrine. These have been touched above, as not correct.

It appears that section 140 of Act 53 was not pleaded in respect of these three sums. If it was, it would not, in my opinion, be proper in view of the absence of particulars of adjustment which should be given to the appellant company with the notice of the additional assessment dated 8th of December 1973 issued to the appellant company at Exhibit A1 folio 48. This is required by sub-section (5) of section 140 of the Act.

Apart from these, there seem to be no other reason of fact to support the finding of the Special Commissioners that the three sums; development cost, planting payment and commission paid to the Society were not outgoings or expenses wholly and exclusively incurred in the production of the appellant company gross income.

But on the facts of the case I would only concede to the argument of the appellant company's learned counsel that in so far as the two payments in respect of Development Cost and Planting payments were concerned, they were the Society's and I would say the Society had to account these two sums to the government and kept them in deposit as directed by them before the land could be effectively alienated to the Society. Otherwise the land would be forfeited by the government - see conditions 10 and 11 at Exhibit A5. These sums were in effect payments made to the government which are deductable under section 33(1) of the Act as outgoing and expenses wholly and exclusively incurred in the production of the appellant company's income.

Regarding the Commission of $140,175.54 paid by the appellant company to the Society, this cannot be said to be in the same position as the other two payments. This sum was clearly a payment made to the Society for its exclusive purpose and therefore not deductable.

On both these issues I find, with respect to the Special Commissioners that they have misdirected themselves in the interpretation of section 20 of the Supplementary Income Tax Act 1967 (Act 54) and the application of section 39(1)(g) in relation to section 33(1) of the Income Tax Act 1967 (Act 53). They have also misdirected themselves on the application of section 140 of Act 53. In doing so they arrived at wrong conclusions.

Paragraph 34 of Schedule 5 of the Income Tax Act 1967 provides that an appeal to this court may be taken on points of law. What is a question of law has been well established. That the decision of the Commissioners when they have ascertained the facts of the case and on conclusion of those facts which they have found proved, is not open to review "provided that they did not misdirect themselves in law in any of the forms of legal error, which amount to misdirection", per Viscount Sumner in Lysaght v. The Commissioners of Inland Revenue (1928) AC 234. And as was said by Lord Radcliffe in the celebrated case of Edwards (H.M. Inspector of Taxes) v. Bairstow & Harrison 36 TC 207 at p. 229:

> "When the Case comes before the Court, it is its duty to examine the determination having regard to its knowledge of the relevant law. If the Case contains anything ex facie which is bad in law and which bears upon the determination, it is, obviously, erroneous in point of law. But, without any such misconception appearing ex facie, it may be that the facts found are such that no person acting judicially and properly instructed as to the relevant law could have come to the determination under appeal. In those circumstances, too, the Court must intervene....."

Having regard to these principles I find that the Special Commissioners have been erroneous in points of law in arriving at their determination on mainly both the issues. In these circumstances I would allow this appeal and order that the decision of the Special Commissioners be varied to the extent that:

(1) the sum of $303,313.00 described as "agency fee" is not assessible as timber profits tax under section 20 of the Supplementary Income Tax Act, 1967 (Act 54);

(2) the two sums $158,000.00 and $201,000.00 described as Development Cost and Planting payments respectively, are outgoings and expenses wholly and exclusively incurred in the production of gross income of the appellant company and therefore

deductible under section 33(1) of the Income Tax Act, 1967 (Act 53).

The decision in respect of a sum of $36,651.52 described as "commission paid to sub-contractor and the sum of $140,175.74 described as commission paid to Society" is confirmed.

Appeal partly allowed.

(YUSOFF, J.)
JUDGE IN BORNEO.

Delivered at Kota Kinabalu on 30th June 1976.

CERTIFIED TRUE COPY

Sgd:-
Ag. Secretary to Judge

No.5
Order of High Court
30th June 1976

No. 5

ORDER OF HIGH COURT

IN THE HIGH COURT IN BORNEO AT KOTA KINABALU

KOTA KINABALU REGISTRY

Originating Motion No.7 of 1974.

BETWEEN

Lahad Datu Timber Sendirian Berhad — Appellant

AND

Director-General of Inland Revenue — Respondent

BEFORE THE HONOURABLE DATUK JUSTICE YUSOFF BIN MOHAMED JUDGE IN BORNEO

IN OPEN COURT THE 30TH DAY OF JUNE, 1976

O R D E R

WHEREAS pursuant to paragraph 34 of Schedule 5 to the Income Tax Act, 1967, a case had been stated at the request of the Appellant by the Special Commissioners of Income Tax for the opinion of the Court:

AND WHEREAS the said case coming up for hearing on the 18th and 19th days of March, 1975 in the presence of Datuk Thomas Jayasuriya Esq. of Counsel for the Appellant and Zulkifli bin Mahmood Esq., Senior Federal Counsel, for the Respondent AND UPON READING the Case Stated AND UPON HEARING both Counsel as aforesaid IT WAS ORDERED that this case do stand adjourned for judgment AND the same coming on for judgment this 30th day of June, 1976 in the presence of Paul Kan Esq. of Counsel for the Appellant and Encik Philip Chong Kui Phin, Assistance Director of Inland Revenue, Sabah, for the Respondent:

THIS COURT IS OF OPINION that the determination of the said Special Commissioners of Income Tax on mainly both the issues under appeal is erroneous AND IT IS ORDERED that the Appeal is hereby partly allowed and the Deciding Order of the said Special Commissioners of Income Tax dated 11th of July, 1974 be varied to the extent that:

(1) the sum of $303,313.00 described as "agency fee" is not assessable as timber profits tax under section 20 of the Supplementary Income Tax Act, 1967 (Act 54);

(2) the two sums of $158,000.00 and $201,000.00 described as Development Cost and Planting payments respectively, are outgoings and expenses wholly and exclusively incurred in the production of gross income of the Appellant company and therefore deductible under section 33(1) of the Income Tax Act, 1967 (Act 53):

AND IT IS FURTHER ORDERED that the decision of the said Special Commissioners of Income Tax in respect of the sum of $36,651.52 described as "Commission paid to sub-contractor" and the sum of $140,175.74 described as "Commission paid to Society" is hereby confirmed AND IT IS LASTLY ORDERED that costs to the Appellant to be taxed.

GIVEN under my hand and the Seal of the Court this 30th day of June, 1976.

L.S. Raymond Wong Tung Chuen,
Senior Assistant Registrar,
High Court In Borneo.

In the Federal Court of Malaysia

No.6

Judgment of Lee Hun Hoe Chief Justice

29th December 1977

No. 6

JUDGMENT OF LEE HUN HOE, CHIEF JUSTICE, BORNEO

IN THE FEDERAL COURT OF MALAYSIA HOLDEN AT KOTA KINABALU

(Appellate Jurisdiction)

Federal Court Civil Appeal No.106 of 1976

BETWEEN

Director-General of Inland Revenue — Appellant

AND

Lahad Datu Timber Sendirian Berhad — Respondent

(In the matter of Originating Motion No. 7 of 1974
In the High Court in Borneo at Kota Kinabalu

BETWEEN

Lehad Datu Timber Sendirian Berhad — Appellant

AND

Director-General of Inland Revenue — Respondent)

Coram: Lee Hun Hoe, C.J. Borneo
Ong, F.J.
Ho, J.

JUDGMENT OF LEE HUN HOE, CHIEF JUSTICE, BORNEO

This appeal against the decision of the learned Judge centres round four sums of money described as agency fee ($303,313.66), development cost ($158,000.00), planting payments ($201,000.00) and commission ($140,175.54). The first three sums are under appeal by the appellant while the last is under cross-appeal by the respondent.

The facts as found by the Special Commissioners are fully set out in the case stated. For the purpose of this appeal I will outline some of the facts. In early 1966 a parcel of State land of approximately 4,364 acres was alienated to the Ulu Tungku Co-operative Land Development Society Ltd. ("the society") for the purpose of agricultural development. At the same time the society was granted a timber licence by the State Government with the rights to extract timber and thereafter remove and sell timber so

extracted from the said land. The society did not carry out the agricultural development or extract timber by itself. On 6th September, 1966 the society entered into an agreement described as "the timber extraction contract" with Dato Donald Stephens and Abdul Majid Khan bin Hj. Kalakhan who were the promoters of Lahad Datu Timber Sdn. Bhd., the respondent, which, however, were incorporated on 10th December, 1966. The two promoters were also the only two subscribers to the Memorandum and Articles of Association of respondent company.

On 13th June, 1967 respondent entered into two agreements with the society. The "first agreement" was merely described as an "agreement for timber extraction" whereby respondent undertook to fell and cut timber and remove the timber to the log pond at the rate of $1.00 per cubic foot to be paid by the society. The "second agreement" was described as an "agreement for timber export and execution of certain works" whereby respondent undertook to sell and export the timber delivered to the log pond, to pay royalties due to the State Government in respect of the timber and also to pay planting fees and fixed commission to the society. In addition, respondent undertook to execute certain works specified in the Schedule to the latter agreement at a total cost not exceeding $632,000.00. Both agreements were specified for a period of four years and, therefore, expired on 13th June, 1971.

The respondent did not. however, intend to carry out the extraction, sale and export of the timber themselves. Consequently, on 28th June, 1967 respondent entered into an agreement with Yong Brothers of Lahad Datu. Under the agreement Yong Brothers undertook to fell the timber and to remove them to the log pond at a fee of 82 cents per cubic foot. Also, Yong Brothers undertook to sell the timber at a commission of 2% of the proceeds of sale. Letters of Credit were opened in favour of Yong Brothers by the buyers. The proceeds of sale were collected by them. After they deducted the extraction charges of 82 cents per cubic foot and the sale of commission of 2% they would pay the balance to respondent.

In the accounts for the year ending 31st December,1968 (Year of Assessment 1969)

the profit and loss account of respondent shows the following income :-

i)	Agency fee	$303,313.66
ii)	Extraction charges received	686,775.70
iii)	Interest received	8,157.82
		$998,247.18

The agency fee of $303,313.66 is derived as follows :-

Proceeds from the sale of 686,775.7 cubic feet of timber		$1,789,645.59
Less		
Royalty	300,380.69	
Fixed commission paid to the society	140,175.54	
Extraction fee at $1.00 per cubic foot	686,775.70	
Planting payments	201,000.00	
Development cost	158,000.00	1,486,331.93
Agency fee earned		$ 303,313.66

The said proceeds of sale of $1,789,645.59 were, in fact, arrived at after deducting the sum of $36,651.52 which was paid to Yong Brothers and shown as commission paid to sub-contractor. This error was discovered during the hearing before the Special Commissioners. The sum was twice deducted, once in the computation of the proceeds of sale and again charged to the Profit and Loss Account (see page 304 of the Appeal Record). The parties agreed that this sum was incorrectly deducted and should, therefore, be added back to the agency fee. This would not affect the issues before the court.

There were two issues before the Special Commissioners. The first is whether the sum of $303,313.66 described as "agency fee" is liable to timber profits tax. The second is whether the three sums described as

development cost ($158,000.00), planting payments ($201,000.00) and commission ($140,175.54) are allowable deductions in ascertaining the adjusted income of the respondent. They were unanimous that the sum of $303,313.66 described as "agency fee" was liable to timber profits tax under section 20 of the Supplementary Income Tax Act, 1967 (Act 54). This sum forms part of the gross income of the respondent from timber operation and should be taken into account in the computation of gross income of respondent company for the year of assessment 1969. They found the gross income of respondent from timber operation for the relevant year of assessment to be $1,026,740.88 which is arrived at as follows :-

a)	agency fee	$303,313.66
b)	extraction fee	686,775.70
c)	commission paid - subcontractor	36,651.52
		$1,026,740.88

The Special Commissioners found that in ascertaining the adjusted income of respondent from timber operations for the relevant year of assessment three sums, namely :-

i)	Development cost	$158,000.00
ii)	Planting payments	201,000.00
iii)	Commission	140,175.54

paid by respondent to the society, were not outgoings or expenses wholly and exclusively incurred in the production of gross income of the respondent under section 33(1) of the Income Tax Act, 1967. They said the sums were in fact paid for the use of the licence or permit to extract timber within the meaning of section 39(1)(g) of the said Act and should not, therefore, be allowed as deductions. They also expressed the view that the three sums were paid to the society as consideration for assignment of the rights and privileges under the timber licence. Accordingly, they ordered (1) that the assessment of income tax in respect of the respondent for the year of assessment 1969, as contained in the notice of additional assessment dated 17th July, 1971, be amended and (2) that the assessment of income tax in respect of the year of assessment 1969, as contained in the notice of additional

assessment dated 8th December, 1973, be confirmed.

The question of law for the opinion of the High Court is whether on the evidence the Special Commissioners have reached a correct decision in law. The learned Judge held that the Special Commissioners were erroneous in points of law in arriving at their determination on both issues. Therefore, he held that :-

1) the sum of $303,313.66 described as "agency fee" is not assessible as timber profits tax under section 20 of the Supplementary Income Tax Act, 1967 (Act 54); and

2) the two sums of $158,000.00 and $201,000.00 described as "development cost" and "planting payments" respectively, are outgoings and expenses wholly and exclusively incurred in the production of gross income of respondent company and, therefore, deductible under section 33(1) of the Income Tax Act, 1967 (Act 53).

However, the learned Judge confirmed the decision of the Special Commissioners in respect of the sums of $36,651.52 described as "commission paid to sub-contractor" and $140,175.54 described as "commission paid to the society". Hence, the parties appealed.

As regard the first issue whether the sum of $303,313.66 which respondent claimed to be "agency fee" was so or not would depend upon the facts of the particular case. The Special Commissioners are Judges of facts and entitled to look at the surrounding facts and circumstances. See Shadford (H.J. Inspector of Taxes) v. H.Fairweather & Co.Ltd. 43 T.C. 291 and Eames (H.M.Inspector of Taxes) v. Stepnell Properties Ltd. 43 T.C.678 They found as a fact that respondent company did not carry out an agency business. The terms of the "agreement for timber export" (page 183 of Appeal Record) do not seem to be compatible with an agency agreement. Instead of the agent getting his commission and paying the proceeds to the principal the agent seemed to keep the proceeds while the principal received the commission.

The learned Judge quite rightly pointed out that the Special Commissioners accepted the contention of the appellant that the two agreements of 13.6.67 were designed for the purpose of avoiding tax and should, therefore, be treated as one as providing for one continuous process of activity of extracting and selling timber. But, he considered the Special Commissioners to be wrong, whether this was an inference of fact or law. He thought that the two agreements provided for different contracts of service and they were not inter-related as each was capable of existing by itself. He stated that there was no timber licence and it was wrong to assume there was. Even if there was such a licence he said that there was no evidence to show that rights under the licence were conferred on the respondent by the agreement. For these reasons he held that the inference drawn by the Special Commissioners on the assignment of rights under the licence was not supported by evidence.

The Special Commissioners found as a fact that the process of extraction and sale of the timber were in fact one continuous operation. It must be kept in mind that the Special Commissioners have before them not only the exhibits but also oral evidence. For however genuinely the agreements may have been drawn up by those responsible, evidence may show that in fact they do not truly indicate the nature of the relevant operations. Just because respondent called the sum "agency fee" it does not necessarily mean that the Special Commissioners must accept it to be such.

I think the learned Judge was wrong to disturb the finding of the Special Commissioners on facts which were admitted and proved. One of these facts is that the society was granted a timber licence by the State Government with the rights to extract timber. The land was granted to the society for the purpose of agricultural development. A person may be granted a piece of land under the Land Ordinance but that does not entitle him to extract and sell timber from the land without a proper licence to be issued under section 24 of the Forest Enactment, 1968. Perhaps, no such licence would be necessary if he cuts the timber for his own use on the land. But, if he cuts and sells or exports the timber

from the land without a proper licence he would be committing an offence under section 20 of the Forest Enactment.

There can be no dispute that the society held a timber licence issued under the Forest Enactment, 1968. Clause 5 of the "first agreement" (page 171 of the Appeal Record) provides that :-

> "The Contractor's operations under this Agreement shall be conducted with due regard to the law, the conditions of the grant of the land to the Society and of the timber licence for the extraction of timber and any instructions given by the conservator of Forests or his officers, and the Contractor shall indemnify the Society against any breaches thereof and against any claims for damage or injury done to any person or property in the undertaking of its operations under this Agreement."

In short, the contractor (i.e. respondent) must not breach the conditions of the grant of the land to the society and also the conditions of the timber licence for extraction of timber granted to the society. He was also to obey the instructions of the Conservator of Forests or his officers. If there was no timber licence there was no necessity to drag in the Conservator or his officers. Again, Clause 8 of the "second agreement" (page 177 of the Appeal Record) is word for word the same as Clause 5 above. Further, Clause 9 of the agreement between respondent and Yong Brothers (page 185 of the Appeal Record) also provides that the sub-contractor, i.e. Yong Brothers should conduct the operations with regard to the conditions of the licence to extract and remove timber and were to obey instructions of the Conservator of Forests or his officers. It is difficult to see how any person could extract and sell timber without a proper licence under the Forest Enactment, 1968. Even counsel for respondent conceded that if a licence was issued it was only for the purpose of removal. That is not all. The accountants for respondent in reply to appellant's letter stated quite clearly in paragraph 10 (page 188 of the Appeal Record) as follows :-

> " Copy of Licence under which timber is cut or extracted is not available in this office; it is with the Ulu Tungku Timber Co-operative Land Development

Society Limited of Lahad Datu."

Under the two agreements the society, for monetary consideration, gave respondent the rights "to fell and cut timber" on the land and then "to sell and export" all timber extracted from the land. Respondent could only do these under the timber licence of the society. In this sense it can be said that the society has assigned the rights under the timber licence to respondent. One of the objects of respondent as stated in their Memorandum of Association (page 132 of the Appeal Record) was clearly :-

> "(MM) To acquire and take over the timber extraction contract now being carried on in Mukim TUNGKU, LAHAD DATU by virtue of an Agreement dated 6th September, 1966 and made between the ULU TUNGKU CO-OPERATIVE LAND DEVELOPMENT SOCIETY of Tungku, Lahad Datu of one part AND DATO DONALD STEPHENS AND MAJID KHAN of the other part with a view thereto to adopt that Agreement and all or any of the assets and liabilities therein."

The object is clear. Respondent has stepped into the shoes of the society in connection with timber extraction and were to assume all assets and liabilities. The Special Commissioners quite properly pointed out that the agreement dated 6.9.66 was not produced. Also, respondent did not make any formal resolution adopting the said agreement. However, before the Special Commissioners, Majid Khan testified that respondent was incorporated solely for the purpose of adopting the said agreement. But what were the arrangements embodied in that agreement? It was for respondent to produce the agreement as they were a party to it. Respondent cannot complain if an adverse inference was drawn. The respondent was incorporated on 10.12.66. Nothing can be clearer than the objects mentioned earlier in their Memorandum of Association. Without acquiring the rights of the society under the licence respondent could not extract and sell the timber. Neither could respondent enter into the agreement with Yong Brothers.

This brings me to the second issue concerning the three sums, namely, $158,000.00 (development cost), $201,000.00 (planting Payments) and $140,175.54 (fixed commission).

In ascertaining the adjusted income of respondent, the Special Commissioners found that the three sums were not expenses wholly and exclusively incurred in the production of gross income of respondent under section 33(1) of the Income Tax Act, 1967. They said the three sums were paid for the use of the licence or permit to extract timber within the meaning of section 39(1)(g). The learned Judge disagreed with the findings of the Special Commissioners in respect of the first two sums. He considered that the third sum (fixed commission) should be treated differently and held that this sum was clearly a payment made to the society for the exclusive purpose and, therefore, not deductible. Although appellant agreed that the learned Judge was right in disallowing this sum he was not in entire agreement with the reasoning of the learned Judge. Appellant contended that this sum should be treated in the same manner as other two sums. On the other hand, respondent submitted that regarding the development cost there was already a liability to incur the expense to undertake works under clause 5 of the agreement for timber extraction. It was deductible regardless of the expenditure having been incurred. The liability had arisen and not contingent. F.C.T. v. James Flood Pty Ltd. 5 A.I.T.R. 579 was cited in support. With regard to the planting payments and fixed commission it was contended that these sums were held by respondent as agent on behalf of the society. The planting payments were to be paid to any contractor authorised by the society and approved by the Director of Agriculture under clause 9(1) of the agreement for timber extraction. The fixed commission was to be paid to the Society. It was submitted that the two sums were not the income of respondent and, therefore, not taxable as their income. Appellant pointed out that there was no evidence to show that these sums had actually been received by the society. Neither had actual planting been carried out to justify the planting payments. The Special Commissioners had examined all the exhibits and seen and heard the witness before they made their finding. The taxpayer and the Revenue had made their points. The Special Commissioners had considered their points and came to a certain conclusion. It would be a fallacy to say that the Special Commissioners must swallow everything a taxpayer says. As Croom-Johnson, J. said in Smart v. Commissioners of Inland Revenue 29 T.C. 338 and 344 at page 344 :-

"....when the Commissioners have the evidence, not only are they not bound to swallow every word of it - that would indeed not be exercising a judicial function at all - but they have the further duty in a proper case of drawing those inferences from all the facts and circumstances before them which will enable them to come to what they think is a right and just conclusion."

The learned Judge was of the view that the Special Commissioners had misdirected themselves in the interpretation of section 20 of the Supplementary Income Tax Act, 1967 (Act 54) and the application of section 39(1)(g) in relation to section 33(1) of the Income Tax Act, 1967 (Act 53) and in so doing they had arrived at wrong conclusion. The submission of appellant is that the Special Commissioners had not misdirected themselves but had applied the law correctly to the facts as found by them. Whether the payments were paid for the use of licence or otherwise is a question of fact. The Special Commissioners were entitled to look at the surrounding facts and circumstances in determining the nature of these payments. Respondent maintained that the Special Commissioners had completely misunderstood the law. His contention is that section 39(1)(g) would only arise if the outgoing or expenses fall within section 33(1). If not, that is the end of the matter and section 39(1)(g) would have no application. Whether the sums are allowable deductions would depend on whether they are outgoing or expenses wholly and exclusively incurred in the production of gross income within the meaning of section 33(1). Even if they are allowable deductions under section 33(1), the court would have to decide whether or not the sums are disallowed under section 39(1)(g) being sums payable for the use of a licence to export timber. In respect of the fixed commission the Special Commissioners found as a fact that this sum was paid for the use of the licence and, therefore, should be disallowed under section 39(1)(g). The onus is on respondent to show that this payment is not made for the use of the licence. He has failed to do so. Despite the fact that the preamble of the agreement for timber extraction expressly stated that respondent was to sell the timber on behalf of the society the facts of the case

indicated respondent was in fact the principal and the society the agent. For otherwise why should respondent pay the society fixed commission if it was not for the use of the licence to extract timber.

The preambles of both agreements are the same in that both state clearly that the society had been granted state land of approximately 4364 acres for purpose of agricultural development "with rights to extract and sell timber on the land and apply the proceeds thereof for development of the land." For all practical purposes the society had assigned the rights to respondent in consideration of certain monetary payments. In other words, respondent had stepped into the shoes of the society to do everything the society was supposed to do. Clause 2(2) of the "second agreement" says that the contractor "shall pay for the timber extracted and delivered to the log pond as may be due to any contractor from the society". The meaning is uncertain. Also, the price is not specified. Clause 3 states that it "shall be the duty of the contractor to find the best markets for the sale and export of the timber and to negotiate with buyers for the best price either in the name of the society or in the name of the contractor." Since the contractor was charged with the only duty to find the best markets for sale of timber and to negotiate for the best price, it is at least equivocal whether the contractor was retained as a salesman and, therefore, and agent or whether had had taken over, on payment, the ownership of the timber. The duty to find the best price for the purpose was presumably to ascertain the amount due to the society. Under Clause 5 the contractor was to execute works specified in the Schedule at a cost not exceeding $632,000.00. But again it is uncertain whether the costs of the works were to be paid by the society as employers to the contractor or to be paid for by the contractor as part of the consideration for working the timber concession. Clause 9(1) says the contractor shall pay to the society a sum of 6587,000.00 assessed and required for planting 1724 acres and for maintenance, in instalments, so that the payment in any one year shall not exceed $198,000.00. But why? The District Officer's letter (see page 218 of Appeal Record) makes clear in paragraph 10 that the society has to deposit 75% of the timber profits in a special account with the Chartered Bank to be used for

cultivation of the land and ancillary development works and the remaining 25% in a special maintenance account to be used for maintenance of the planted area. As the society had engaged a contractor to do all the works it would have to ensure the timber profits be so deposited. If it had assigned the benefits of the licence to another party, it would have to ensure that the assignee complied with this requirement, unless, of course, the requirement is a dead letter, as it would seem to be so. If it is not so, then why were the two agreements not shown to ensure compliance with the term of the licence said to be issued by the District Officer? I cannot see how a District Offier could issue a timber licence under the Forest Enactment, 1968.

I am inclined to accept the view of the Special Commissioners that the society had assigned the rights to respondent as correct on the facts. Otherwise, there was no reason for respondent to assume control of the whole assets and liabilities as stated in their Memorandum of Association. The control was directed to the realization of the society's timber concession and undertaking in respect of agricultural development. There is no evidence that respondent has divested or passed the control to the society. If the divesting or passing of control had taken place, then respondent, having made certain deductions, should not retain such deductions in their own hands. In the first place the deductions should have been handed over. In the second place the society would have to account for the deductions if such deductions were handed over. The overall effect is that when such deductions were made, but not handed over, then the respondent would have to account for the retention of such deductions to the satisfaction of the Inland Revenue.

The provisions of section 33(1) and section 39(1)(g) were discussed in Director-General of Inland Revenue v. L.T.S. (1974) 1 M.L.J. 187, 188 and 189 which was also cited by the learned Judge. In that case Chang Min Tat, J., as he then was, in his usual lucid style, stated :-

> "Section 39 refers to deductions that are not allowed. Subsection (1) specified such deductions. They include in sub-section (g) any sum payable otherwise than to a State Government

for the use of a licence or permit. Sub-section (2) must with respect mean that the deductions allowed in section 33 as expenses wholly and exclusively incurred do not extend to the expenditure mentioned in sub-sub-sections 39(1)(a) to (g).

It therefore means that the sum paid by the taxpayer to the permit-holders is caught by subsection (1)(g) of section 39 and is not deductible.

It also means that the sum paid to the Government of the State of Kedah in respect of the royalties, is deductible under the relief provided in "otherwise than to a State Government" in this subsection, as rightly conceded by Revenue."

The question of commission paid by the taxpayer to the permit-holders necessitated the interpretation of section 39 in conjunction with section 33. It was held that the commission paid to the permit-holders was not deductible as it was caught by section 39(1)(g). Respondent paid the Sabah Government royalty amounting to $300,380.69. They were entitled to relief on this under section 39(1)(g). One does not pay for extraction of timber unless one holds a licence issued under the Sabah Forest Enactment, 1968. There is no provision in the Sabah Land Ordinance concerning payment of royalty. However, respondent could not claim for relief in respect of commission they paid to the society, the licence holder.

With respect, the learned Judge was wrong to interfere with the decision of the Special Commissioners as there was sufficient evidence to support their conclusion. The learned Judge, in exercising appellate jurisdiction, was not supposed to alter conclusion of facts simply because he feels that on the evidence the Special Commissioners should not have arrived at the conclusion of facts they did. In Bracegirdle v. Oxley (1947) 1 All E.R. 126 and 127 Lord Goddard, C.J. made these observations :-

"It is, of course, said that we are bound by the findings of fact set out in the Case by the justices, and it is perfectly true that this court does

not sit as a general court of appeal against justices decisions in the same way as quarter sessions, for instance, sit as a court of appeal against the decisions of courts of summary jurisdiction. In this court we only sit to review the justices' decisions on points of law, being bound by the facts which they find, provided always that there is evidence on which the justices can come to the conclusions of fact at which they arrive."

The House of Lords in Edwards (H.M. Inspector of Taxes) v. Bairstow & Harrison 36 T.C. 207 accepted that the inference of "trade" or "no trade" in a particular case was a question of fact but pointed out that the question of what the statute means by "trade" is a question of law. The learned Judge considered that the Special Commissioners were wrong in their conclusion of fact. The question is whether their decision was unreasonable. The learned Judge cannot disturb the finding of facts by the Special Commissioners however strongly he may have felt. In Leeming v. Jones (H.M. Inspector of Taxes) 15 T.C. 333 Rowlatt, J. remitted the case to the General Commissioners for a finding whether there was or was not a concern in the nature of trade. The case came back to him and he gave judgment in favour of appellant and respondent appealed. Although Rowlatt, J. disagreed with the finding of the Commissioners he did not disturb their finding. Thus, Lord Hanworth, M.R. said at page 346 :-

"...I think he was right, for however strongly one may feel as to the facts, the facts are for the decision of the Commissioners. It would make an inroad upon their sphere if one were to say in a case such as the present that there could only be one conclusion. The Commissioners are far better judges of these commercial transactions than the Courts, and although their attention has been drawn to what happened, they have in their final Case negatived anything in the nature of an adventure or trade."

As Lord Radcliffe said in Edward's case 36 T.C. 207 at page 228 :-

"I see nothing more than this in anything that was said in this House in

Leeming v. Jones 15 T.C. 333. The only thing that I would deprecate is too much abbreviation in stating the question as by asserting that it is simply a question of fact whether or not a trade exists. It is not simply a question of fact. The true clue to the understanding of the position lies, I think, in recalling that the Court can allow an appeal from the Commissioners' determination only if it is shown to be erroneous in point of law."

He concluded this judgment in these words:-

"As I see it, the reason why the Court do not interfere with Commissioners' findings or determinations when they really do involve nothing but questions of fact is not any supposed advantage in the Commissioners of greater experience in matters of business or any other matter. The reason is simply that by the system that has been set up the Commissioners are the first tribunal to try an appeal and in the interests of the efficient administration of justice their decisions can only be upset on appeal if they have been positively wrong in law. The Court is not a second opinion, where there is reasonable ground for the first. But there is no reason to make a mystery about the subjects that Commissioners deal with or to invite the Courts to impose any exceptional restraints upon themselves because they are dealing with cases that arise out of facts found by Commissioners. Their duty is no more than to examine those facts with a decent respect for the tribunal appealed from, and, if they think that the only reasonable conclusion on the facts found is inconsistent with the determination come to, to say so without more ado."

However much one may disagree with the decision of the Special Commissioners one must accept their finding of facts. Where they made finding of primary facts it is not open to the High Court to challenge their accuracy. As Raja Azlan Shah, F.J. in U.H.G. v. Director-General of Inland Revenue (1974) 2 M.L.J. 33 and 37 rightly pointed out :-

"But where there is evidence to consider, the decision of the Special Commissioners is final, even though the court might not, on the materials, have come to the same conclusion. In treating the question I can desire no more apt exposition of the law than what is contained in Lord Atkinson's speech in Great Western Railway Co. v. Bater (1928) 8 T.C. 231, 244 :-

> 'Their (Commissioner's) determination of questions of pure fact are not to be disturbed, any more than are the findings of a jury, unless it should appear that there was no evidence before them upon which they, as reasonable men, could come to the conclusion to which they have come: and this, even though the Court of Review would on the evidence have come to a conclusion entirely different from theirs.' ".

For reasons given, I do not think it can be said that on the evidence the Special Commissioners have come to a wrong decision in law. Accordingly, I would allow the appeal of the appellant with costs and dismiss the appeal of the respondent with costs. Deposit to respondent on account of taxed costs.

(Sgd) Lee Hun Hoe
Chief Justice
Borneo

Kota Kinabalu,
29th December, 1977.

Notes:

Judgment delivered by Lee Hun Hoe, C.J.(Borneo) Ong, F.J. and Ho, J. concurred.

Hearing on Monday, 3rd October, 1977.

Counsel:

Encik Alauddin bin Dato' Mohd. Sheriff for appellant. Senior Federal Counsel.

Datuk Thomas Jayasuriya for respondent. Messrs. Jayasuriya, Kah & Co.

Certified true copy:
Sgd.
(Puan Valerie Kueh)
P.A. to Chief Justice (Borneo)
5th January, 1978.

In the Federal Court of Malaysia

No.7

Order of the Federal Court

29th December 1977

No. 7

ORDER OF THE FEDERAL COURT

CORAM:-

LEE HUN HOE, CHIEF JUSTICE, HIGH COURT IN BORNEO;

ONG HOCK SUM, JUDGE, FEDERAL COURT, MALAYSIA;

CHARLES HO NYEN CHEUNG, JUDGE, HIGH COURT, BORNEO.

IN OPEN COURT

THIS 20TH DAY OF DECEMBER, 1977

O R D E R

THIS APPEAL coming on for hearing on the 3rd day of October, 1977 in the presence of Encik Alauddin bin Dato' Mohd. Sheriff, Senior Federal Counsel on behalf of the Appellant and Datuk Thomas Jayasuriya of Counsel for the Respondent AND UPON READING the Record of Appeal herein AND UPON HEARING Counsel as aforesaid IT WAS ORDERED that this Appeal do stand adjourned for Judgment AND the same coming on for Judgment this day in the presence of Counsel for the Appellant and Counsel for the Respondent. IT IS ORDERED that this Appeal be and is hereby allowed. AND IT IS ORDERED that the Respondent do pay to the Appellant the costs of this Appeal as taxed by the proper officer of theCourt.

AND IT IS LASTLY ORDERED that the Deposit of $500/- (Ringgit Five Hundred) paid into Court by the Appellant as security for costs of this appeal be paid to the Respondent on account of taxed costs

GIVEN under my hand and the seal of the Court this 29th day of December, 1977.

CHIEF REGISTRAR,
FEDERAL COURT,
MALAYSIA.

No. 8

ORDER GRANTING FINAL LEAVE TO APPEAL TO HIS MAJESTY THE YANG DI-PERTUAN AGONG

In the Federal Court of Malaysia

No.8

Order granting Final Leave to Appeal to His Majesty the Yang Di-Pertuan Agong

10th July 1978

CORAM:- GILL, CHIEF JUSTICE, HIGH COURT, MALAYA:
SYED OTHMAN, JUDGE, HIGH COURT, MALAYA:
ABDUL HAMID, JUDGE, HIGH COURT, MALAYA.

IN OPEN COURT

THIS 10TH DAY OF JULY 1978

O R D E R

UPON MOTION made unto Court this day by Encik R.T.S. Khoo of Counsel for the Respondent abovenamed in the presence of Encik Zulkifli bin Mahmood, Senior Federal Counsel for the Appellant abovenamed AND UPON READING the Notice of Motion dated the 6th day of June 1978 and the Affidavit of Encik S.Woodhull affirmed on the 6th day of June 1978 and filed herein AND UPON HEARING Counsel as aforesaid IT IS ORDERED that final leave be and is hereby granted to the Respondent abovenamed to appeal to His Majesty the Yang Dipertuan Agung from the decision of this Court given on the 29th day of December 1977.

AND IT IS ORDERED that the costs of and incidental to this application be cost in the cause.

Given under my hand and the seal of the Court this 10th day of July 1978.

Sgd.
CHIEF REGISTRAR,
FEDERAL COURT,
MALAYSIA.

No.28 of 1978

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

O N A P P E A L

FROM THE FEDERAL COURT OF MALAYSIA

B E T W E E N :

LAHAD DATU TIMBER SENDIRIAN BERHAD — Appellant

- and -

THE DIRECTOR-GENERAL OF INLAND REVENUE — Respondent

RECORD OF PROCEEDINGS

SLAUGHTER AND MAY,
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London, EC2V 5DB

Solicitors for the Appellant

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London, EC2V 6BS

Solicitors for the Respondent