35/85

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL NO. 43 of 1983

ON APPEAL FROM THE FEDERAL COURT OF MALAYSIA

B E T W E E N:-

MAMOR SENDIRIAN BERHAD — Appellant

and

THE DIRECTOR-GENERAL OF INLAND REVENUE — Respondent

CASE FOR THE APPELLANT

Page in Record

1. This is an appeal from the decision of the Federal Court of Malaysia held at Johore Bahru dated 14th May 1982 (Wan Suleiman, Ag. C.J. syed Othman and Abdul Hamid, F.J.J.) which allowed an appeal by the Respondent from the decision of Mr. Justice Annuar dated 29th November 1979 allowing the Appellant's appeal from the decision of the Special Commissioners of Income Tax contained in a case stated dated 11th April 1977. pp. 47-55 pp. 31-40 pp. 1-3 pp. 4-30

2. The notices of assessment appealed against are as follows:- pp. 64-66

Year	Income Tax	Timber Profits Tax	Development Tax	Tax	
1971	$ 54,466.40	17,850.40	6,808.30	79,125.10	p. 64
1972	86,334.00	9,289.70	10,791.75	106,415.45	p. 65
1973	100,000.00	-	12,500.00	112,500.00	p. 66

The total tax payable for 1973 was later reduced to $30,835.05 by the issue of a Reduced Assessment dated 21st December 1974. p. 67

3. The issue in this Appeal is whether the Special Commissioners were correct in their decision that the Appellant derived income from timber operations on land in the district of Kluang during the years under appeal or whether the transactions in question were partial

realizations of a capital asset and accordingly not taxable as income.

4. The Appellant was incorporated under the Companies Act 1965 on 14th May 1968 as a private limited company. In 1968 the Johore State Government was contemplating a scheme for the alienation of State land to the private sector for development purposes. In August 1968 the Government announced that it would on application alienate on 99 year leases 42,000 acres of virgin jungle land in the district of Kluang and 7000 acres of Government land at Sungei Pangoli to the private sector for oil palm development and that each successful applicant would be given 7000 acres for such development. Successful applicants would be required to surrender 1500 acres of the 7000 acres when fully planted for the purpose of reallocating that acreage among smallholders.

5. The Appellant applied for an alienation of land and was informed by a notice dated 30th November, 1968 that its application had been successful. The Appellant was allotted a parcel of virgin land described as Block 6 comprising approximately 7000 acres in the Mukim of Niyor in the district of Kluang, Johore for development into an oil palm plantation subject to various terms and conditions stipulated in the notice. These included provisions that the Appellant would be given the right to extract timber from the land and would be required to enter into an agreement with the State Government to do so. In the event of the Appellant failing to remove any tree the Appellant undertook to pay on demand by way of compensation a sum not exceeding $20 per tree. pp. 97-98

6. On 2nd June 1969 Block 6 was alienated to the Appellant. In doing so the Government departed from normal practice which was to alienate only de-timbered land for development purposes. The departure from normal practice was intended to accelerate the oil palm development scheme. On 3rd January 1970 the Appellant entered into an agreement with Syarikat Kilang Papan Low Nam Hui Sdn. Bhd (hereinafter called "the Contractor") under which the Contractor would extract the marketable timber and deliver it to a stockpile. The first logging licence was applied for and obtained in April 1970 and logging operations began on 20th July 1970. pp.104-10

Page in Record

7. The Appellant had no experience in the timber market and appointed Pan-Singapore Timber Enterprise Company of Singapore as its agents to find buyers for the cut timber. Buyers sent their lorries to the stockpiles and removed the timber to Singapore, the Appellant receiving an agreed sale price less transport charges, export duty and related expenses. Not all timber delivered to the stockpiles was sold. Unsuitable timber was left in the stockpiles.

8. By December 1972 2000 acres had been logged but not cleared or readied for planting oil palm. Substantial expenditure was incurred by the Appellant on further felling in early 1973. Thereafter development of the oil palm plantation commenced in earnest and by the time of the Special Commissioners' hearing in December 1973 all but 300 acres were planted with oil palm and the Appellant had surrendered to the State Government the agreed 1500 acres oil palm plantation intended for reallocation to smallholders. p.16,11. 46-51 & p.17 11 1-3

9. In respect of its receipts from the sale of timber the Appellant was assessed to income tax under Section 4 of the Income Tax Act 1967 and to timber profits tax and development tax under Section 16(1) and Section 20 of the Supplementary Income Tax Acts, 1967, respectively. Appeals against the assessments for the years 1971, 1972 and 1973 were heard by the Special Commissioners for Income Tax on 11th - 14th December 1976 when the assessments were upheld. pp.64-66 pp.68-70 p4.11 25-30

10. The Special Commissioners concluded that the Appellant was carrying on two different activities, namely the extraction and sale of timber and the development of the land into an oil palm plantation, and that in extracting the timber the Appellant was commercially exploiting it. As a result they concluded that the extraction and sale of the timber constituted the carrying on of a business of timber operators within the Income Tax Act 1967 section 4(a).

11. In the Appellant's contention the decision of the Special Commissioners is wrong in law because it equates the inference of fact that the Appellant carried on two separate activities with a conclusion of law that the Appellant's receipts from timber sales were of an income nature.

Page in Record

12. On the facts as found there can be no doubt that Block 6 was when acquired a capital asset of the Appellant. Under Section 5 of the National Land Code 1965, "land" is defined to include "all vegetation and other natural products ..... on ..... the surface". The Appellant did not acquire merely a right to fell timber, but acquired a proprietary interest in the land, which included the timber thereon. That the land was a capital asset is unambiguously shown by the fact that the Appellant retained it and proceeded to develop it as an oil palm plantation, as was found by the Special Commissioners at paragraph 7(xviii) of the Case Stated. p.16,11 38-51 & p.17,11 1-3

13. The realization of timber which forms part of a capital asset of the Seller is part of the normal occupation of woodlands and does not amount to a trade. (C.I.R. v. Williamson Brothers (1950) 31 Tax Cas 370). Moreover, the realization of that which was acquired as a capital asset does not produce trading income unless there is an appropriation of a capital asset to a pre-existing or distinct trade. (Taylor v. Good [1974] 1 W.L.R. 556). In the present case the Appellant had no pre-existing timber trade; nor did he commence such a trade. The Appellant acquired a capital asset part of which it realized in order to carry out its objective of developing an oil palm plantation.

14. The Special Commissioners have not found that the Appellant acquired Block 6 for the purpose of exploiting it as a timber plantation. In paragraph 11(viii)(d) they appear to regard the question of the Appellant's motive as irrelevant to the question whether there was a trade of the exploitation of timber. In the Appellant's submission this error of law on the part of the Special Commissioners has led them to omit a proper consideration of the Appellant's motives, which were to develop an oil palm plantation. In order to do so, the standing timber had to be cleared. p.28,11 24-45

15. That the Appellant organised the sale of timber on commercial lines is indicative only of common commercial prudence, and not of a trading motive. That the realization of a capital asset is accomplished by commercially-effective and businesslike methods does not call into question the quality of the asset as a capital asset. In Commissioner of Taxes v. British Australian Wool

Page in Record

Realization Association Ltd. [1931] A.C. 224 Lord Blanesburgh put the point as follows at page 252:-

> "Upon the facts stated, any other conclusion would be tantamount to saying that a realisation such as that effected by the Association must be a trade because of the bringing into existence of a selling organisation made necessary only by reason of the mere magnitude of the realization - a proposition not to be entertained."

In giving their reasons for their decision the Special Commissioners at paragraph 11(viii)(g) of the Case Stated have erred in applying the fallacious reasoning rejected by Lord Blanesburgh. p.29,11 22-42

16. The conclusion of the Special Commissioners that the Appellant engaged in two activities can be accepted as one way of looking at the activities of the Appellant in relation to Block 6. The Special Commissioners have erred in regarding that conclusion as a conclusive indication that the Appellant carried on a timber business giving rise to taxable income. The opening words of paragraph 11 (viii) of the Case Stated show that this is the approach adopted by the Special Commissioners. It is further illustrated by their conclusions at paragraphs 12 and 13 of the Case Stated. For the reasons given in paragraphs 12 to 15 hereof above, the Special Commissioners have asked themselves the wrong question and have incorrectly assumed that the answer to that question resolves the appeals. p.27,11 35-43 p.29,11 43-52 & p.30, 11 1-19

17. The Special Commissioners reveal by their decision that they have inextricably linked findings of fact with conclusions of law in a way which has recently been criticized by the Judicial Committee in Chua Lip Kong v. Director-General of Inland Revenue [1981] S.T.C. 653. Their findings that the Appellant carried on two activities cannot in the Appellant's submission be regarded either as a pure finding of fact or exclusively as one of law. Rather, the Special Commissioners appear to have regarded it as a compendious means of expressing a conclusion of both fact and law. In the Appellant's respectful submission if it is a conclusion of law it is wrong ex facie. If it is a finding of fact it does not justify the conclusion of law that the Special Commissioners have drawn from it and there is no other finding of primary fact to justify that conclusion.

18. On the facts as found the inference the Special Commissioners should have drawn was that the Appellant was interested only in establishing an oil palm plantation and had to realize the timber in order to prepare the land. And that the realization was the realization of part of a capital asset. Since the decision of the Special Commissioners is on its face wrong in law the Appellant respectfully submits that your Lordships should conclude on the basis of the facts as found that in cutting and selling the timber in Block 6 the Appellant was preparing the land for an oil palm plantation and not realizing trading stock or carrying on any trade or business.

19. AND the Appellant respectfully submits that the Appeal should be allowed for the following among other

REASONS

1. BECAUSE the Appellant was not carrying on a business of exploiting timber within the meaning of Section 4(a) of the Income Tax Act 1967.

2. BECAUSE the proceeds of sale of timber sold by the Appellant represented the proceeds of the partial realization of a capital asset.

3. BECAUSE the Case Stated by the Special Commissioners of Income Tax is on its face erroneous in point of law.

4. BECAUSE the fact that the cutting and selling of timber may have been in fact a separate activity does not justify the conclusion of law that it was a business producing profits liable to income tax.

5. BECAUSE the decisions of the Special Commissioners and of the Federal Court were wrong and ought to be overruled.

.....
Stewart Bates Q.C.

.....
Stephen Allcock

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CASE OF THE APPELLANT

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