IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

No. 31 of 1976

ON APPEAL

FROM THE FEDERAL COURT OF MALAYSIA

BETWEEN :-

Hock Heng Company Sdn. Berhad ... Appellant

AND

The Director-General of Inland Revenue ... Respondent

CASE FOR THE APPELLANT

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1. This is an appeal from the judgment of the Federal Court of Malaysia (Suffian, L.P. and Lee Hun Hoe, C.J., Borneo) dated the 19th January, 1976 dismissing an appeal by the Appellant from the judgment of the High Court of Malaya (Chang Min Tat, J.) dated the 11th July, 1975 allowing an appeal by the Respondent from an Order of the Special Commissioners of Income Tax dated the 19th day of September, 1973 which had allowed the Appellant's appeal against a notice of additional assessment to income tax dated the 16th May, 1970 in respect of the Year of Assessment 1968.

2. No evidence was adduced at the hearing before the Special Commissioners but the following were the facts agreed or admitted. pp. 12/13

(i) The Appellant is a company incorporated in Malaysia. It has a branch in Singapore through which it carries on its business through a "permanent establishment" in Singapore;

(ii) The Appellant is ordinarily resident in Malaysia under the provisions of the Income Tax Act 1967;

(iii) For the Year of Assessment 1968 the Appellant

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derived income from Malaysia in the sum of $31,415.00 and suffered a loss of $538,335.00 attributable to their business carried on through their Singapore branch;

(iv) The Double Taxation Relief (Singapore) Order 1966 (hereinafter referred to as the "Double Taxation Agreement, 1966") was by an amendment dated 9th August, 1973 made to remain effective up to and including the Year of Assessment 1968;

(v) Under paragraph 7 of Schedule 7 of the Income Tax Act 1967, the Appellant elected that bilateral credit shall not be allowed against Malaysian tax payable by them for the Year of Assessment 1968;

(vi) In ascertaining the Appellant's income for the Year of Assessment 1968 the Respondent has disallowed the Appellant's claims to have the Singapore loss of $538,335.00 set off against the income derived from Malaysia.

3. The issue which arises upon this appeal is whether or not the Singapore loss of $538,335.00 may be brought into account in computing the Appellant's income chargeable to Malaysian tax for the Year of Assessment 1968.

4. The relevant provisions of the Malaysian Income Tax Act 1967 and subsidiary legislation can be summarized as follows :-

Section 3 provides, in the case of a person ordinarily resident in Malaysia for the basis year for the year of assessment, for income to be assessed upon income from wherever derived. The charge is upon income in respect of "profits and gains from a business" as stipulated under Section 4(a), that is, in respect of profits and gains of the Appellant's rubber dealing business carried out in Malaysia and in Singapore. The profits and gains from that business are computed as a global amount representing profits less losses of the business wherever such profits and losses arise or are incurred.

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Section 5(2)(b) enables the ascertainment of any adjusted loss of a person from any source or sources that do not provide any gross income.

Section 132 authorises the Government of Malaysia to enter into Double Taxation Agreements with the Government of any territory outside Malaysia with a view to affording relief from double taxation and a statutory order to this effect made by the Minister in regard to these arrangements shall have effect in relation to tax under the Income Tax Act of 1967 and the provisions of Schedule 7 of the Act shall apply by virtue of Section 132(3) when such arrangements have been entered into by the Government.

Schedule 7 Paragraph 7 provides that bilateral credit shall not be allowed against Malaysian tax payable by a person for a year of assessment if he elects that credit shall not be allowed for that year.

Article IV(1)(a) Double Taxation Agreement, 1966, makes provision, inter alia, for tax to be imposed in Singapore on the income or profits of a Malaysian enterprise but only on so much thereof as it is attributable to that permanent establishment in Singapore.

5. At the hearing before the Special Commissioners, the Appellant contended that the basis of computation of income under the Income Tax Act, 1967 was one of a world income scope and that the losses in Singapore should be taken into account in ascertaining the Appellant's total Malaysian income for tax purposes, relief being granted only for taxes imposed on the income or profits of the permanent establishment in Singapore for the purposes of the Double Taxation Agreement, 1966.

6. The Special Commissioners held that Section 3(a) of the Income Tax Act, 1967 provides for the assessment of income tax on a person ordinarily resident in Malaysia upon his income from wherever derived, subject to and in accordance with the Act, and therefore in the ascertainment of the Appellant's total income for the Year of Assessment 1968 all profits and losses from wherever derived and incurred should be brought into account.

7. Upon the appeal of the Respondent to the High

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Court of Malaya, Chang Min Tat J gave Judgment as follows :-

> "For the reasons given in my judgment in Federal Court Civil Appeal No. 165/74 between United National Finance Berhad v. Director-General of Inland Revenue delivered by me on July 3, 1975, the deciding order of the Special Commissioners is set aside and I order that the assessment of income-tax in respect of the Respondent for the Year of Assessment 1968 as contained in the Notice of Additional Assessment dated May 16, 1970 be restored."

8. The facts and summary of the decision in regard to the United National Finance Berhad -v- The Director-General of Inland Revenue were set out in the Judgment of Lee Hun Hoe, C.J., Borneo, in this appeal before the Federal Court and may be stated as follows:

> "The taxpayer is a wholly-owned subsidiary of the United Malayan Banking Corporation Berhad which is a finance company. It commenced business in Malaysia in 1964 and its sister branch in Singapore in 1965. Up to 1969 it bought and sold shares in eleven companies both private and public. Some shares were sold at profits and others were transferred to its parent company and to the United National Finance (Singapore) Ltd., its sister branch in Singapore. The profits realised by the taxpayer were used in the course of its business as a finance company. It was contended that the profits which had been assessed to tax for the Year of Assessment 1968 and 1969 were capital gains and not trading income as the shares formed part of a holding which was purchased and held as investment. The Special Commissioners considered that in buying and selling shares the taxpayer was carrying on a business in dealing in shares as an adventure or concern in the nature of trade. They, therefore, held that the profits were assessable to tax under Section 4(a) of the 1967 Act. This was upheld by both Hamid J. and this court. In respect of the second limb the factum or quantum of loss sustained

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by the Singapore branch was not in dispute though the figure of losses was not disclosed. The Special Commissioners held that the taxpayer was entitled to deduct the Singapore losses from its income derived in Malaysia. Hamid J. considered that the Special Commissioners had erred in law as the net effect of their decision would result in the Singapore losses to be taken into consideration twice, once in Singapore and again in Malaysia. Chang Min Tat, J. agreed with this view and dismissed the appeal."

9. Upon the appeal of the Appellant to the Federal Court of Malaysia, Suffian L.P. and Lee Hun Hoe, C.J. Borneo delivered the Judgment of the Court. Suffian L.P. made no reference to the case of United National Finance Berhad -v- The Director-General of Inland Revenue. He took the view that Malaysian profits must be ascertained by deducting Malaysian losses from Malaysian gains. Singapore profits were to be ascertained by deducting Singapore losses from Singapore gains. He considered that for the purposes of ascertaining Malaysian profits it would not be proper to deduct Singapore losses from Malaysian gains as this would mean the deduction twice of Singapore losses. He noted further that his view was quite contrary to Section 3(a) of the Income Tax Act 1967 which at all material times provided that the taxpayer should be taxed on its world income, i.e. on both its Malaysian and Singapore income, and that Singapore losses must be set off against Malaysian profits. However, Suffian L.P. took the view that this would only be so in relation to countries with which Malaysia does not have a Double Taxation Agreement as Section 132 provides that the Double Taxation Agreement may override the Act. Suffian L.P. concluded that the Double Taxation Agreement, 1966, has overridden the Income Tax Act, 1967 in so far as the losses of the Appellant's Singapore branch are concerned.

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10. Lee Hun Hoe, C.J. Borneo in delivering his Judgment referred to the case of United National Finance Berhad -v- The Director-General of Inland Revenue as quoted in paragraph 8 above. He took the view that the Singapore branch of the Appellant must be treated as a distinct and separate enterprise from its Head Office in Malaysia and, reading the Double Taxation Agreement, 1966, together with the Income Tax Act, 1967 he arrived at the conclusion that the Double Taxation Agreement, 1966, had

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transformed the basis of ascertaining chargeable income on a world income scope, namely, that Section 3 of the Income Tax Act, 1967, has been modified by Double Taxation Agreement, 1966.

11. The relevant legislation is now agreed upon. The Respondent having contended before the Special Commissioners that the relevant legislation was the Income Tax Ordinance of 1947 and not the Income Tax Act, 1967, abandoned this contention before the High Court and the Federal Court.

12. It is now agreed that the applicable legislation are the Income Tax Act, 1967 and the Double Taxation Agreement, 1966. The Special Commissioners, having held that the above legislation apply, found in favour of the Appellant.

13. The Appellant submits that the Double Taxation Agreement, 1966 sets out the arrangements "with a view to affording relief from double taxation in relation to Malaysian tax and Singapore tax". Section 132 of the Income Tax Act, 1967 provides that if any double taxation arrangements have been concluded by statutory order the arrangements afford relief from double taxation, those arrangements shall have effect in relation to tax under the Act, notwithstanding anything in any written law.

14. Article XVII of the Double Taxation Agreement, 1966 provides that "the law of each Contracting State shall continue to govern the taxation of income in that State except where the express provision to the contrary is made in this Agreement".

15. Section 3(a) of the Income Tax Act, 1967 i.e. the relevant governing law, provides that the income from wherever derived shall be assessable to tax and by the express provision of this section and the ordinary principles of commercial accounting the Singapore losses should be brought into account in determining the Appellant's chargeable income.

16. The Appellant further submits that the provisions of the Income Tax Act, 1967 are regulated by the Double Taxation Agreement, 1966, and by Article IV(1)(a) relief is granted in respect of tax payable on income of the Appellant's

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Singapore establishment. Article IV provides that in the event the Malaysian enterprise carries on the business in Singapore through a permanent establishment, tax may be imposed in Singapore on the profits of the enterprise, but only on so much of them as is attributable to that permanent establishment. Where tax is paid by virtue of Article IV, no further tax shall be imposed in Malaysia in respect of the profits of the permanent establishment which are remitted to Malaysia.

17. The basis of the computation of the Appellant's income under the Income Tax Act, 1967, is not transformed by the Double Taxation Agreement, 1966. Article IV only provides relief for tax paid in Singapore leaving the basis of computation intact, that is, the global computation of income, income wherever derived as stated under Section 3(a) of the Income Tax Act, 1967.

18. The Appellant submits that the Judgment of the Federal Court should be reversed and that this Appeal should be allowed with costs here and below and the Order of the Special Commissioners restored for the following, among other

R E A S O N S

(1) BECAUSE the basis of computation under Section 3(a) of the Income Tax Act, 1967, is on a world income basis, that is income wherever derived the gains and losses in Singapore should be brought into account.

(2) BECAUSE the Double Taxation Agreement, 1966 and its enabling authority, Section 132, provides for relief from tax and not for an increase in the amount of tax payable under the Income Tax Act, 1967.

(3) BECAUSE the relief provided from double tax is on tax on the profits paid in Singapore and does not conflict against, detract from or vary the basis of computation on a global scale for Malaysian Tax purposes.

(4) BECAUSE the ordinary principles of commercial accounting require the bringing into account of all gains and profits, subject to or in the absence of statutory directions as to computation.

(5) For the reasons appearing in the grounds of the decision of the Special Commissioners.

Michael Nolan Q.C.
S. Woodhull

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CASE FOR THE APPELLANT

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