No. 19 of 1982

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

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O N A P P E A L

FROM THE FEDERAL COURT OF MALAYSIA
(Appellate Jurisdiction)

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B E T W E E N :

THE RIVER ESTATES Sdn. Bhd. — Appellant

- and -

THE DIRECTOR GENERAL OF INLAND REVENUE — Respondent

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# CASE FOR THE RESPONDENT

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1. This is an appeal from the judgment and order of the Federal Court of Malaysia (Lee Hun Hoe, C.J. Borneo, Syed Othman, F.J. Hamid, F.J.) dated the 8th September 1980 dismissing an appeal by the Appellant from an Order of the High Court in Borneo (Datuk B.T.H. Lee, J.) dated 18th January 1980 dismissing an appeal by the Appellant from a Deciding order of the Special Commissioners of Income Tax dated the 28th August 1976 by which Order the Special Commissioners determined that the Appellant was carrying on three businesses and had five separate sources of income during the years of assessment 1968 to 1972 inclusive. p. 76 p. 41 p. 9

2. The question in issue is whether the Appellant is entitled for the said years 1968 to 1972 to set off capital allowances and plantation allowances due under Schedule 3 of the Income Tax Act 1967 of Malaysia against its total business income. The Appellant contends that it is so entitled because its activities together constituted a single business. The Respondent contends that the Appellant is not so entitled because the Appellant had at least two

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separate sources of income consisting of at least two separate businesses. Capital allowances and plantation allowances given in respect of a particular business can be set against and only against income from that particular source consisting of business. Allowances not utilised against income from that particular source consisting of a business cannot be set against income from a different source consisting of a different business.

3. It is not disputed that in the years 1968 to 1972 inclusive the Appellant owned the following five estates on which it carried on the activities briefly described in
p. 9 the Deciding Order of the Special Commissioners and summarised below. Bode Estate is excluded from the summary because the Appellant disposed of it in 1955.

(i) Litang Estate

This had a total area of 4,700 acres of which 1,000 acres were planted with rubber. The balance of 3,700 acres was virgin jungle reserve. Logging operations were commenced in 1950 in the jungle reserve and part of it was planted with rubber, cocoa and oil palms.

(ii) Dagat

In 1952 the Appellant began to carry out timber logging in a virgin jungle area at Dagat. No specific area was allotted to the Appellant but the Appellant logged between 2 to 3 square miles per year. In the year 1967 the Appellant applied for alienation of 10,000 acres in this area for the purposes of banana growing. This application was turned down, and the Appellant is still carrying on timber operations in this area.

(iii) Malubok Estate

This was acquired by the Appellant in 1959. It had a total area of 3,960 acres of largely jungle land. By the end of 1962 the Appellant had logged 1,500 acres and planted up 600 acres with cocoa and 100 acres with rubber. Flooding in 1963 destroyed 600 acres of the newly planted area. Subsequently the area was abandoned after extraction of all valuable timber from it.

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(iv) Tomanggong Estate

This was acquired in 1961 and had a total area of 10,025 acres. Extraction of timber commenced in 1962 and was followed by the planting of oil palms. The Appellant also acquired from the Sabah State Government an adjoining area of 6,454 acres of de-timbered land and planted it with oil palms. By 1975 the Appellant had planted up a total area of 8,382 acres with oil palms.

(v) Tenggara

The Appellant was contracted to log for the Borneo Timber Company in this area. The Appellant was paid at a fixed rate per cubic foot of logs delivered to the North Borneo Timber Company. This contract terminated in 1969 when the latter company ceased logging in that area.

4. On the foregoing facts and on the findings of fact set out in paragraph 7 of the Case Stated the Special Commissioners found that :-

(i) The Appellant's operations at Litang Estate, Tomanggong Estates and Malubok Estate constituted a single business and that each estate was a separate source of income. p.23

(ii) The Appellant's timber operations at Dagat constituted another separate business and was another source of income. p.24

(iii) The Appellant's contract to log for the North Borneo Timber Company at Tenggara constituted another separate business and was another source of income. p.24

5. The decision of the Special Commissioners was upheld by the Honourable Justice Datuk B.T.H. Lee in the High Court. The decision of the Special Commissioners was upheld with a variation by the Federal Court. The Federal Court agreed with the Special Commissioners in finding that the Appellant had five separate sources of income, but it differed from the Special Commissioners in one particular. Namely, by its finding that the Appellant's timber operations at Dagat and Tenggara constituted a single business whereas the p.30 p.75

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Special Commissioners had regarded them as two separate businesses.

6. The Respondent submits that there was ample evidence upon which the Special Commissioners could reach their conclusion that the three estates known as Litang, Tomanggong and Malubok together constituted a single "plantation" business to be distinguished from the timber operations carried on elsewhere. The three plantation estates mentioned had much in common in that they were all estates where initially the land was cleared by logging operations and subsequently planted variously with oil palms, cocoa and rubber. The plantation activities were completely different from the two separate timber operations carried on by the Appellant, each of which differed from the other. One of these operations was at Dagat where the Appellant owned no specific area of land. Purely timber-logging operations were carried on at Dagat by the Appellant on its own account under an annual licence between 1952 and 1957 and subsequently under a 21-year licence which permitted only timber extraction. Unlike the three plantation estates mentioned above the timber land at Dagat did not belong to the Appellant and use for agricultural purposes on that land was expressly prohibited. Different again were the activities of the Appellant at Tenggara, where the Appellant logged not on its own account but under contract for the Borneo Timber Company. The Appellant acted as agent and cut timber for a fee from the Borneo Timber Company.

7. The decision of the Special Commissioners to regard the three plantation estates and the two timber activities (one of logging on its own account and one for a fee as a logging contractor) as three businesses each separate and distinct from the other cannot be overruled unless it was a decision which no reasonable Commissioners properly directed as to the law could have reached. Applying this test, being that laid down in Edwards v. Bairstow & Harrison [1956] AC 14 the Respondent submits that the decision of the Special Commissioners insofar as it distinguishes the plantation estates from the timber activities ought to be upheld. The question whether a number of activities constitute a business or several businesses is a question of fact as is established by the decision in Scales v. George Thomson Limited (1927) 13 Tax Cas. 83. In Rolls Royce Motors Limited v. Bamford (1976) 51 Tax Cas. 519 Mr.

Justice Walton recognised that the question whether a trade was a new trade was one of fact (at page 186h). Yet he would himself have drawn from the facts the inference that the six divisions into which the trading activities of Rolls Royce Limited were divided constituted six separate trades (at page 183d).

8. In the Respondent's submission there is nothing in the decision of the Privy Council in American Leaf Blending v. Director General of Inland Revenue /1979/ AC 670 which casts any doubt upon the correctness of the decision of the Federal Court or of the Special Commissioners. The decision in American Leaf Blending establishes two propositions only. Namely, that the five paragraphs in Section 4 of the Income Tax 1967 which specify the five classes of income in respect of which tax is chargeable under that Act are not mutually exclusive. Also, that the letting of property can be the carrying on of a business within the meaning of Section 43 of the Income Tax Act 1967. The American Leaf Blending case was dealing with the uses to which the taxpayer company could put brought-forward trading losses. As the High Court and the Federal Court make clear in their judgments, American Leaf Blending did not address the question of capital allowances. As is pointed out in the judgment of the Federal Court the taxpayer company's claim to utilise the balance of unabsorbed capital allowances in American Leaf Blending was decided against the taxpayer in both the High Court and the Federal Court. The claim was subsequently abandoned in relation to capital allowances and this aspect of the matter was not argued in the Privy Council.

10. What the Appellant in its submissions to the Federal Court called "the principle of aggregation" of income under Section 43 of the Income Tax Act 1967 does not universally apply to capital allowances or plantation allowances. The aggregation directed by Section 43 is an aggregation of "statutory income" as defined in ibid Section 42. Broadly "statutory income" is defined to mean "adjusted income", to which is added balancing charges but from which is deducted any capital allowance. "Adjusted income" is in turn defined by ibid Section 33 to mean trading income, which is computed without deducting capital expenditure (ibid Section 39 (1) (c)). It follows that "aggregate income" is determined after adding to trading income balancing charges and deducting therefrom any capital allowances.

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11. The same principle does not hold good when capital allowances in a particular business exceed trading profits. As is emphasised by the decision of the Privy Council in American Leaf Blending, supra, at page 682A it is only "adjusted losses" that are set against the taxpayer's aggregate income. And "adjusted losses" are defined by Section 40 of the Income Tax Act 1967 to mean losses of an income nature. Computation of such losses does not take into account any allowances for capital expenditure. This is shown by the fact that Section 40 refers to the total of deductions "allowed under the foregoing provisions of this chapter". Those provisions do not include capital allowances and expressly exclude capital expenditure (Section 39 (1) (c)). Further support for this conclusion may be derived from the fact that to arrive at "statutory income" it is necessary under Section 42 to add to or subtract from "adjusted income" the amount of any balancing charges or capital allowances.

12. Capital allowances and plantation allowances are given by Schedule 3 to the Income Tax Act 1967. Paragraph 10 of that Schedule expressly provides that allowances for business expenditure shall be made "in relation to the source consisting of that business". Similar express provision is made in Schedule 3 paragraphs 15, 22 and 23. In the submission of the Respondent it would be odd if despite these express statutory provisions allowances were available to be used against all categories of income. In the face of those provisions the use of allowances given in one business cannot without express provision to that effect be used against the profits of other businesses. The Respondent contends that Sections 43 and 44 far from making such express provision are explicit and unambiguous in excluding capital allowances and plantation allowances from being used in the same way as business losses of a Revenue nature could be used.

13. The Respondent therefore submits that the decision of the Special Commissioners was correct and should be affirmed for the following among other :-

R E A S O N S

1. BECAUSE the Appellant was carrying on three separate businesses and was deriving income from five sources.

2. BECAUSE all the activities of the Appellant did not together constitute a single business.

3. BECAUSE the Special Commissioners directed themselves correctly in law and the decision which they reached was correct on the basis of the primary findings of fact.

4. BECAUSE capital allowances are available against a source consisting of a business and allowances given in relation to one business and not wholly relieved against the profits of that business cannot be set against profits in another business carried on by the same taxpayer.

STEWART BATES Q.C.

S.A. ALLCOCK

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BETWEEN:

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Sdn. Bhd. Appellant

- and -

THE DIRECTOR GENERAL OF
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# CASE FOR THE RESPONDENT

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