

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

O N A P P E A L

FROM THE COURT OF APPEAL OF THE REPUBLIC OF SINGAPORE

B E T W E E N:

THOMSON HILL LIMITED

Appellants

- and -

THE COMPTROLLER OF INCOME TAX

Respondent

(IN THE MATTER OF CIVIL APPEAL NO. 10 OF 1981)

RECORD OF PROCEEDINGS

PART I

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Respondent

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PART 1

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(IN THE MATTER OF CIVIL APPEAL NO. 10 OF 1981)

10

RECORD OF PROCEEDINGS

PART I

No. 1

Grounds of decision of Income Tax
Board of Review

No. 1

Grounds of
decision of
Income Tax
Board of
Review

INCOME TAX BOARD OF REVIEW

Income Tax Appeal No. 2 of 1978

Thomson Hill Limited

v

The Comptroller of Income Tax

20

GROUND OF DECISION

The appellant company was incorporated on 15th April 1970 as a public company, carrying on business as a housing developer.

2. From the time of its incorporation the company purchased various parcels of land, some of which were developed while the others were held in its "land bank". As a consequence of

(continued)

a slump in the property market prevailing in Singapore around 1974, several development projects were halted in mid-stream and were delayed for about five years.

3. In its accounts pertaining to its various development projects the company has adopted the "completed contract" cost accounting system, whereby profit is recognised only when the contract or project is completed. Under this system, expenditure incurred in a development together with receipts from booking fees and progress payments are accumulated during the course of the project and profit is not reported until the project is substantially completed.

10

4. Each project is treated separately and individual cost records are kept for each project. Development expenses are then capitalised in the balance sheet and are accumulated and carried forward from year to year until the project is completed. Upon completion all the expenses attributable to a particular project are deducted from proceeds of sale, with net profits assessed to tax.

20

5. For the accounting years 1970 to 1973 property tax incurred annually in respect of properties held by the company was "capitalised" in the balance sheet as part of the overall development expenditure and did not appear in the profit and loss accounts.

30

6. For the financial year 1974 however, payments of property tax were for the first time treated as an item of expenditure and charged into the debit side of the profit and loss account. Property tax paid amounting to \$253,980 was claimed as an item of allowable expenditure under section 14 of the Income Tax Act (Cap. 141) against income of the appellant company.

7. This change in treatment of property tax payment was not allowed by the Comptroller of Income Tax on the grounds that property tax paid was not in the production of income assessable to tax, that it was paid in respect of properties that were being developed and should therefore form part of the cost of development and that as the development projects were dealt with on a project basis, all direct expenses incurred in connection with each project had to be capitalised and allowed against the sale proceeds received on the completion of the project.

40

50

8. For the appellant company it was contended that -

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Decision of
Income Tax
Board of
Review

- 10
- (a) there was no requirement in law that property tax paid for the year ended 31st December 1974 must have produced income assessable to tax for the year of assessment 1975;
- (b) the Comptroller of Income Tax erred in law in requiring that property tax be capitalised and allowed against the sale proceeds to be received on completion of the project;
- (c) property tax is an item of revenue expense as distinct from a capital expense. It is in no way related to the acquisition of a capital asset nor does it enhance the value of property; and
- 20 (d) the properties being the appellant company's stocks in trade, property tax is properly a revenue expense incurred in the maintenance of those stocks.

(continued)

30 9. The sole issue for determination in this appeal related to the proper treatment of property tax paid by the appellant company in respect of properties purchased for development. Of primary importance is the question whether the company was wrong in its previous treatment of property tax payments.

Reasons for change

40 10. On behalf of the appellant company, various reasons were given for the change in treatment of property tax, the chief of which was that because of the slump in the property market in 1974, doubts were cast about market conditions and the future viability of various projects which were halted. Development costs would thus be increased by the addition of property tax although no development work was being carried out. The value of the stock in trade would thus be overstated.

11. The company was further advised by its tax advisers that it did not have to "capitalise" property tax because such tax is in no way related to the acquisition of a capital asset, nor did it enhance the value of the properties. Furthermore, since property tax was a revenue expense incurred in the

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Review

(continued)

maintenance of the company's stock in trade,
it should not be capitalised.

12. Mr Anthony John Coomber, a partner in a well established firm of accountants in Singapore, was of the opinion that the company's treatment of property tax for the year 1974 was consistent with ordinary principles of commercial accountancy. Since property tax did nothing to enhance the value of a property and produces no benefit lasting beyond the period it is paid, it is not an expense incurred in bringing that property to its present location and condition. He further stressed that the fact that property tax had not been included in the cost of development in no way detracted from the "completed contract" method.

10

13. He found support for his opinion in the "Statement of Standard Accounting Practice No. 9" (SSAP 9) issued by the Institute of Chartered Accountants in England and Wales, and in "Exposure Draft No. 12 of the International Accounting Standard". He expressed the opinion that in view of the standards set out therein, it would now be incorrect to defer property tax. However, while maintaining that deferring property tax is "incorrect", he would nevertheless "allow a client to defer property tax where it is formed only to develop one property".

20

14. On behalf of the respondents, Mr Yip Thin Peng, Senior Assessment Officer at the Inland Revenue Department, testified that to his knowledge property development companies in Singapore adopt the completed contracts method. In so doing, they have treated property tax as part of the costs of development so as to be able to arrive at the true profits of each project.

30

15. Since property tax is suffered by the company in maintaining its stock in trade, a developer who develops land would take into account the amount of property tax paid in arriving at the cost of each unit sold. In his view "the practice of capitalising property tax is in accordance with normal accounting practice".

40

16. He added that a development company is assessed "on a project to project basis as it is completed, not as a whole", although it is taxed from its whole business. He concluded that the practice of housing developers in "capitalising" property tax is not inconsistent

50

with standards set out in SSAP 9 and Exposure Draft 12.

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10 17. It is perhaps pertinent to point out that the "Statement of Standard Accounting Practice No. 9" merely "seeks to define the practices, to narrow the differences and variations in those practices and to ensure adequate disclosure in the accounts". The Exposure Draft 12 of IAS remains a draft issued solely for comment by the International Accounting Standards Committee.

(continued)

18. It must be borne in mind that the effect of not "expensing off" property tax payments in the year they are paid is that they are deferred until completion of the projects in respect of which they are paid, at which time they are taken into account in computing the profits or loss of the projects concerned.

20 19. Considering the evidence before us and the submissions of counsel, we are of the view that the accumulation of property tax payments by the company pending the completion of the projects in respect of which they are paid, is not inconsistent with ordinary principles of commercial accounting where the "completed contract cost" method of accounting is adopted. We do not accept Mr Coomber's opinion that such a treatment would only be proper in respect of the accounts of single-development companies.

30 Onus on appellants

40 20. It has been clearly established that if a particular method of accounting has been applied consistently in the past it should not be changed, unless good reason is shown for that change (see Duple Motor Bodies Ltd v Ostine /1961/ 2 All E.R. 167, cited with approval in BSC Footwear Ltd v Ridgeway /1971/ 47 TC 495). The onus of proving that there was good reason for the change falls on the person seeking it.

21. Lord Morris of Borth-y-Gest in BSC Footwear succinctly put the position which we rely upon at page 528 of the report:-

50 " For many years the Company have kept their accounts on a particular basis. The Crown with appreciation of it have accepted it. The onus must be upon the Crown to show that the basis is unacceptable and must be changed. As between competing methods and practices

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(continued)

of commercial accounting a mere preference for one should not give it priority if the others are not open to objection. What must in the present case be considered is whether the basis which the Company adopted was or was not a basis which would show the full amount of the profits or gains of a particular year ..."

22. While we agree with the appellants that what they seek is not a change in method of accounting but merely a change in treatment of an item of expense, they must nevertheless show good reason for this change, unless of course the former treatment is wrong. 10

23. The appellants have ever since their incorporation until 1973, maintained their accounts on the basis that property tax payments are accumulated and deferred. This is the basis which other housing developers in Singapore adopt and is accepted by the respondent. While it is accepted that the appellants are not assessed to tax on an individual project basis, it is only on the completion of each project that the gross profits of each is known and subject to tax. 20

24. The onus being on the appellants to satisfy the Board that their former treatment of property tax was wrong and must be changed, we are of the opinion that they have not discharged that onus and that the Comptroller was justified in disallowing the deduction claimed. 30

25. We accordingly dismiss the appeal with costs.

Dated this 16th day of May 1979

(Signed) MICHAEL KHOO KAH LIP
CHAIRMAN

(Signed) LIM SEAN TECK
MEMBER

(Signed) ROBERT IAU KUO KWONG
MEMBER 40

Notes of Evidence

INCOME TAX BOARD OF REVIEW

ITBR Appeal No: 2/78

Thomson Hill Ltd v Comptroller of Income
Tax

NOTES OF EVIDENCE

MON 15 JAN 79

Coram:

10 Mr Michael Khoe Kah Lip - Chairman
Mr Robert Iau - Member
Mr Lim Sean Teck - Member

Miss Loo Liam Ho for Comptroller/
Respondent

Andrew Ang for Appellants

Miss LOO:

20 Applies for Mr Yip, an accountant with
Inland Revenue to sit in Court to assist as
the arguments concern difficult questions of
accounting practice. He is giving expert
opinion.

Ang:

Object. Witness of fact. Appellants
calling accountant to state commercial practice.

Board:

Objection overruled.

Ang:

30 Appeal concerns proper treatment to be
given to property tax paid by appellant company
in 1974 which appellants sought to have
deducted as allowance expenditure.

Comptroller disallowed deductions. P2
Agreed bundle.

Property tax should be allowed in the year
it was incurred and not capitalised.

Grounds P3 (Agreed bundle).

(continued)

- 1) ascertain the profits of the trade in accordance with ordinary principles of commercial accountancy.
- 2) one must adjust this account by reference to the express prohibitions contained in the relevant statute.

A.W.1 (Affirmed/English)

Robin Kang
5 Li Hwan View

10

I am a director of Thomson Hill Ltd. Appellants incorporated on 15.4.70 carrying on business as a housing developer.

Purchased many properties and commenced development work on some P66 of agreed bundle sets out list of properties held by each company and property tax payable.

The only project going on in 1974 were 1, 2, 3, 4.

20

Two properties, in Mayer Road (No. 55, 75 and 77) and at Tamjong Katong Road were rented out.

Rent received \$4,750 (P60 of A.B.)

Not necessary to develop land soon after purchase.

There was 4-5 years' delay in the properties being developed then.

We adopt the completed contract costs accounting system. Revenue or income is recognised only when the project is completed. Cost of the development and progress payments received from purchases are accumulated during course of projects but profit is not reported to Inland Revenue until the contract activity is substantially completed.

30

For Financial Year 1971, 1972 and 1973, property tax was capitalised into either development expenditure or fixed assets. It did not appear in profit and loss account.

40

In F/Y 1974 property tax incurred was charged into debit side of Profit and Loss

Account. It was treated as an item of expenditure in the year and deducted.

No. 2
Notes of
Evidence

Many reasons for change:

(continued)

In 1973 slump in property market and by capitalising property tax the work and value of property will be overstated.

10 In view of government restrictions on property, we did not know when we could recommence development. All developments were halted.

We had tax advisers from Arthur Young who advised us that property tax in previous years should not be capitalized as it did not enhance value of property. It should be in profit and loss account. Development costs would have increased without enhancing value of property.

20 We were advised that property tax was a revenue expense in maintenance of stock in trade.

Cross-examination: Miss Loo:

Q: What is your professional qualification?

A: None.

Q: When you purchase properties they are done with reasonable expectation that they would be developed?

A: Yes.

30 Q: Properties purchased do not appear as stock in trade in profit and loss account?

A: No. It is in the balance sheet.

Q: In 1974 you completed Golden Hill Project?

A: Yes.

Q: In 1974 the company first reported profits?

A: Yes.

Q: From 1970-73 none of the projects had been completed and losses were reported?

No. 2
Notes of
Evidence
(continued)

A: Yes.

Q: In accounting year 1974 the company reported profits of \$7.6 m?

A: Yes.

Q: I put it to you that your real reason for changing your practice is because company wanted to mitigate tax payable on the Golden Hill Project?

A: No.

Re-examination: Nil

10

Witness stands down.

Sgd. Michael K L Khoe

A.W.2 (Affirmed/English)

Yang Pah Liang
8-J Tamam Serasi

I am employed by Singapore Fodder Co Ltd. I am professionally qualified as an accountant with a degree of Bachelor of Accountancy, University of Singapore.

I was employed by Far East Singapura Intercontinental Ltd from Jan 75 to Mar 76, an associated company of the appellants. I was asked to assist in the accounting matters of Appellant.

20

I was asked for my view on the property tax treatment.

Property tax is payable on annual value of property. It does not enhance value nor produce any benefit lasting beyond period paid. Therefore it is not an item to be capitalised in the balance sheet.

30

When property ceases development it would be absurd to capitalise it and to charge to development costs.

In general accounting principles you should not overstate any item in the balance sheet. It would be wrong but I believe some property development companies do capitalise.

Cross-examination: Miss Loo:

No. 2
Notes of
Evidence

- (continued)
- Q: Look at accounts of company for 1971.
The company did not charge property tax
to profit and loss account?
- A: Yes.
- Q: The company capitalized property tax
either as part of development expenditure
or as part of fixed assets?
- A: Yes.
- 10 Q: This practice was followed in 1970, 1971,
1972 and in 1973?
- A: Yes.
- Q: What was the reason for so capitalizing?
- A: I do not know the reason.
- Q: From 1970-1973 it did not report any sales
deposits in its profit and loss accounts
but capitalised them including progress
payments, etc?
- A: Yes. It is in the balance sheet.
- 20 Q: These receipts were not taxed in the year
received?
- A: Yes.
- Q: Current assets at P59 not reported in profit
and loss account?
- A: Yes.
- Q: From 1970-1973 all the company's projects
were in various stages of development?
- A: I do not know that.
- 30 Q: In 1974, the company completed the
Golden Hill Project?
- A: A project was completed.
- Q: Look at accounts for 1974. (P61). It
still reflected sales deposits in balance
sheet together with stock of unsold houses?
- A: Yes.
- Q: However it charged property tax to profit

No. 2
Notes of
Evidence

(continued)

and loss account. . What was the reason?

A: I do not see how unsold houses has anything to do with charging of property tax.

Q: Property tax in each project is identifiable?

A: Yes.

Q: You ascertain profits based on sales less expenses?

A: Yes.

Q: In 1974 the company completed the Golden Hill and reported a gross profit of \$7.6m. It would be distorted as it includes property tax of other properties? 10

A: Not distorted. As developers they have to include property tax for other properties.

Refer to SSAP No. 9 para 1.

Re-examination: Ang:

There are 2 ways of treating stock-in trade: 20

1) The perpetual inventory method; and

2) The profit and loss account system.

Both systems should give the same result.

Property tax should not be capitalised.

Looking at P60. Gross Profit is \$7,629,893.26. Property tax of \$253,979.92 did not distort figure of gross profit.

Witness stands down.

Sgd. Michael K L Khoe

Adjourned: 2.30 pm. 30

A.W.3 (Affirmed/English)

Albert Goh
11, Li Hwan Place (19)

I am employed by Thomson Hill Ltd as a taxation adviser since 1.12.75.

During period 31.12.74 till 23.6.75 I was employed by Arthur Young & Co., an International auditors and accountants' firm, as a tax manager.

No. 2
Notes of
Evidence

(continued)

I had 16 years experience working in the Income Tax Department since 1957 till 1973.

10 Before I left the Department I was the Courts Officer for 4 years and prosecutor. I then held the substantive post of Senior Assessment Officer and statutory post of Assistant Comptroller of Income Tax.

Arthur Young was consulted by Far East Organisation Group of Companies, The Thomson Hill being a member of that group.

20 We were consulted on the proper treatment of property tax. The problem posed was whether Thomson Hill Ltd for Income Tax purposes can claim a deduction for property tax incurred by the company in respect of all properties owned by company be deducted in year incurred.

I looked at list of properties owned by company and found that that company owned more than a dozen.

Most were not under development and came to the conclusion after research and discussion with tax partner and director for Asia and FE who supported my views.

- 30
- 1) The various properties represent the stocks in trade as the company is a housing developer. Property tax is not a cost of development.
 - 2) Property tax is a charge on property a recurring expense payable annually. Such an expense does not enhance value of property. It is a holding expense, incurred in maintaining the stocks.

40 The property tax for Mukim 18 Lot 2282 Lorong Chuan (P66) had already been reflected in gross profits. So also for 55 Meyer Road and Mukim 25 Lot 1038 Tg Katong Road.

Property tax is a payment which should be allowed under S.14(1).

Cross-examination: Miss Loo:

Q: What are your professional qualifications?

(continued)

A: Associate Member of English Association of Accountants and Auditors, although this is not recognised by the Singapore Society for Public Accountants.

Q: During your time with Arthur Young you were not employed as an accountant?

A: No.

Q: You are then not qualified to give expert opinion on accounting practice?

A: No.

10

Re-examination: Nil.

Witness stands down.

sgd: Michael K L Khoe

A.W.4 (Sworn/English)

Anthony John Coomber
14 Woollerton Drive (10)

I am a practising Chartered Accountant with Turquand Youngs & Co. I am a fellow of Institute of Chartered Accountants, England and Wales and member of Singapore Society of Accountants.

20

I am a member of Institute of Taxation. I am Chairman of Financial Statements Committee of SSA since September 1973.

I have seen the accounts of the appellant for 1974. From my perusal, although it does not show any accounting policy used it appears to have used completed contracts accounting basis. It is the most conservative method of computing contracts covering more than 1 year. Revenue is recognised when contract is completed or substantially completed.

30

Costs and progress payments are received but profit is not reported till contract is substantially completed.

From perusal of P & L accounts it would appear that property tax has been expensed under profit & loss account.

Such a treatment of property tax is not inconsistent with commercial accounting practice. It is not inconsistent with completed contracts accounting basis.

40

Property tax should never be capitalised as it does nothing to enhance value of property concerned and is paid solely in the period it becomes payable and certainly produces no benefit lasting beyond such period.

No.2
Notes of
Evidence

(continued)

10 Comparing accounts for 1974 with previous years, the change in treatment was not wrong, not by itself but there should have been a correction shown of previous years' wrong. This has not been done.

SSAP issued support my views that properties of Thomson Hill should be treated as trading stocks.

(SSAP 9 marked Exhibit 1

Exposure Draft 12 marked Exhibit 2)

Refer to Exhibit 2 para 15(c) Property tax would be included in 15(c). Refer paras 18 & 19.

20 A client would have to substantiate such an item to carry forward.

Refer to P5 para 17 (Exhibit 1). Definition of "cost". You must only include those items of expenditure that have enhanced value of stock.

Refer paras 19 and 20.

3 separate issues

- 30
- 1) Property with which there are no development.
 - 2) Properties in process of development.
 - 3) Properties in respect of which there has been completion.

Cross-examination: Miss Loo:

Q: How many years practice in Singapore?

A: 9 years.

Q: Are you familiar with treatment of property tax by other Housing Developers in Singapore?

A: Not all.

Q: There are other accountants who capitalise

(continued)

property tax?

A: Not capitalise but I would say defer.
If it is done it is incorrect. The
only instance where I would allow a
client to defer property tax is where it
is formed only to develop one property.

Q: The accounting standards did not come into
being till 1975?

A: Yes.

Q: Is there a principle of consistency -
once a method is used it should be used
throughout?

10

A: Yes, except for instance in Introduction
of accounting standards.

Re-examination: Nil.

Witness stands down.

sgd. Michael K L Khoe

R.W.1 (Affirmed/English)

Yip Thin Peng
Senior Assessment Officer
Block 1, 79D, Marine Vista

20

I am employed by Department of Inland
Revenue. I am qualified as a certified
accountant. I have been with this Dept
for 16 years. In the course of my work I
have had experience in dealing with files of
property developers.

2 methods are normally used to reflect
profits:

- 1) by completed contracts method, and
- 2) by the percentage of completion method.

30

Under (1) costs of development are
accumulated in respect of each project. When
completed, profits are brought into F/L
account and assessed for tax. Expenses should
be deferred for matching revenue with expenses.

Under (2) a company would take account of
the progress of development. It would bring
in part of the profits earned over the years
during which the contracts run. Part of the

40

profits will be assessed to tax.

No. 2
Notes of
Evidence

The company has adopted the completed contracts method. Property tax has been treated as part of costs of development by most property development companies in Singapore to be able to arrive at true profits of that project.

(continued)

Practice of capitalising property tax is in accordance with normal accounting practice.

10 Appellants' method for 1970-73 is considered proper.

We assess a company on a project to project basis as it is completed, not as a whole.

Nothing in accounts of appellants to explain change in accounting policy.

In 1974 (P61) the charging of property tax to P & L would have resulted in tax savings of over \$100,000/-.

20 In my opinion, the change was made to gain a tax savings of over \$100,000/-. 1974 was the first year the company reported profits.

Adjourned: 10.00 a.m. on 16 Jan 1979

TUES 16 JAN 1979

Coram as before

Parties as before.

R.W.1 (on former oath)

Cross-examination: Ang:

Q: How did you obtain your accountancy qualification?

A: By self study.

30 Q: What is your commercial experience?

A: None.

Q: You have experience with accounts of property development companies?

A: Yes, in my capacity as Assessment Officer.

Q: Have you kept yourself up to date by attending seminars etc on up to date practices?

No. 2
Notes of
Evidence

(continued)

- A: No.
- Q: How many accounts of such companies do you examine each year?
- A: 7-8.
- Q: There are over 300 who have been issued development licences?
- A: It does not necessarily mean that if it holds licences it would develop properties. There are those who hold licence for investment purposes. 10
- Q: Of the accounts which you have examined, how many are true developers?
- A: All except one.
- Q: What are they?
- A: Success Realty, Kian Ann Realty, Central etc. Syndicate Pte Ltd.
- Q: How many are single property?
- A: Multiple property companies are Syndicate, Kiam Ann, Success.
- Q: How can you say what is the correct commercial accounting practice? 20
- A: By my understanding of SSAP (No. 9) and Exposure draft No. 12.
- Q: What is your view of the proper treatment to be given to property tax in accordance with the commercial practice.
- A: I draw your attention to the meaning of "stock in trade" in para 16 of SSAP No.9. Costs is defined in para 17. Refer to paras 3, 18. "Import duties", which is a tax, does not enhance value of property. Para. 20: Land for development is its raw material. Property tax is on land and accrues on time basis. It can be regarded as production overheads. 30
- Q: I put it to you that property tax has no part to play in bringing product to its present location and condition.
- A: Para 3: Such costs will include all 40

related production overheads.

No. 2
Notes of
Evidence

Property tax is suffered by the company in maintaining the stock in trade.

(continued)

Q: Does it enhance the value?

A: It does not.

Q: Why cannot it be expense but capitalised?

A: Any expense that is incurred in reference to any raw material must be part of the cost.

10 Q: You agree that "cost of conversion" is qualified by the phrase "in bringing the product to its present condition and location" in para 17.

A: Yes.

Q: Have you examined any percentage of completion method?

A: Not of property development companies but of construction companies.

20 Q: Do you consider it wrong for a company to change its practice to mitigate tax losses?

A: If it conforms to current accounting practice it is not wrong.

Q: Has the company changed its accounting policy?

A: It has changed its basis of valuation and therefore its policy.

Q: Look at IAS (8) para 17. Do you agree with it?

30 A: Yes.

Q: There has been no change in policy then?

A: There may not have been. I can't say. I was under the impression that there was a change in policy. I may be wrong.

Q: As of now you cannot say that the company has been inconsistent in its accounting policy?

No. 2
Notes of
Evidence
(continued)

- A: Yes.
- Q: What is true benefit to the company by this change in treatment of property tax?
- A: It is a deferral of tax.
- Q: That saving you spoke of \$100,000/- will eventually have to be paid?
- A: Yes.
- Q: The real saving is that of interest?
- A: Yes.
- Q: If the company had treated it as an expense item right from 1970, there would not be inconsistency? 10
- A: It depends on whether it is acceptable to the Department.
- Q: It could have been a coincidence that they changed treatment when profits were shown for the first time?
- A: Could be.
- Q: Revenue is taxing the company on each project and not on the performance of the company as a whole? 20
- A: Yes.
- Q: What is the source of income of appellants?
- A: From trade of housing developer.
- Q: From which provision of Income Tax Act?
- A: S10(1)(a). When income is earned or accrued.
- Q: At what stage?
- A: When completed.
- Q: If the company had adopted the completed contract method, amounts received by way of deposits etc., would not be the income of the company from which profits can be adduced? 30
- A: Yes.
- Q: Although profits are from each project,

the company is taxed from its whole business?

No. 2
Notes of
Evidence

A: Yes.

Q: Refer A.B.24 last para. This sentence is wrong?

(continued)

A: Yes.

10 Q: Because even if no income is produced for a land but for another, it is an expense incurred in the expectation of production of income?

A: Yes.

Q: Was Mr Coomber's opinion wrong in any way?

A: He has a different interpretation. It is wrong.

Re-examination: Miss Loo:

Q: Were you aware of SSAP (9) and IAS at the time of issue?

A: I was.

20 Q: Refer para 18. If a developer develops land, he would have to take into account the cost of property tax paid in arriving at the cost of each unit sold?

A: Yes.

Q: Would you regard property tax under cost of conversion?

A: Yes. Under para 19(b) - production overheads.

30 Q: The practice of housing developers is not inconsistent with standards set out in Exhibit 1?

A: No.

Q: Under IAS is it necessary for a cost to enhance value of property before it can be attributed to costs?

A: No.

Adjourned: 2.30 pm.

Sgd. Michael K L Khoe

R.W.1 (recalled/former oath)

Contd Re-examination: Miss Loo:

(continued)

Q: In 1974, was there a change in accounting method of treating property tax?

A: Yes.

Q: Was there in fact a change in valuing Co's valuing method of stock in trade?

A: Yes.

Q: What is your understanding of income?

A: Receipts less expenses.

10

Witness stands down.

Sgd: Michael K L Khoe

Ang submits:

Undisputed facts -

Appellants incorporated in 1970 as housing developers. Purchased many properties and commenced development on some.

From 1970-73 property tax deferred or capitalised and did not appear in the P & L account.

20

For 1974 property tax charged to debit of P & L account.

On advice of tax advisers, the company did not have to capitalise property tax and that being a revenue expense did not have to be capitalised or deferred. If it does not enhance value of property.

If added as a development costs, it would have enhanced value of property without development taking place.

30

Even if the true intention of the company was to mitigate tax liability, though not admitted, nothing wrong was done.

Ayrshire Pullman Motor Service v IRC (1929) 14 Tax cases 754 at 763-64.

Odeon Theatres v Jones 48 Tax Cases 257 per V.C. Pennycuick (at p272-3).

In arriving at profits of company in 1974, was treatment of property tax in accordance with correct principles of commercial accountancy?

No. 2
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Evidence

(continued)

10 Coomber's expert opinion that the company's treatment of property tax in 1974 was consistent with commercial accounting practice. Not inconsistent with completed contracts method adopted by appellants. Property tax does nothing to enhance value of property.

Ryam v Asia Mills Ltd

32 Tax Cases 275 at P298-99, P300

IAS Exposure Draft No 12 - accountant has to comply with SSAP (No. 9).

Coomber: it would be incorrect to capitalise property tax.

Questions of fact.

20 Yip has no commercial experience - cannot express expert opinion of commercial accountancy. He could not say if change of treatment was a change in accounting policy, that there was no change in accounting policy.

"Source" of company is its business as housing developer. The company cannot be taxed "project by project". Receipts of sales deposits is not income.

30 Property tax from other properties could be taken into account in ascertaining income of appellants.

S14 - "in the production of income".

Properties of the company are stock in trade held in land bank. Expenses incurred in maintaining them are deductible.

Vallambrosa Rubber Co Ltd v Farmer

5 Tax Cases 529 at P534

Duple Motor Bodies

39 Tax Cases 537 at P571

40 Property Tax must be allowed as a revenue expense unless it can be shown that treatment

No. 2
Notes of
Evidence

(continued)

is wrong and that it is not allowed by
S14(1).

Good reasons for change given by the
company.

Income Tax paid should be refunded.

Adjourned for a date to be fixed
pending written submissions within a week.

sgd: Michael K L Khoe

EXAMINED BY

TRUE COPY

(Sgd)

(sgd)

10

Clerk to the Income
Tax Board of Review

Chairman
Income Tax Board of
Review
Singapore

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Statement of standard accounting
practice

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STOCKS AND WORK IN PROGRESS

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1. Further Practical Considerations
2. Glossary of Terms
3. Statement of the Inland Revenue's Practice.

STATEMENTS OF STANDARD ACCOUNTING PRACTICE

9. STOCKS AND WORK IN PROGRESS

(Issued May 1974)

(C) 1973 The Institute of Chartered Accountants
in England and Wales.

No area of accounting has produced wider differences in practice than the computation of the amount at which stocks and work in progress are stated in financial accounts. This Statement of Standard Accounting Practice seeks to define the practices, to narrow the differences and variations in those practices and to ensure adequate disclosure in the accounts.

Introduction

1. The determination of profit for an accounting year requires the matching of costs with related revenues. The cost of unsold or unconsumed stocks and work in progress will have been incurred in the expectation of future revenue, and when this will not arise until a later year it is appropriate to carry forward this cost to be matched with the revenue in the year in which the revenue arises rather than in the year in which the cost is incurred. If there is no reasonable expectation of sufficient future revenue to cover cost incurred (e.g. as a result of deterioration, obsolescence or a change in demand), the irrecoverable cost should be charged to revenue in the year under review. Thus, stocks and work in progress normally need to be stated at cost, or, if lower, at net realisable value.

10

20

2. The comparison of cost and net realisable value needs to be made in respect of each item of stock separately. Where this is impracticable, groups or categories of stock items which are similar will need to be taken together. To compare the total realisable value of stocks with the total cost could result in an unacceptable setting of of foreseeable losses against unrealised profits.

30

3. In order to match costs and revenue, 'costs' of stocks and work in progress should comprise that expenditure which has been incurred in the normal course of business in bringing the product or service to its present location and condition. Such costs will include all related production overheads, even though these may accrue on a time basis.

4. The methods used in allocating costs to stocks and work in progress need to be selected with a view to providing the fairest possible approximation to the expenditure actually incurred in bringing the product to its present location and condition. For example, in the case of retail stores holding a large number of rapidly changing individual items, stocks on the shelves have often been stated at current selling prices less the normal gross profit margin. In these particular circumstances this may be acceptable as being the only practical method

40

50

of arriving at a figure which approximates to cost.

Net Realisable value

5. Net realisable value is the amount at which it is expected that items of stocks and work in progress can be disposed of without creating either profit or loss in the year of sale i.e., the estimated proceeds of sale less all further costs to completion and less all costs to be incurred in marketing, selling and distributing directly related to the items in question.

(continued)

Replacement cost

6. Items of stock and work in progress have sometimes been stated in accounts at estimated replacement cost where this is lower than net realisable value. Where the effect is to take account of a loss greater than that which is expected to be incurred, the use of replacement cost is not regarded as acceptable. However, in some circumstances (e.g. in the case of materials whose price has fluctuated considerably and which have not become the subject of firm sales contracts by the time the accounts are prepared) replacement cost may be the best measure of net realisable value.

Long-term contract work in progress

7. Separate consideration needs to be given to work in progress arising from long-term contracts. Owing to the length of time taken to complete such contracts, to defer taking profit into account until completion may result in the profit and loss account reflecting not so much a fair view of the activity of the company during the year but rather the results relating to contracts which have been completed by the year end. It is therefore appropriate to take credit for ascertainable profit while contracts are in progress, subject to the limitations in paragraph 8 below.
8. The profit, if any, taken up needs to reflect the proportion of the work carried out at the accounting date and to take into account any known inequalities of profitability in the various stages of a contract. Many businesses, however, carry out contracts where the outcome cannot reasonably be assessed before the conclusion of the contract and in such cases

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it is prudent not to take up any profit.
Where the business carries out contracts and
it is considered that their outcome can be
assessed with reasonable certainty before their
conclusion, then the attributable profit should
be taken up, but the judgement involved should
be exercised with prudence.

(continued)

9. If, however, it is expected that there will
be a loss on a contract as a whole, provision
needs to be made (in accordance with the
prudence concept), for the whole of the loss
as soon as it is recognised. This has the
effect of reducing the work done to date to
its net realisable value. Where unprofitable
contracts are of such magnitude that they can
be expected to absorb a considerable part of
the company's capacity for a substantial period,
related administration overheads to be incurred
during the period to the completion of those
contracts should also be included in the
calculation of the provision for losses. 10
10. Thus, the gross amount of long-term contract
work in progress should be stated in accounts
at cost plus attributable profits (if any)
less foreseeable losses (if any). In arriving
at a decision as to whether there are attributable
profits, a company should consider whether having
regard to the nature of the contracts undertaken
it is reasonable to foresee profits in advance
of the completion of the contracts. 20
- Disclosure in accounts
11. A suitable description of the amount at which
stocks and work in progress are stated in
accounts might be 'at the lower of cost and net
realisable value' or, in the case of long-term
contract work in progress 'at cost plus
attributable profit (if any) less foreseeable
losses (if any) and progress payments received
and receivable'. 30
12. In order to give an adequate explanation of
the affairs of the company the accounting
policies followed in arriving at the amount at
which stocks and work in progress are stated
in the accounts should be set out in a note.
Where differing bases have been adopted for
different types of stocks and work in progress
the amount included in the accounts in respect
of each type will need to be stated. 40
13. In the case of long-term contract work in
progress the terms of a contract usually involve 50

progress payments which reduce the amount at which the contract is stated in the accounts. The financial position of a company may be materially dependent on the outcome of such contracts despite this lessening of their apparent significance. A related note should, therefore, indicate the amount of progress payments received and receivable separately from the net amount of cost plus attributable profit, less foreseeable losses as appropriate.

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(continued)

10

Further practical considerations

14. The basic considerations which must be taken into account in determining costs and net realisable value in relation to stocks and work in progress are set out in Parts 2 and 3 of this statement. The majority of problems which arise in practice in determining both the cost and the net realisable value of stocks and work in progress result from considerations which are relevant to particular businesses and are not such universal application that they can be the subject of a statement of standard accounting practice. Accordingly Appendix I sets out in more detail some general guidelines which may be of assistance in determining cost and net realisable value and in identifying those situations in which net realisable value is likely to be less than cost. Appendix 1 also sets out considerations which need to be borne in mind in calculating the amount of profit to be taken into account in respect of long-term contracts.

20

30

PART 2 - DEFINITION OF TERMS

15. The following definitions of terms are used for the purpose of this statement.

16. Stocks and work in progress comprise:

- (a) goods or other assets purchased for resale;
- (b) consumable stores;
- (c) raw materials and components purchased for incorporation into products for sale;
- (d) products and services in intermediate stages of completion;
- (e) finished goods.

40

<p>No. 3 Statement of standard accounting practice No. 9 (continued)</p>	<p>17. Cost is defined in relation to the different categories of stocks and work in progress as being that expenditure which has been incurred in the normal course of business in bringing the product or service to its present location and condition. This expenditure should include in addition to cost of purchase (as defined in paragraph 18) such costs of conversion (as defined in paragraph 19) as are appropriate to that location and condition.</p>	<p>10</p>
	<p>18. Cost of purchase comprises purchase price including import duties, transport and handling costs and any other directly attributable costs, less trade discounts, rebates and subsidies.</p>	
	<p>19. Cost of conversion comprises:</p> <ul style="list-style-type: none"> (a) costs which are specifically attributable to units of production, i.e. direct labour, direct expenses and sub-contracted work; (b) production overheads (as defined in paragraph 20); (c) other overheads, if any, attributable in the particular circumstances of the business to bringing the product or service to its present location and condition. 	<p>20</p>
	<p>20. Production overheads: overheads incurred in respect of materials, labour or services for production, based on the normal level of activity, taking one year with another. For this purpose each overhead should be classified according to function (e.g., production, selling or administration) so as to ensure the inclusion in cost of conversion of those overheads (including depreciation) which relate to production, notwithstanding that these may accrue wholly or partly on a time basis.</p>	<p>30</p>
	<p>21. Net realisable value: the actual or estimated selling price (net of trade but before settlement discounts) less:</p> <ul style="list-style-type: none"> (a) all further costs to completion; and (b) all costs to be incurred in marketing, selling and distributing. 	<p>40</p>
	<p>22. Long-term contract: a contract entered into for manufacture or building of a single</p>	

substantial entity or the provision of a service where the time taken to manufacture, build or provide is such that a substantial proportion of all such contract work will extend for a period exceeding one year.

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10 23. Attributable profit: that part of the total profit currently estimated to arise over the duration of the contract (after allowing for likely increases in costs so far as not recoverable under the terms of the contract) which fairly reflects the profit attributable to that part of the work performed at the accounting date. (There can be no attributable profit until the outcome of the contract can be assessed with reasonable certainty.)

(continued)

20 24. Foreseeable losses: losses which are currently estimated to arise over the duration of the contract (after allowing for estimated remedial and maintenance costs, and increases in costs so far as not recoverable under the terms of the contract).

This estimate is required irrespective of:

- (a) whether or not work has yet commenced on such contracts;
- (b) the proportion of work carried out at the accounting date;
- (c) the amount of profits expected to arise on other contracts.

30 PART 3 - STANDARD ACCOUNTING PRACTICE

The expressions used in this Statement of Standard Accounting Practice are defined in Part 2.

Stocks and work in progress other than long-term contract work in progress

40 The amount at which stocks and work in progress, other than long-term contract work in progress, is stated in periodic financial statements should be the total of the lower of cost and net realisable value of the separate items of stock and work in progress or of groups of similar items.

Long-term contract work in progress

The amount at which long-term contract work in

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progress is stated in periodic financial statements should be cost plus any attributable profit, less any foreseeable losses and progress payments received and receivable. If, however, anticipated losses on individual contracts exceed cost incurred to date less progress payments received and receivable, such excesses should be shown separately as provisions.

Disclosure in financial statements

10

The accounting policies which have been used in calculating cost, net realisable value, attributable profit and foreseeable losses (as appropriate) should be stated.

Stocks and work in progress should be sub-classified in balance sheets or in notes to the financial statements in a manner which is appropriate to the business and so as to indicate the amounts held in each of the main categories.

20

In relation to the amount at which long-term contracts are stated in the balance sheet there should be stated:

- (a) the amount of work in progress at cost plus attributable profit, less foreseeable losses;
- (b) cash received and receivable at the accounting date as progress payments on account of contracts in progress.

Date from which effective

30

The accounting practice set out in this statement should be adopted as soon as possible and regarded as standard in respect of accounts relating to accounting periods starting on or after 1st January 1976.

APPENDICES

The appendices are for general guidance and do not form part of the Statement of Standard Accounting Practice.

Appendix I

40

This appendix is for general guidance and does not form part of the Statement of Standard Accounting Practice.

FURTHER PRACTICAL CONSIDERATIONS

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Many of the problems involved in arriving at the amount at which stock and work in progress are stated in accounts are of a practical nature rather than resulting from matters of principle. This appendix discusses some particular areas in which difficulty may be encountered.

(continued)

The allocation of overheads

- 10 1. Production overheads are included in cost of conversion (as defined in Part 2) together with direct labour, direct expenses and sub-contracted work. This inclusion is a necessary corollary of the principle that expenditure should be included to the extent to which it has been incurred in bringing the product to its present location and condition (paragraph 17 of Part 2). All abnormal conversion costs, however (such as exceptional
20 spoilage, idle capacity and other losses), which are avoidable under normal operating conditions need, for the same reason, to be excluded.
2. Where firm sales contracts have been entered into for the provision of goods or services to customer's specification, overheads relating to design, and marketing and selling costs incurred before manufacture may be included in arriving at cost.
- 30 3. The costing methods adopted by a business are usually designed to ensure that all direct material, direct labour, direct expenses and sub-contracted work are identified and charged on a reasonable and consistent basis, but problems arise on the allocation of overheads which must usually involve the exercise of personal judgement in the selection of an appropriate convention.
- 40 4. The classification of overheads necessary to achieve this allocation takes the function of the overhead as its distinguishing characteristic (e.g. whether it is a function of production, marketing, selling or administration), rather than whether the overhead tends to vary with time or with volume.
5. The costs of general management, as distinct from functional management, are not directly related to current production and are, therefore,

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(continued)

excluded from cost of conversion and hence from the cost of stocks and work in progress.

6. In the case of smaller organisations whose management may be involved in the daily administration of each of the various functions, particular problems may arise in practice in distinguishing these general management overheads. In such organisations the cost of management may fairly be allocated on suitable bases to the functions of production, marketing, selling and administration. 10

7. Problems may also arise in allocating the costs of central service departments, the allocation of which should depend on the function or functions that the department is serving. For example the accounts department will normally support the following functions:

(a) production - by paying production direct and indirect wages and salaries, by controlling purchases and by preparing periodic accounts for the production units; 20

(b) marketing and distribution - by analysing sales and by controlling the sales ledger;

(c) general administration - by preparing management and annual accounts and budgets, by controlling cash resources and by planning investments. 30

Only those costs of the accounts department that can reasonably be allocated to the production function fall to be included in the cost of conversion.

8. The allocation of overheads included in the valuation of stocks and work in progress needs to be based on the company's normal level of activity, taking one year with another. The governing factor is that the cost of unused capacity should be written off in the current year. In determining what constitutes 'normal' the following factors need to be considered: 40

(a) the volume of production which the production facilities are intended by their designers and by management to produce under the working conditions (e.g. single or double

- shift) prevailing during the year;
- (b) the budgeted level of activity for the year under review and for the ensuing year;
 - (c) the level of activity achieved both in the year under review and in previous years.

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(continued)

10 Although temporary changes in the load of activity may be ignored, persistent variation should lead to a revision of the previous norm.

9. Where management accounts are prepared on a marginal cost basis, it will be necessary to add to the figure of stock so arrived at the appropriate proportion of those production overheads not already included in the marginal cost.

20 10. The adoption of a conservative approach to the valuation of stocks and work in progress has sometimes been used as one of the reasons for omitting selected production overheads. In so far as the circumstances of the business require an element of prudence in determining the amount at which stocks and work in progress are stated, this needs to be taken into account in the determination of net realisable value and not by the exclusion from cost of selected overheads.

30 Methods of costing

11. It is frequently not practicable to relate expenditure to specific units of stocks and work in progress. The ascertainment of the nearest approximation to cost gives rise to two problems:

- 40 (a) the selection of an appropriate method for relating costs to stocks and work in progress (e.g. job costing, batch costing, process costing, standard costing);
- (b) the selection of an appropriate method for calculating the related cost where a number of identical items have been purchased or made at different times (e.g. unit cost, average cost or FIFO).

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(continued)

12. In selecting the methods referred to in paragraphs 11 (a) and (b) above, management must exercise judgement to ensure that the methods chosen provide the fairest practicable approximation to 'actual cost'. Furthermore, where standard costs are used they need to be reviewed frequently to ensure that they bear a reasonable relationship to actual costs obtaining during the period. Methods such as base stock and LIFO do not usually bear such a relationship. 10
13. The method of arriving at cost by applying the latest purchase price to the total number of units in stock is unacceptable in principle because it is not necessarily the same as actual cost and, in times of rising prices, will result in the taking of a profit which has not been realised.
14. One method of arriving at cost, in the absence of a satisfactory costing system, is the use of selling price less an estimated profit margin. This is acceptable only if it can be demonstrated that the method gives a reasonable approximation of the actual cost. 20
15. In industries where the cost of minor by-products is not separable from the cost of the principal products, stocks of such by-products may be stated in accounts at their net realisable value. In this case the costs of the main products are calculated after deducting the net realisable value of the by-products. 30
- The determination of net realisable value
16. The initial calculation of provisions to reduce stocks from cost to net realisable value may often be made by the use of formulae based on predetermined criteria. The formulae normally take account of the age, movements during the past, expected future movements and estimated scrap values of the stock, as appropriate. Whilst the use of such formulae establishes a basis for making a provision which can be consistently applied, it is still necessary for the results to be reviewed in the light of any special circumstances which cannot be anticipated in the formulae, such as changes in the state of the order book. 40
17. Where a provision is required to reduce the value of finished goods below cost, the stocks of the parts and sub-assemblies held 50

for the purpose of the manufacture of such products, together with stocks on order, need to be reviewed to determine if provision is also required against such items.

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18. Where stocks of spares are held for sale special consideration of the factors in paragraph 16 of this appendix will be required in the context of:

(continued)

- 10
- (a) the number of units sold to which they are applicable;
 - (b) the estimated frequency with which a replacement spare is required;
 - (c) the expected useful life of the unit to which they are applicable.

19. Events occurring between the balance sheet date and the date of completion of the accounts need to be considered in arriving at the net realisable value at the balance sheet date (e.g. a subsequent reduction in selling prices). However, no reduction falls to be made when the realisable value of material stocks is less than the purchase price provided that the goods into which the materials are to be incorporated can still be sold at a profit after incorporating the materials at cost price.
- 20

The application of net realisable value

20. The principal situations in which net realisable value is likely to be less than cost are where there has been:
- 30

- (a) an increase in costs or a fall in selling price;
- (b) physical deterioration of stocks;
- (c) obsolescence of products;
- (d) a decision as part of a company's marketing strategy to manufacture and sell products at a loss;
- (e) errors in production or purchasing.

40 Furthermore, when stocks are held which are unlikely to be sold within the turn-over period normal in that company (i.e. excess stocks), the impending delay in realisation increases the risk that the situations outlined in (a) to (c) above may occur before

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the stocks are sold and needs to be taken
into account in assessing net realisable value.

Long-term contract work in progress

No. 9
(continued)

21. In ascertaining cost of long-term contract work in progress it is not normally appropriate to include interest payable on borrowed money. However, in those infrequent circumstances where sums borrowed can be identified as financing specific long-term contracts, it may be appropriate to include such related interest in cost, in which circumstances the facts should be clearly stated. 10
22. In some businesses, long-term contracts for the supply of services or manufacture and supply of goods exist where the prices are determined and invoiced according to separate parts of the contract. In these businesses the most appropriate method of reflecting profits on each contract is usually to match costs against performance of the separable parts of the contract, treating each such separable part as a separate contract. In such instances, however, future revenues from the contract need to be compared with future estimated costs and provision made for any foreseen loss. 20
23. In determining whether there is attributable profit to be included in the amount at which long-term contract work in progress is stated in the accounts, and in calculating such attributable profit, account should be taken of the type of business concerned. It is necessary to define the earliest point for each particular contract before which no profit is taken up, the overriding principle being that there can be no attributable profit until the outcome of a contract can reasonably be foreseen. Of the profit which in the light of all the circumstances can be foreseen with a reasonable degree of certainty to arise on completion of the contract, there should be regarded as earned to date only that part which prudently reflects the amount of work performed to date. The method used for taking up such profits needs to be consistently applied. 30 40
24. In calculating the total estimated profit on the contract, it is necessary to take into account not only the total costs to date and the total estimated further costs to completion (calculated by reference to the 50

(continued)

- 10 same principles as were applied to cost to date) but also the estimated future costs of rectification and guarantee work, and any other future work to be undertaken under the terms of the contract. These are then compared with the total sales value of the contract. In considering future costs it is necessary to have regard to likely increases in wages and salaries, to likely increases in the price of raw materials and to rises in general overheads so far as these items are not recoverable from the customer under the terms of the contract.
- 20 25. Where approved variations have been made to a contract in the course of it and the amount to be received in respect of these variations has not yet been settled and is likely to be a material factor in the outcome, it is necessary to make a conservative estimate of the amount likely to be received and this is then treated as part of the total sales value. On the other hand, provision needs to be made for foreseen claims or penalties payable arising out of delays in completion or from other causes.
- 30 26. The settlement of claims arising from circumstances not envisaged in the contract or arising as an indirect consequence of approved variations is subject to a high level of uncertainty relating to the outcome of future negotiations. In view of this, it is generally prudent to make provision for receipts in respect of such claims only when negotiations have reached an advanced stage and there is evidence in writing of the acceptability of the claim in principle to the purchaser, an indication of the magnitude of the sum involved also being available.
- 40 27. The amount to be reflected in the year's profit and loss account will be the appropriate proportion of this total profit by reference to the work done to date, less any profit already taken up in prior years. The estimated outcome of a contract which extends over several accounting years will nearly always vary in the light of changes in circumstances and for this reason the result of the year will not necessarily represent the proportion of the total profit on the contract which is appropriate to the amount of work carried out in the period: it may also reflect the effect of changes in circumstances during the year which affect the total profit estimated to accrue on completion.
- 50

This appendix is for general guidance and does not form part of the Statement of Standard Accounting Practice.

GLOSSARY OF TERMS

(continued)

The use of the following terms in describing the accounting policies adopted in arriving at the amount at which stocks and work in progress are stated in accounts should be restricted in conformity with the definitions given to each. Where these definitions are inapplicable, alternative expressions should be used and explained. 10

1. Unit cost: the cost of purchasing or manufacturing identifiable units of stock.
2. Average cost: the calculation of the cost of stocks and work in progress on the basis of the application to the unit of stocks on hand of an average price computed by dividing the total cost of units by the total number of such units. This average price may be arrived at by means of a continuous calculation, a periodic calculation or a moving periodic calculation. 20
3. FIFO (first in, first out): the calculation of the cost of stocks and work in progress on the basis that the quantities in hand represent the latest purchases or production.
4. LIFO (last in, first out): the calculation of the cost of stocks and work in progress on the basis that the quantities in hand represent the earliest purchases or production. 30
5. Base stock: the calculation of the cost of stocks and work in progress on the basis that a fixed unit value is ascribed to a predetermined number of units of stock, any excess over this number being valued on the basis of some other method. If the number of units in stock is less than the predetermined minimum, the fixed unit value is applied to the number in stock. 40
6. Replacement cost: the cost at which an identical asset could be purchased or manufactured.
7. Standard cost: the calculation of the cost

of stocks and work in progress on the basis of periodically predetermined costs calculated from management's estimates of expected levels of costs and of operations and operational efficiency and the related expenditure.

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8. Completed long-term contract: a long-term contract on which no further work, apart from maintenance work, is expected to take place.

10

Appendix 3

This appendix is for general guidance and does not form part of the Statement of Standard Accounting Practice.

The accountancy bodies have received the following statement from the Board of Inland Revenue in response to their request for clarification of the Revenue's practice on the publication of SSAP 9 Stocks and Work in Progress.

20

Changes in basis of valuation

1. After the publication of N22, the Revenue explained their practice with regard to changes in the basis of valuation in a statement published in "The Accountant" on 17th November 1962. The practice set out in that statement applies to changes made as a result of the adoption of SSAP 9 in the following way. References to stock in trade cover manufacturing work in progress but not professional work in progress or work under long term contracts.

30

2. First, the basis set out in SSAP 9 will be regarded as a valid basis, and will be accepted as a good reason for a change from a previously valid basis. Therefore on such a change the opening stock of the year of change is to be valued on the same basis as the closing stock of that year. Whether the change is to a higher or lower level, the valuations of previous years will not be revised. Further assessments for past years will not therefore be raised nor will relief under the 'error or mistake' provisions be admitted on this account.

40

3. Where the existing basis of stock valuation is valid under recommendation N22 and is such that the adoption of the new

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(continued)

Standard could be argued to be merely a refinement and not a change of basis, the Revenue will be prepared to accept a valuation of the opening stock in the year of change by reference to the new standard, i.e., the argument that there has only been a refinement, so that the opening valuation should be the same as the closing valuation of the preceding year, will not be used.

4. Where stock has been brought into accounts in the past on a basis which was not a valid basis under recommendation N22, the Revenue must reserve the right to review past liabilities. However, where there is no question of past irregularities (i.e. fraud, wilful default or neglect), the Revenue would not in any event seek to recover tax for past years on an amount greater than that involved in the uplift of the closed valuation of the year preceding the year of change to a valid basis within the old code. 10 20

5. These comments are made on the basis of existing law and practice. The Revenue reserve the right to reconsider their attitude in the event of any change in the law, and in any case, at the expiry of 3 years.

Discounted selling price

6. Where stock is valued at current selling prices less the normal gross profit margin in the circumstances described in paragraph 4 of Part 1 of the Statement, the valuation will be acceptable only if the further test set out in paragraph 14 of Appendix 1 to the Statement is clearly satisfied. 30

It is considered that the selling price to be used for the purpose of discounting should normally be the original price fixed for the article determined by operating the normal mark-up on the original cost price. 40

Replacement cost

7. Where the value of the raw material content forms a high proportion of the total value of stock in process of production and the price of the raw materials is liable to considerable fluctuation, it is common practice to make rapid changes in selling

prices to accord with the changes in the price of the raw material. In cases of this kind the replacement cost basis may be extended to cover stock in process of production and finished stock as well as to the stocks of raw material.

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Long-term contracts

10 8. Where a loss on a contract as a whole is foreseen, a proportion of the overall loss, calculated either by reference to time normally up to the due completion date under the terms of the contract, or to expenditure incurred, may normally be taken into account year by year during the remainder of the contract period so long as all contracts, profitable or otherwise, are dealt with similarly. Further, when the work on a long-term contract has been substantially completed, so that it is possible to assess the financial
20 outcome of the contract with reasonable certainty, the Inland Revenue do not normally object to account being taken, at that point, of the foreseeable further expenditure representing obligations arising out of the contract up to the time of final delivery and also of a reasonable provision to allow for expenditure under any guarantee or warranties included in the contract. Beyond
30 these limits it is not permissible for tax purposes to take account of expenditure which has not then been incurred. It follows that a provision for an expected future loss made in accordance with paragraph 9 of Part 1 of the Statement would be disallowed for tax purposes to the extent that it is in excess of the amount determined above.

40 9. Where there is a change in the basis for treatment of long-term contracts, the opening figure in the year of change must, for taxation purposes, be the same as the closing figure for the preceding year.

The Inland Revenue will not accept a claim for a tax-free uplift based on the grounds that the opening and closing figures in the year of change must be on the same basis. Alternatively, the Inland Revenue would accept the continuance of the existing basis for long-term contracts current at the beginning of the year of change, with the new
50 basis being applied only to contracts entered into in or after the year of change.

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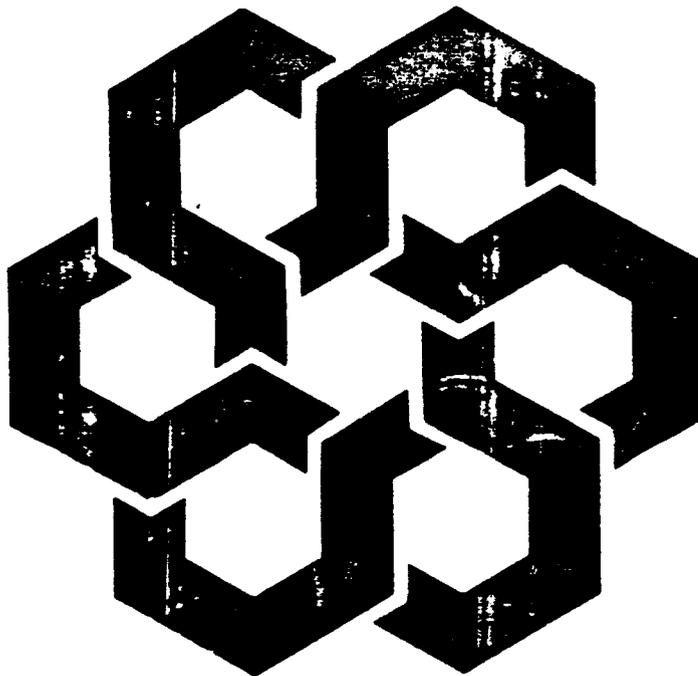
E12

Exposure Draft 12

1 DECEMBER 1977

International Accounting Standard

Proposed Statement Accounting for Construction Contracts



Issued for comment by the
International Accounting Standards Committee

This draft is issued by the International Accounting Standards Committee for comment only and does not necessarily represent the views of the Governing Bodies of the Founder Members. The draft may be modified in the light of the comments received before being issued in the form of an International Accounting Standard.

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(continued)

10

Comments should be submitted in writing so as to be received by 28 April 1978 and addressed to :

The Secretary
The Consultative Committee of Accountancy
Bodies
Chartered Accountants' Hall
Moorgate Place
London EC2P 2BJ
England

The English text is the definitive version of the Proposed Statement.

INTRODUCTION

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1. This Statement deals with accounting for construction contracts.

2. For the purposes of this Statement a construction contract is a contract for the construction of an asset or of a combination of assets which together constitute a single substantial project. Examples of activity covered by such contracts include the construction of bridges, dams, ships, buildings including site preparation and complex pieces of equipment.

(continued)

3. The feature which characterises a construction contract dealt with in this Statement is the fact that the date at which the contract activity is entered into and the date when the contract activity is completed fall into different accounting periods. The specific duration of the contract performance is not used as a distinguishing feature of a construction contract.

4. Contracts for the provision of services come within the scope of this Statement to the extent that they are directly related to a contract for the construction of an asset. Examples of such service contracts are contracts for the services of architects and for technical engineering services related to the construction of an asset.

EXPLANATION

5. The principal problem relating to accounting for construction contracts is the allocation of revenues and related costs to accounting periods over the duration of the contract. Contracts of a short duration pose few special problems because revenues and costs are usually recognised in the financial statements of the period during which the major portion of the related activity is undertaken by the enterprise. The longer the duration of contracts, the less likelihood there is that the results of contracts completed in an accounting period will portray the results of the business activity which takes place during the accounting period.

Types of Construction Contracts

(continued)

6. Construction contracts are negotiated in a number of ways. The two basic types of contract are:

(a) fixed price contracts - the contractor agrees to a fixed contract price, in some cases subject to cost escalation clauses

(b) cost plus contracts - the contractor is reimbursed for allowable or otherwise defined costs, plus a percentage of these costs or a fixed fee.

10

Both types of contract are within the scope of this Statement.

7. It may be necessary to combine contracts made with a single customer or to combine contracts made with several customers if the contracts are negotiated as a package or if the contracts are for a single project. Conversely, if a contract covers a number of projects and if the costs and revenues of such individual projects can be identified within the terms of the overall contract, each such project can be treated as equivalent to a separate contract.

20

The Accounting Treatment of Construction Contract Costs and Revenues

8. Two methods of accounting for contracts which are commonly followed by contractors are the percentage of completion method and the completed contract method.

30

9. Under the 'percentage of completion method', revenue is recognised as the contract activity progresses. This revenue is matched against the costs incurred in reaching the stage of completion, resulting in the reporting of profit which can be attributed to the proportion of work completed.

40

10. Under the 'completed contract method', revenue is recognised only when the contract is completed or substantially completed. Costs and progress payments received are accumulated during the course of the contract, but profit is not reported until the contract

activity is substantially completed.

11. Under both methods any foreseeable losses are usually provided for and reported in the financial statements both for the stage of completion reached on the contract and for future losses on the contract.

(continued)

The Costs to be Accumulated for
Construction Contracts

10 12. The total period to be considered for identifying the costs attributable to a contract usually is the period which commences with the signing of the contract, and closes when the contract is substantially complete; that is when only minor work is expected other than warranty work.

20 13. Costs incurred by the contractor before a contract is signed are usually treated as expenses of the period in which they are incurred. However, if costs can be directly associated with a specific future contract and there is a reasonable basis to expect that the contract will be obtained, the costs are often treated as applicable to the contract and are accumulated.

14. Expected warranty costs are provided for during the contract period when such costs can be determined with reasonable accuracy.

30 15. The costs incurred by an enterprise which undertakes construction contracts can be divided into three classes:

- (a) costs which relate directly to a specific contract
- (b) costs which can be attributed to the contract activity and are allocated to specific contracts
- (c) costs which are incurred to carry out the activities of the enterprise, but which cannot be directly related to a specific contract.

40

16. Examples of costs directly related to a specific contract include:

site labour costs, including supervision;
materials used for project construction;

depreciation or loss of value of plant
and equipment used on a contract;
costs of moving equipment to site.

(continued)

17. Examples of costs which can be attributed
to the contract activity and are allocated
to specific contracts include:

insurance;
design and technical assistance;
manufacturing overhead.

18. Examples of costs usually not directly
related to a specific contract or to contract
activity include: 10

general administration and selling
costs;
finance costs;
research and development costs;
depreciation of idle plant and equipment
which is not used on a particular
contract.

19. Costs of the types referred to in
paragraph 18 are usually excluded from the
accumulated contract costs because they do
not relate to putting the contract work in
its present condition. However, in some
circumstances general administrative expenses,
development costs and finance costs are
specifically attributable to a particular
contract and are sometimes included as part
of accumulated contract costs. 20

THE BASIS FOR RECOGNISING REVENUE ON
CONSTRUCTION CONTRACTS 30

The Percentage of Completion Method

20. Under the percentage of completion method
the recognition of revenue is determined by
the stage of completion of the contract
activity at the end of each accounting period.
The advantage of this method of accounting
for contract revenue is that it reflects
income in the accounting period during which
activity was undertaken in order to earn such
income. 40

21. Measurement of the stage of completion
is often determined by calculating the
proportion that costs incurred to date bear
to the estimated total costs of the contract
activity. However measures of progress
other than the proportion of total contract
costs incurred to date are also used, or may

assist in determining the stage of completion. For example, surveys which measure work performed and completion of a physical proportion of the contract work can be used in conjunction with the proportion of costs method to assess attributable revenue for the purposes of recognition in the financial statements.

(continued)

10 22. Progress payments and advances received from customers do not necessarily reflect the stage of completion and therefore cannot usually be treated as equivalent to revenue earned.

20 23. If the percentage of completion method is applied by calculating the percentage of incurred costs compared with total contract costs, adjustments are made in order to include only those costs which reflect work performed. Examples of items which may need adjustment include:

- (a) the costs of materials which have been purchased for the contract but which have not been installed or used during contract performance, and
- (b) payments to subcontractors, to the extent that they do not reflect the amount of work performed under the sub-contract.

30 In making the calculation, all types of costs included in costs incurred to date are also included in the total cost estimate.

40 24. The application of the percentage of completion method is subject to a risk of error in making estimates. For this reason profit is not included in the amount at which contract work in progress is stated in financial statements unless the outcome of the contract can be assessed with reasonable assurance. The conditions which will usually provide this degree of assurance are as follows:

- (a) total contract revenues to be received can be determined, and
- (b) an adequate estimating process exists, and both the costs to complete the contract and the percentage of contract performance completed at the reporting date can

be reliably estimated, and

- (c) the construction contract is clearly defined and the costs attributable to the contract can be clearly identified so that actual experience can be compared with prior estimates.

(continued)

25. In some cases the uncertainty inherent in making estimates of future costs or variations in work which render recoverable costs and revenue subject to further negotiation is so significant that the use of the percentage of completion method may result in the recognition of profit that may not be subsequently realised. In these cases, the completed contract method is used. 10

The Completed Contract Method

26. Under the completed contract method revenue is not recognised until performance of the contract activity is complete or substantially complete. This occurs when the risks of contract performance have been eliminated and only minor costs remain to be incurred. 20

27. The principal advantage of the completed contract method is that it is based on results as finally determined, rather than on estimates which may require subsequent adjustment as a result of unforeseen costs and possible losses. The risk of recognising profits that may not subsequently be realised is therefore eliminated. 30

28. The principal disadvantage of the completed contract method is that periodic reported income does not reflect the level of contract activity during the period. For example, when a few large contracts are completed in one accounting period, but no contracts have been completed in the previous period or will be completed in the subsequent period, the level of reported income can be erratic, although the level of contract activity may have been relatively constant throughout. Even when numerous contracts are regularly completed in each accounting period, and reported income may appear to reflect the level of contract activity, there is a continuous lag between the time when work is performed and the related revenue is recognised. 40

Selection of Method

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10 29. The selection of a method of accounting for a construction contract depends on the view taken by the contractor in respect of the uncertainties attached to the estimates of contract costs and revenues. In some cases, the contractor may decide that the level of uncertainty warrants the selection of the completed contract method for all contracts. In other cases, the conditions described in paragraph 24 will be satisfied, and some of the contracts may be accounted for using the percentage of completion method. The contractor may be using both methods simultaneously for different types of contracts.

(continued)

20 30. A contractor may use pre-determined criteria for the selection of an accounting method for construction contracts. For example, contracts for which the revenue is less than a stated value, or which have a duration of less than a certain period of time, may be accounted for by the completed contract method even when the conditions specified in paragraph 24 are satisfied.

30 31. The method selected by the contractor under his criteria represents an accounting policy. The accounting policy, including the method of accounting used and the criteria adopted in selecting the method, is consistently applied - see International Accounting Standard 1, Disclosure of Accounting Policies.

40 32. The application of the assumption of consistency requires that if, for example, a contractor uses the percentage of completion method for a particular contract, then all other contracts which satisfy the conditions in paragraph 24 and any pre-determined criteria selected by the contractor, are also accounted for by the percentage of completion method. Similarly, the use of the percentage of completion method for a contract in an accounting period requires the consistent use of the method in subsequent periods if the conditions for the use of the method continue to be satisfied.

Change in Method

33. Where, as a result of a change in an accounting policy, there is a change in the

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(continued)

accounting method used for construction contracts, there is disclosure of the effect of the change and its amount, together with the reasons for the change - see International Accounting Standard 1, Disclosure of Accounting Policies. If the contractor changes from the percentage of completion method to the completed contract method it may not be possible to quantify the full effect of the change in the current accounting period. In such cases there is disclosure, in respect of contracts in progress at the beginning of the accounting period, of at least the amount of attributable profits reported in prior years.

10

PROVISIONS FOR FORESEEABLE LOSSES

34. When current estimates of total contracts costs and revenues indicate a loss, provision is made for the entire loss on the contract irrespective of the amount of work done. In some circumstances the foreseeable losses may exceed the costs of work done to date. Provision is nevertheless made for the entire loss on the contract.

20

35. In circumstances where contracts are of such magnitude that they can be expected to absorb a considerable part of the capacity of the enterprise for a substantial period, some indirect costs to be incurred during the period of the completion of the contracts are considered to be directly attributable to the contracts and included in the calculation of the provision for losses on the contracts.

30

36. If a provision for loss is required, the amount of such provision is usually determined irrespective of:

- (a) whether or not work has commenced on the contract, and
- (b) the stage of completion of contract activity, and
- (c) the amount of profits expected to arise on other unrelated contracts.

40

37. In some cases the determination of a future loss on a contract may be subject to a high degree of uncertainty. Nevertheless, provision for future losses is made on the

basis of all available information. However, explanation is usually given of the circumstances of the contract and the major uncertainties to be resolved.

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CLAIMS AND VARIATIONS ARISING UNDER
CONSTRUCTION CONTRACTS

(continued)

10 38. Amounts due in respect of claims made by the contractor and of variations in contract work approved by the customer, are recognised as revenue in the financial statements only in circumstances where the contractor has evidence of the acceptability of the amount of the claim or variation.

20 39. Claims against or penalties payable by the contractor arising out of delays in completion or from other causes are provided for in full in the financial statements. Claims in the nature of contingencies are treated according to International Accounting Standard -, Contingencies and Events Occurring After the Balance Sheet Date.

PROGRESS PAYMENTS, ADVANCES AND RETENTIONS

40. Progress payments and advances received from customers in respect of construction contracts are disclosed in financial statements, either as a deduction from the amount of contract work in progress or classified as a liability.

30 41. Progress payments due but not received and amounts retained out of contract revenues until the satisfaction of conditions specified in the contract for release of such amounts, are either recognised in financial statements as receivables, with a corresponding deduction from contract work in progress, or alternatively indicated by way of a note.

INTERNATIONAL ACCOUNTING STANDARD

Accounting for Construction Contracts

(continued)

International Accounting Standard comprises paragraphs 42-49 of this Statement. The Standard should be read in the context of paragraphs 1-41 of this Statement and of the Preface to Statements of International Accounting Standards.

10

42. The amount at which work in progress related to a construction contract is included in financial statements should be determined by use of either the percentage of completion method, subject to the criteria in paragraph 43, or the completed contract method.

43. The percentage of completion method may be adopted only if all the following conditions are satisfied:

- (a) total contract revenues can be determined, and 20
- (b) an adequate estimating process exists and both the costs to complete the contract and the percentage of contract performance completed at the reporting date can be reliably estimated, and
- (c) the construction contract is clearly defined and the costs attributable to the contract can be clearly identified so that actual experience can be compared with prior estimates. 30

44. The costs included in the amount at which construction contract work in progress is stated should comprise those which relate to the contract activity.

45. A foreseeable loss on a contract should be provided for in the financial statements, both for the stage of completion reached on the contract and for future work on the contract. If the anticipated losses provided for exceed costs incurred to date on individual contracts, the resulting credit balances should be stated as a liability. 40

Disclosure

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46. The accounting policies adopted for recognising revenue on construction contracts should be applied consistently and disclosed in the financial statements (see International Accounting Standard 1. Disclosure of Accounting Policies).

(continued)

47. There should be disclosure in the financial statements of:

- 10 (a) the amount of construction work in progress, and
- (b) cash received and receivable as progress payments, advances and retentions on account of contracts in progress.

20 If both the percentage of completion method and the completed contract method are simultaneously used by the contractor, the amount of contract work in progress described in (a) above should be analysed to disclose separately the amounts attributable to contracts accounted under each method.

48. If there is a change in an accounting policy for construction contracts that has a material effect in the current period, or may have a material effect in subsequent periods, the effect of the change should be disclosed and quantified, if practicable, together with the reasons for the change.

30 Effective Date

49. This International Accounting Standard becomes operative for financial statements covering periods beginning on or after _____.

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(continued)

CURRENT POSITION OF IASC SUBJECTS		December 1977		
	Issued	Price		
Preface to Statements of International Accounting Standards	January 1975	45p		
International Accounting Standards issued				
IAS 1 Disclosure of Accounting Policies	January 1975	45p		
IAS 2 Valuation and Presentation of Inventories in the Context of the Historical Cost System	October 1975	55p		10
IAS 3 Consolidated Financial Statements	June 1976	50p		
IAS 4 Depreciation Accounting	February 1977	45p		
Exposure Drafts issued				
E5 Information to be Disclosed in Financial Statements	June 1975	45p		20
E6 Accounting Treatment of Changing Prices	January 1976	45p		
E7 Statements of Source and Application of Funds	June 1976	45p		
E8 The Treatment in the Income Statement of Unusual Items and Changes in Accounting Estimates and Accounting Policies	October 1976	45p		30
E9 Accounting for Research and Development Costs	February 1977	45p		
E10 Contingencies and Events Occurring After the Balance Sheet Date	July 1977	45p		
E11 Accounting for Foreign Transactions and Translation of Foreign Financial Statements	December 1977	45p		40
E12 Accounting for Construction Contracts	December 1977	45p		

No. 5

Petition of Appeal to the
High Court

No. 5
Petition
of Appeal
to the High
Court

SUBORDINATE COURTS
SINGAPORE

D.C. Appeal No. 39 of 1979

B E T W E E N

Thomson Hill Limited Appellants

- and -

10 The Comptroller of Income Tax Respondent
(In the Matter of Income Tax Appeal No. 2 of
1978)

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

PETITION OF APPEAL

To the Honourable the Judges of the Supreme
Court.

20 The Petition of the above named Appellants
showeth :

1. The appeal arises from a Notice of
Assessment dated 30th June 1976 for Year of
Assessment 1975, against which assessment the
Appellants appealed to the Income Tax Board
of Review.

2. By judgment dated the 16th day of
May, 1979, judgment was given for the
abovenamed Respondent.

30 3. Your Petitioners are dissatisfied
with the said judgment on the following grounds:-

(1) That the learned Board of Review
erred in law in that no reasons were
given for the rejection of the

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to the
High Court

evidence of Mr. A.J. Coomber, expert witness for the Appellants nor for the learned Board's preference for the evidence of Mr. Yip Thin Peng, witness for the Respondent.

(continued)

- (2) The learned Board of Review erred in fact and law in accepting the evidence of Mr. Yip Thin Peng, witness for the Respondent, who not having had any commercial accounting experience could not have been in a position to give evidence based on personal knowledge as to whether or not the Appellants' treatment of property tax payments was in accordance with "ordinary principles of commercial accountancy". 10
- (3) That the learned Board erred in -a law in not having considered and/or not having given grounds for the rejection of the evidence of Mr. Yang Pah Liang and of Mr. Albert Goh, witnesses for the Appellants. 20
- (4) That the learned Board was influenced and/or had taken into consideration statements of alleged fact relating to accounting principles and practice made by Counsel for the Respondent which statements had not been adduced in evidence. 30
- (5) That these statements of alleged fact relating to accounting principles and practice had not been put to Mr. A.J. Coomber, the expert witness for the Appellants and accordingly he did not have the opportunity to rebut same.
- (6) That the learned Board's finding and decision was against the weight of the evidence. 40
- (7) That the learned Board of Review erred in law and in fact in that they failed to understand the concept and application of the 'completed contract' cost accounting system.
- (8) That the learned Board of Review misdirected itself and erred in

law in holding that the question whether the Appellants were wrong in its previous treatment of property tax payments was of primary importance when the real test was whether the treatment of property tax payments in the year in question was in accordance with "ordinary principles of commercial accountancy".

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(continued)

10

(9) That the learned Board of Review erred in law and fact in failing to give sufficient weight to the "Statement of Standard Accounting Practice No. 9" (SSAP 9) and "Exposure Draft 12 of the International Accounting Standard".

20

(10) That the learned Board of Review erred in law and fact in failing to accept evidence for the Appellants' contentions :-

(i) that the Appellants' treatment of property tax payments for the year 1974 was consistent with "ordinary principles of commercial accountancy"

30

(ii) that the fact that the property tax payments for the year in question had not been included in the costs of development in no way detracted from the "completed contract" method.

40

(iii) that the Appellants' change in the treatment of property tax payments did not amount to a change in the basis or method of accounting but represented merely a refinement of the "completed contract" method of accounting.

(iv) that even if such change in the treatment of property tax payments amounted to a change in the basis or method of accounting (which is denied) there were good reasons for the change.

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of Appeal
to the
High Court

(continued)

- (11) That the learned Board of Review erred in law and fact in holding that although the Appellants had not changed their method of accounting but merely changed their treatment of an item of expense the Appellants had nevertheless to show good reasons for this change when properly once the Board had found that there had been no change in method but merely in the treatment of an item of expense, the Appellants were not required to show good reasons for the change. 10
- (12) That the learned Board erred in law and fact in failing to find that the Appellants had shown good reasons for the change even if such reasons were required (which is denied). 20
- (13) That the learned Board erred in law and on the facts in holding that the onus was upon the Appellants to satisfy the Board that the Appellants' former treatment of property tax payments was wrong and had to be changed.
- (14) That even if the onus of proof was on the Appellants to show that their former treatment of property tax payments was wrong (which is denied), the learned Board erred in law and fact in holding that the Appellants had not discharged their onus of proof when the weight of evidence was to the contrary. 30
- (15) That the learned Board erred in law and fact when in dismissing the Appellants' appeal on the ground that the Appellants had not discharged their onus of proof as set out in paragraphs 13 and 14 above, it failed to consider the Appellants' other contentions that even if good reasons had to be shown for the Appellants' change in the treatment of property tax (which is denied) there were indeed good reasons for the change. 40
50

4. Your Petitioners pray that such judgment may be reversed.

Dated the 4th day of February, 1980.

(Sgd)

SOLICITORS FOR THE APPELLANTS

We hereby consent to this Petition of Appeal being filed out of time.

(Sgd)

SOLICITOR FOR THE RESPONDENT

No. 5
Petition
of Appeal
to the
High Court

(continued)

IN THE HIGH COURT OF THE REPUBLIC OF SINGAPORE

District Court Appeal)
No. 39 of 1979)

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

(In the Matter of Income Tax Appeal No. 2 10
of 1978)

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

JUDGMENT OF CHUA. J.

This appeal arises from a Notice of Assessment dated 30th June, 1976, for Year of Assessment, 1975, against which assessment the appellant company (the Company) appealed to the Income Tax Board of Review (the Board) which dismissed the appeal with costs. The Company now appeals to this Court. 20

The Company was incorporated on 15th April, 1970, as a public company, and carried on business as a housing developer. Since its incorporation the Company purchased various parcels of land, some of which were developed while the others were held in its "land bank". As a consequence of a slump in the property market prevailing in Singapore around 1974, several development projects were halted in mid-stream and were delayed for about five years. 30

In its accounts pertaining to its various development projects the Company has adopted the "completed contract" cost accounting system, whereby profit is recognised only when the contract or project is completed.

Under this system, expenditure incurred in a development together with receipts from booking fees and progress payments are accumulated during the course of the project and profit is not reported until the project is substantially completed.

No. 6
Judgment
of Chua J.

(continued)

10 Each project is treated separately and individual cost records are kept for each project. Development expenses are then capitalised in the balance sheet and are accumulated and carried forward from year to year until the project is completed. Upon completion all the expenses attributable to a particular project are deducted from proceeds of sale, with net profits assessed to tax.

20 For the accounting years 1970 to 1973 property tax incurred annually in respect of properties held by the Company was "capitalised" in the balance sheet as part of the overall development expenditure and did not appear in the profit and loss accounts.

30 However, for the financial year 1974, payments of property tax were for the first time treated as an item of expenditure and charged into the debit side of the profit and loss account. Property tax amounting to \$253,980 was claimed as an item of allowable expenditure under Section 14 of the Income Tax Act (Cap 141) (the Act) against income of the Company.

This change of treatment of property tax payment was not allowed by the Comptroller of Income Tax (the Comptroller) on the grounds that:-

- (i) the property tax paid was not in the production of income assessable to tax for Year of Assessment, 1975;
- 40 (ii) the property tax had been paid in respect of properties that were being developed and should therefore form part of the costs of development;
- (iii) as the development projects were dealt with on a project basis, all direct expenses incurred in connection with each particular project had to be capitalised and

No. 6
Judgment
of Chua J.

allowed against the sale proceeds
received on the completion of the
project.

(continued)

The main point of issue is ground (ii)
of the Comptroller.

The dispute in this appeal is concerned
not with the question whether the property
tax is an allowable deduction per se but
rather with the question of when the
property tax should be allowed as a
deduction.

10

The Company contends that the property
tax of \$253,980 paid in 1974 in respect of
its properties is deductible in the Year of
Assessment, 1975. The Comptroller, on the
other hand, does not dispute that property
tax is a revenue expense that is deductible
under the Act. He is disputing only the
time when the property tax should be
deducted. It is the Comptroller's
contention that on the basis of the
"completed contract" method of accounting
adopted by the taxpayer, the property tax
in respect of each project is deductible
only upon the completion of that
development project.

20

The Company is charged to tax under
Section 10 (1) (a) of the Act, which provides,
inter alia, that "income tax shall be payable
for each year of assessment upon the income
of any person in respect of - gains or
profits from any trade, business, profession
or vocation". The resolution of the
dispute in the present appeal necessitates
an examination of the proper method of
computing the Company's profits or gains
for the Year of Assessment, 1975. The Act
is silent as to the proper methods of
computation.

30

Let us look at the reasons why the
Company changed its previous treatment of
property tax.

40

Reasons for change

Various reasons were given for the
change. The main one was that because of the
slump in the property market in 1974 doubts
were cast about market conditions and the
future viability of various projects which
were halted. Development costs would thus

be increased by the addition of property tax although no development work was carried out. The value of the stock-in-trade would thus be overstated.

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Judgment
of Chua J.

(continued)

10 Another reason was that the Company was advised by its tax advisers that it did not have to "capitalise" property tax because such tax is in no way related to the acquisition of a capital asset, nor did it enhance the value of the properties. Furthermore, since property tax was a revenue expense incurred in the maintenance of the Company's stock-in-trade, it should not be capitalised.

20 Mr. Anthony John Coomber, a practising chartered accountant with a well-established firm of accountants in Singapore, said in evidence that he had seen the accounts of the Company for 1974; that from his perusal, although it did not show any accounting policy used, it appeared to have used completed contracts accounting basis; that it was the most conservative method of computing contracts covering more than one year; and that revenue was recognised when contract was completed or substantially completed.

30 He further said that from the perusal of the Profit & Loss Account it would appear the property tax had been expensed under Profit and Loss Account. He stressed that such a treatment of property tax was not inconsistent with commercial accounting practice and that it was not inconsistent with completed contract accounting basis. He said that property tax should never be capitalised as it did nothing to enhance the value of the property concerned and was paid solely in the period it became payable and certainly
40 produced no benefit lasting beyond such period.

He further said that comparing the accounts for 1974 with previous years, the change in treatment was not wrong, not by itself but there should have been a correction shown of previous years' wrong. This had not been done.

50 He said that the "Statement of Standard Accounting Practice No. 9" (SSAP 9) (Ex. 1) and "Exposure Draft No. 12 of the International Accounting Standard" (Ex. 2)

No. 6
Judgment
of Chua J.

supported his views that the properties of the Company should be treated as trading stocks.

(continued)

SSAP 9 was issued by the Institute of Chartered Accountants in England and Wales in May, 1975, and Ex. 2 was issued in December, 1977. He expressed the view that in view of the standards set out therein, it would now be incorrect to defer property tax, but however, he said in cross-examination that the only instance where he would allow a client to defer property tax was where it was formed only to develop one property.

10

Mr. Yip Thin Peng gave evidence on behalf of the Comptroller. He is qualified as a certified accountant and is the Senior Assessment officer in the Inland Revenue Department. He has been in the Department for sixteen years and in the course of his work he had had experience in dealing with files of property developers.

20

He testified that two methods were normally used to reflect profits - (1) by completed contracts method and (2) by the percentage of completion method.

Under the first method costs of development were accumulated in respect of each project. When completed, profits would be brought into the Profit & Loss Account and assessed for tax. Expenses should be deferred for matching revenue with expenses.

30

Under the second method a company would take account of the progress of development. It would bring in part of the profits earned over the years during which the contracts run. Part of the profits would be assessed to tax.

He said that most property development companies in Singapore adopted the completed contracts method. In so doing, they have treated property tax as part of the costs of development so as to be able to arrive at the true profits of that project and that the Company has adopted the completed contracts method.

40

Since property tax was suffered by the company in maintaining its stock-in-trade,

a developer who developed land would take into account the amount of property tax paid in arriving at the cost of each unit sold. In his view the "practice of capitalising property tax is in accordance with normal accounting practice."

10 He added that a development company was assessed "on a project to project basis as it is completed, not as a whole", although it was taxed from its whole business.

He said that there was nothing in the accounts of the Company to explain the change in the accounting policy. He expressed the view that the change was made to gain a tax savings of over \$100,000, and said that 1974 was the first year the Company reported profits.

20 He expressed the view that the practice of housing developers in "capitalising" property tax was not inconsistent with standards set out in SSAP 9 and Exposure Draft 12 (Ex. 2) and that it was not wrong for a company to change its practice to mitigate tax loss if it conformed to current accounting practice.

The Board in their Grounds of Decision said:

30 "Considering the evidence before us and the submission of counsel, we are of the view that the accumulation of property tax payments by the company pending the completion of the projects in respect of which they are paid, is not inconsistent with ordinary principles of commercial accounting where the "completed contract cost" method of accounting is adopted. We do not accept
40 Mr. Coomber's opinion that such a treatment would only be proper in respect of the accounts of single-development companies."

The Company contends that the Board erred in law and on the facts in holding that the onus was upon the Company to satisfy the Board that the Company's former treatment of property tax was wrong and had to be changed. It says that the real test was whether its new treatment of property tax payments was in accordance with "ordinary principles of
50 commercial accountancy."

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Judgment
of Chua J.

(continued)

The Board was of the view that of primary importance was the question whether the Company was wrong in its previous treatment of property tax payments. The Board found that "it had been clearly established that if a particular method of accounting has been applied consistently in the past it should not be changed, unless good reason is shown for that change (see *Duple Motor Bodies Ltd. v Ostime* ((1961) 2 All E.R. 167, cited with approval in *BSC Footwear Ltd. v Ridgeway*, ((1971) 47 T.C. 495).). The onus of proving that there was good reason for the change falls on the person seeking it."

10

Counsel for the Company contends that the Board has applied the wrong test. He submits that there are two tests applicable - (i) whether the profits of the Company in the year in question were arrived at in accordance with the ordinary principles of commercial accountancy and (ii) whether the deduction of property tax violates any tax statute. Counsel says that he does not discard entirely this so-called "consistency principle" but what he submits is that in the present case the consistency principle is inapplicable for the reasons that there was no change in the Company's method of accounting but merely a change in the treatment of one item namely property tax. He concedes that where there is a change in method the consistency principle is applicable and argues that when it becomes applicable it is not a third test, it is merely part and parcel of the first test namely whether the deduction is in accordance with the ordinary principles of commercial accountancy and that consistency is one of the principles to be observed in commercial accountancy. Counsel says that if it is found that there is a change in method then the Company says that it has good reasons.

20

30

40

Under Section 80(3) of the Act a taxpayer who disputes the Comptroller's assessment must prove that the assessment is excessive. The law as regards the taxpayer's onus of proof in an income tax appeal was summarised succinctly by the Privy Council in Minister of Revenue v Anaconda American Brass Ltd. ((1956) 1 All E.R. 20) wherein Viscount Simonds stated (p. 22):

50

"The question, then, is whether the

Minister correctly assessed the annual net profit or gain of the company for 1947 or, to state the question more accurately, whether the company has established that his assessment was incorrect."

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Judgment
of Chua J.

(continued)

10 The onus is therefore on the Company to prove that the Comptroller's assessment is wrong. In a dispute where the ascertainment of the taxpayer's income for any year involves the application of competing methods or practices of accounting, the taxpayer can only discharge his onus under Section 80 (3) by proving that the accounting practice on which the Comptroller has based his assessment is wrong. In my view it is not sufficient for the taxpayer merely to prove that the taxpayer's practice is also correct. In this case the Company must go further and
20 prove that its former method of accumulating property tax in respect of each project until the completion of the particular housing project was wrong and should be changed.

The Board is quite correct that if a particular method of accounting has been applied consistently in the past it should not be changed unless good reason is shown for that change. The principle of consistency established by Lord Reid in *Duple Motor Bodies Ltd. v Ostime* (39 T.C. 537) should
30 be observed. Lord Reid said (p. 572):

"One thing clearly emerges as approved by the accountancy profession - whatever method is followed, it must be applied consistently. I accept that. So the real question is what method best fits the circumstances of a particular business. And if a method has been applied consistently in the
40 past, then it seems to follow that it should not be changed unless there is good reason for the change sufficient to outweigh any difficulties in the transitional year."

The principle of consistency was approved and applied in the later House of Lords case of *BSC Footwear Ltd. v Ridgeway* (47 T.C. 495). In that case the taxpayer had applied a particular method of valuing stock-in-trade consistently over a number of years. The
50 Crown with appreciation of it had accepted it, but in the year of assessment under

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Judgment
of Chua J.

(continued)

dispute the Crown sought to substitute a new method of valuation. It was held that the onus was on the party seeking the change in the accountancy method to justify the change on the ground that the old method was wrong. It was conceded by counsel for the Crown that in such a situation the Crown could only succeed if it could be proved that the method that had been consistently applied was wrong.

10

In the present case the method of accumulating property tax in the balance sheet had been applied consistently by the Company since its incorporation in 1970. It is the Company who is seeking a change in the accounting treatment of property tax, and, therefore, it is the Company which must prove that the former method was wrong. The Board had directed itself correctly in law in holding that the question of primary importance was whether the Company was wrong in its previous treatment of property tax payments. The Company's contention that the real test was whether its new treatment of property tax payments in the year in question was in accordance with ordinary principles of commercial accountancy is misconceived.

20

The Board also held that "while we agree with the appellants that what they seek is not a change in method of accounting but merely a change in treatment of an item of expense, they must nevertheless show good reason for this change, unless of course the former treatment is wrong".

30

The Company contends that this ruling of the Board is wrong in that the principle of consistency is applicable only where there has been a change in method and once the Board has found that there had been no change in method but merely in the treatment of an item of expense the Company was not required to show good reason for the change.

40

In the Duple Motor Bodies case Lord Reid was using the word "method" to describe the process by which the cost of work-in-progress was to be valued. That process involved the determination of whether items of overhead expenditure could be included in the cost. The taxpayer was not changing

50

(continued)

from one method of valuation to another entirely different method, such as from the "cost or market value method" to the "Base Stock Method". The taxpayer had all along used the cost or market value method. What was in dispute in that case was whether certain items of overhead expenditure should be included in the cost of work-in-progress. Similarly in the present case we are dealing with the determination of the cost of work-in-progress and stock-in-trade to be accumulated in the balance sheet. The issue here is whether an expense such as property tax should be included in the cost of the work-in-progress and stock-in-trade. The problem in these two cases is similar and the dictum of Lord Reid is applicable to the present case.

20 The Company says that the Board erred in law and fact in failing to find that the Company had shown good reasons for the change and that the Board's finding and decision were against the weight of evidence.

The main ground of objection is that the Board was wrong in that it failed to give reasons for the rejection of the evidence of its expert witness, Mr. Coomber, in preference for the evidence of the Comptroller's expert witness, Mr. Yip.

30 The Board was entitled in law to reject the accountancy evidence given by Mr. Coomber. It is an established principle that the ascertainment of a taxpayer's income for tax purposes is primarily a question of law for the sole decision of the Court. In determining the proper tax treatment of a transaction the Court may have recourse to the evidence of accountants. But the evidence of accountants, in itself, can never be conclusive or a question of law. (See *Heather v P-E Consulting Group Ltd.*, 48 T.C. 293 at pages 322 and 323).

50 To succeed in this appeal the Company must prove that the Comptroller's assessment is incorrect. The Comptroller's assessment is based on the Company's previous treatment of accumulating the property tax payments. So to establish that the Comptroller's assessment is incorrect the Company has to prove that its previous method of accumulating property tax was wrong. The primary issue is, therefore, as correctly stated by the

No. 6
Judgment
of Chua J.

(continued)

Board, whether the Company was wrong in its previous treatment of property tax payments.

The primary issue is a question of law for the Board alone to decide. In determining this question of law the Board has to look at all the facts, and consider the accountancy evidence. Lord Denning in *Heather v P-E Consulting Group Ltd.* said (p. 322):

"The Courts have always been advised greatly by the evidence of accountants. Their practice should be given due weight; but the Courts have never regarded themselves as being bound by it. It would be wrong to do so."

10

And Lord Buckley in the same case stated (p. 323);

"Skilled accountants may well be much better qualified than most Judges to formulate and explain such principles; but nevertheless in every case of this kind it is the Judge and not the witness who must decide whether a witness's evidence in fact exemplifies sound accountancy principles. A Judge may, as Lord Wilberforce did in *Strick v Regent Oil Co. Ltd.* 43 T.C. 1, reject the accountant's evidence, or he may accept it."

20

Having heard and seen the witnesses the Board was entitled to accept the evidence of one accountant in preference to the evidence of the others. I am unable to say that the Board was wrong in preferring the evidence of Mr. Yip to that of Mr. Coomber and the other witnesses for the Company.

30

In my view the Board was justified in deciding that "considering the evidence before us and the submissions of counsel, we are of the view that the accumulation of property tax payments by the Company pending the completion of the projects in respect of which they are paid, is not inconsistent with ordinary principles of commercial accounting where the "completed contract cost" method of accounting is adopted."

40

The Company contends that the Board erred in law and fact in failing to find that the Company had shown good reasons for the change in its treatment of property tax.

The reasons brought forward by the Company before the Board did not justify a change in its treatment of property tax and the Board was correct in holding that the Company had failed to discharge the onus that its former treatment of property tax was wrong and must be changed.

No. 6
Judgment
of Chua J.

(continued)

In the result this appeal fails and is dismissed with costs.

10

(Sgd) F A CHUA

Judge

Certified true copy

(Sgd)

Private Secretary to the
Court
Supreme Court, Singapore.

No. 7
Order of
the High
Court

No. 7
Order of the High Court

IN THE HIGH COURT OF THE REPUBLIC OF SINGAPORE

District Court Appeal)
no. 39 of 1979)

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

(In the Matter of Income Tax Appeal No. 2
of 1978)

10

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

ORDER OF COURT

BEFORE THE HONOURABLE MR JUSTICE F A CHUA

IN OPEN COURT

UPON the appeal of the abovenamed
Appellant made by way of Notice of Appeal
dated the 28th day of May 1979 coming on for
hearing on 13th and 14th August 1980 and on
27th August 1980 AND UPON HEARING counsel
for the Appellant and State Counsel for the
Comptroller of Income Tax, IT IS ORDERED THAT:

20

The Appeal be dismissed with costs.

Dated the 14th day of January, 1981.

(Sgd)

ASSISTANT REGISTRAR

No. 8

No. 8
Notice of
Appeal

Notice of Appeal

IN THE COURT OF APPEAL OF THE REPUBLIC OF SINGAPORE

CIVIL APPEAL No. 10 OF 1981

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

10 (In the Matter of D.C. Appeal No. 39 of 1979)

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

NOTICE OF APPEAL

20 Take Notice that Thomson Hill Limited, the above-named Appellants being dissatisfied with the decision of the Honourable Mr. Justice F.A. Chua given at Singapore on the 14th day of January, 1981 appeal to the Court of Appeal against the whole of the said decision.

Dated the 12th day of February, 1981.

(Sgd)

SOLICITORS FOR THE APPELLANTS

To: The Registrar,
Supreme Court, Singapore.

and to: The State Counsel for the
Comptroller of Income Tax, Singapore.

30 The address for service of the Appellants is care of Messrs. Lee & Lee, 18th Floor, U.I.C. Building, No. 5, Shenton Way, Singapore 0106.

No. 9
Petition
of Appeal

No. 9
Petition of Appeal

IN THE COURT OF APPEAL OF THE REPUBLIC OF
SINGAPORE

Civil Appeal No.10 of 1981

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

(In the Matter of D.C. Appeal No. 39 of
1979)

10

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

PETITION OF APPEAL

To the Honourable the Judges of the Court
of Appeal.

The Petition of the abovenamed Appellants
showeth :

1. The appeal arises from a Notice of
Assessment dated 30th June 1976 for Year of
Assessment 1975, against which assessment the
Appellants appealed to the Income Tax Board of
Review.

20

2. By judgment of the learned Board
of Review dated the 16th day of May, 1979,
judgment was given for the abovenamed
Respondent.

3. The abovenamed Appellants appealed
against the said judgment of the learned
Board of Review and on the 14th day of
January, 1981 the Honourable Mr. Justice
Chua dismissed the appeal with costs.

30

4. Your Petitioners are dissatisfied

with the said judgment of the Honourable Mr. Justice Chua on the following grounds:-

No. 9
Petition
of Appeal

(continued)

A. The learned Appellate Judge erred in Law and/or in fact in upholding the decision of the learned Board of Review when :-

- 10 (1) the learned Board of Review had erred in law in that no reasons were given for the rejection of the evidence of Mr. A.J. Coomber, expert witness for the Appellants nor for the learned Board's preference for the evidence of Mr. Yip Thin Peng, witness for the Respondent;
- 20 (2) the learned Board had erred in law in not having considered and/or not having given grounds for the rejection of the evidence of Mr. Yang Pah Liang and Mr. Albert Goh, witnesses for the Appellants:
- (3) the learned Board had been influenced and/or had taken into consideration statements of alleged fact relating to accounting principles and practice made by Counsel for the Respondent which statements:-
- 30 (i) had not been adduced in evidence; and
- (ii) had not been put to Mr. A.J. Coomber, the expert witness for the Appellants who therefore did not have the opportunity to rebut same;
- (4) the learned Board's finding and decision was against the weight of the evidence;
- 40 (5) the learned Board of Review had erred in law and in fact in that they failed to understand the concept and application of the "completed contract" costs accounting system;
- (6) the learned Board of Review had misdirected itself and erred in law in holding that the question whether the Appellants were wrong

No. 9
Petition
of Appeal

in its previous treatment of property tax payments was of primary importance when the real test was whether the treatment of property tax in the year in question was in accordance with "ordinary principles of commercial accountancy";

(continued)

- (7) the learned Board of Review had erred in law and fact in failing to give sufficient weight to the "Statement of Standard Accounting Practice No. 9" (SSAP 9) and "Exposure Draft 12 of the International Accounting Standard"; 10
- (8) the learned Board of Review had erred in law and fact in failing to accept evidence for the Appellants' contentions:-
- (i) that the Appellants' treatment of property tax payments for the year 1974 was consistent with "ordinary principles of commercial accountancy" 20
- (ii) that the fact that the property tax payments for the year in question had not been included in the costs of development in no way detracted from the "completed contract" method
- (iii) that the Appellants' change in the treatment of property tax payments did not amount to a change in the basis or method of accounting but represented merely a refinement of the "completed contract" method of accounting 30
- (iv) that even if such change in the treatment of property tax payments amounted to a change in the basis or method of accounting (which was denied) there were good reasons for the change. 40
- (9) the learned Board of Review had erred in law and fact in holding that although the Appellants had not changed their method of accounting but merely changed their treatment of an item of expense the Appellants had nevertheless to show good reasons for the change 50

when properly once the Board had found that there had been no change in method but merely in the treatment of an item of expense, the Appellants were not required to show good reasons for the change;

10 (10) the learned Board had erred in law and fact in failing to find that the Appellants had shown good reasons for the change even if such reasons were required (which was denied);

(11) the learned Board had erred in law and on the facts in holding that the onus was upon the Appellants to satisfy the Board that the Appellants' former treatment of property tax payments was wrong and had to be changed;

20 (12) even if the onus of proof was on the Appellants to show that their former treatment of property tax payments was wrong (which was denied), the learned Board had erred in law and fact in holding that the Appellants had not discharged their onus of proof when the weight of evidence was to the contrary.

30 B. The learned Appellate Judge was wrong in law and on the facts in holding that the reasons put forward by the Appellants did not justify a change in the treatment of property tax.

5. Your Petitioners pray that such judgment be reversed.

Dated the 25th day of April, 1981.

(Sgd)

SOLICITORS FOR THE APPELLANTS

No. 10
Judgment of
Court of
Appeal

No. 10
Judgment of Court of Appeal

IN THE COURT OF APPEAL OF THE REPUBLIC OF
SINGAPORE

CIVIL APPEAL NO. 10 OF 1981

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

(In the Matter of D.C. Appeal No. 39 of 1979 10

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent)

Coram:

Wee Chong Jin, C.J.
T. Kulasekaram, J.
A.P. Rajah, J.

JUDGMENT

Thomson Hill Ltd., the appellant company, 20
was incorporated on 15th April 1970 and
carries on the business of a housing developer.
The company purchased several properties some
of which it proceeded to develop and the rest
it retained as its "land bank".

Since its incorporation the company in
its accounts pertaining to its development
projects used the "completed contract"
method of accounting. Under this method
revenue is recognised only when the project 30
is completed or substantially completed,
costs and progress payments received are
accumulated during the course of the project,
but profit is not reported until the project
is substantially completed.

The company treated each development
project separately and individual cost records

(continued)

are kept for each project. Development expenses are "capitalised" in the balance sheet and are accumulated and carried forward from year to year until the project is completed. Upon completion all expenses attributable to a particular project are deducted from proceeds of sale and the net profits, if any, are assessed to tax.

10 For the accounting years 1970 to 1973 property tax incurred and paid annually by the company in respect of all its properties was "capitalised" in the balance sheet as part of the cost of the company's properties and did not appear in the profit and loss account. During these accounting years the Comptroller of Income Tax, the respondent, did not object to the company's adoption of the "completed contract" method of accounting and accepted the treatment of
20 the property tax paid in the accounts as part of the cost of the properties and assessed the income tax payable on that basis.

30 However, for the accounting year 1974 the property tax paid amounting to \$253,980.00 was for the first time treated in the accounts as an item of expenditure and charged into the debit side of the profit and loss account and this amount was claimed by the company as an item of deductible expenditure under Section 14(1) of the Income Tax Act (Cap. 141). The Comptroller disallowed this change in the treatment of the property tax payment and assessed the income tax payable accordingly. The company appealed to the Board of Review and the sole issue for determination related to the proper treatment in its accounts of property tax paid by the company in respect of its properties.

40 The Board heard accountancy evidence. In support of the company Mr. Coomber, a practising chartered accountant said that the expensing of the property tax paid under the profit and loss account of the company was not inconsistent with commercial accounting practice and with the "completed contract" method of accounting. He said that property tax should never be capitalised as it does nothing to enhance the value of the property in respect of which property tax is payable and that it
50 would be incorrect to do so.

On the other hand in support of the Comptroller Mr. Yip a certified accountant with no commercial accounting experience but

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Judgment of
Court of
Appeal

(continued)

employed by the Inland Revenue Department for sixteen years said that the practice of capitalising property tax is in accordance with normal accounting practice in the case of a housing developer who adopts the "completed contract" method of accounting. He based his opinion on two publications. One is called "Statement of Standard Accounting Practice No. 9 Stocks and Works in Progress" (SSAP 9) published in May 1975 by the Institute of Chartered Accountants in England and Wales. The other is called "Exposure Draft 12, International Accounting Standard, Proposed Statement, Accounting for Construction Contracts" (Exposure Draft 12) issued for comment in December 1977 by the International Accounting Standards Committee.

10

The Board of Review held that "considering the evidence before us and the submissions of counsel, we are of the view that the accumulation of property tax payments by the company pending the completion of the projects in respect of which they are paid, is not inconsistent with ordinary principles of commercial accounting where the 'completed contract cost' method of accounting is adopted" and dismissed the company's appeal. The High Court on appeal upheld the Board's decision and the company now appeals.

20

In the present case we are concerned with ascertaining the true profit of the company for the year of assessment 1974. That and nothing else, apart from express statutory adjustments, is the subject of taxation in respect of a trade (see *Odeon Associated Theatres Ltd. v Jones* 48 Tax Cases 257). That profit must be ascertained in accordance with the ordinary principles of commercial accounting, including the principle that stock in trade must be brought into account at the beginning and end of the year at its cost or market value whichever is the lower (see *Whimster & Co. v The Commissioners of Inland Revenue* 12 Tax Cases 813 at 823).

30

40

Although accountancy evidence is conclusive on the practice of accountants in the sense of the principles on which accountants act in practice it is for the Court to decide what are the correct principles of the prevailing system of commercial accounting and to apply those principles in order to ascertain the true profit in the particular case (see *Odeon*

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Associated Theatres Ltd. case supra).

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Judgment of
Court of
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(continued)

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It was and is common ground in this case that the company's properties acquired for development (including those in its land bank) are its stock in trade and that the use of the completed contracts accounting method is in accordance with the ordinary principles of commercial accounting. The dispute in this case is whether the property tax paid by the company in respect of its properties is part of their cost. If it is not then the treatment of property tax paid in the 1974 accounts would be in accordance with the ordinary principles of ordinary accounting.

20

On behalf of the company it is submitted that in the present case the correct approach in law is to treat the property tax paid as a straightforward deductible expense and not as part of the cost of the properties as to do so accords with common sense, with the accountancy evidence called by the company and with the principles applied in the case of Duple Motor Bodies Ltd v Catime (39 Tax Cases 537). In the Duple case Viscount Simonds said at page 567:

30

"My Lords, a first principle of tax law is that the taxpayer, in ascertaining his profit, is entitled to debit his expenditure in the year of assessment unless it is excluded by Section 137 of the Income Tax Act, 1952. And this is so although the whole of that expenditure may not bear fruit in that year."

Lord Reid said at page 571 :

40

"It has long been established that you are entitled to include in expenditure for the year all business expenses in that year not excluded by ... Section 137 of the Income Tax Act, 1962, whether or not they can be attributed to the production of goods in that year. It matters not that certain expenditure may have proved abortive, or may have been spent solely with a view to production and profit in some future year and have no relation at all to

50

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Judgment of
Court of
Appeal

(continued)

production during the year of account....
Expenditure which it is permissible to
include in the account is the whole
general expenditure during the period,
and it can only be said to have been
spent to earn the profits of that year
in the sense that it was all spent
during that year to keep the business
going and that, during that year, the
business yielded the profit shown in
the account. So the question is not
what expenditure it is proper to leave
in the account as attributable to goods
sold during the year, but what
expenditure it is proper in effect to
exclude from the account by setting
against it a figure representing
stock-in-trade and work in progress.
You must justify what you seek to
exclude in this way as being properly
attributable to, and properly represented
by, those articles."

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Relying on the Duple case the submission
is that it is for the Comptroller to justify
what he seeks to treat as costs as "being
properly attributable to, and properly
represented by, the stock" and that the
evidence of Mr. Yip relied on by the
Comptroller does not justify the treatment
of property tax as costs.

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The Comptroller's submission is that
under Section 80(3) of the Income Tax Act
the onus is on the company to prove that the
Comptroller's assessment is wrong and that
the Board was justified on the evidence
before it to find that the company had
failed to discharge the onus on it to
satisfy the Board that its former
treatment of property tax was wrong and not
in accordance with the ordinary principles
of commercial accounting. It is also
submitted that the Board was correct in
applying the consistency principle
enunciated by Lord Reid in the Duple case
and referred to with approval by Lord
Morris of Borth-y-Gest in *B.S.C. Footwear
Ltd. v Ridgway* (47 Tax Cases 495) at
page 529:

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"It was recognised by the Special
Commissioners and in the judgments
that good reason must be shown before
giving endorsement to the action of
the Crown in requiring a change of
method of accountancy which the

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Company for at least thirty years had adopted and which the Crown had not in that time challenged. Guidance was given as to this by my noble and learned friend Lord Reid in his speech in Duple Motor Bodies v. Catime.

No. 10
Judgment of
Court of
Appeal

(continued)

10 Following that guidance our concern must be to consider whether the method required by the Crown is better calculated than the method hitherto adopted by the Company to reveal the full amount of the profits or gains of the Company."

Earlier on in his speech Lord Morris at page 528 said:

20 "For many years the Company have kept their accounts upon a particular basis. The Crown with appreciation of it have accepted it. This onus must be upon the Crown to show that the basis is unacceptable and should be changed. As between competing methods and practices of commercial accounting a mere preference for one should not give it priority if the others are not open to objection. What must in the present case be considered is whether the basis which the Company adopted was or was not
30 a basis which would show 'the full amount of the profits or gains' of a particular year : see S.127 of the Income Tax Act, 1952."

The passage of Lord Reid's speech referred to reads as follows:

40 "It appears to me that we must begin at the other end and simply ask what, in all the circumstances of a particular business, is a figure which fairly represents the cost of stock-in-trade and work in progress. One thing clearly emerges as approved by the accountancy profession - whatever method is followed, it must be applied consistently. I accept that. So the real question is, what method best fits the circumstances of a particular business. And if a method has been applied consistently in the past, then it seems to follow that
50 it should not be changed unless there is good reason for the change sufficient to outweigh any difficulties in the transitional year. There might, perhaps

No. 10
Judgment of
Court of
Appeal

(continued)

be good reason for a change in a particular case in the other direction. But I can find nothing in the Case to justify such a change in the present case."

The Board found no good reason for the change in the treatment of the property tax for the accounting year 1974 and that on the accountancy evidence the company had failed to discharge the onus on them to show that the treatment of the property tax in the accounts for the earlier years was wrong in law and in fact. Those findings were accepted by the High Court and we have not been persuaded on the undisputed facts and on the accountancy evidence before the Board that the decision of the Board in dismissing the appeal of the company against the assessment was wrong. The appeal is dismissed with costs.

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(Sgd) S.D. WEE CHONG JIN
CHIEF JUSTICE
SINGAPORE

(Sgd) T. Kulasekaram
Judge

(Sgd) A.P. Rajah
Judge

Singapore, 4th March 1982

Certified true copy

(Sgd)

Private Secretary to the
Hon. the Chief Justice
Supreme Court, Singapore.

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IN THE COURT OF APPEAL OF THE .REPUBLIC OF
SINGAPORE

No. 10
Judgment of
Court of
Appeal

Civil Appeal No. 10)
of 1981)

(continued)

B E T W E E N

THOMSON HILL LTD

Appellant

- and

COMPTROLLER OF INCOME TAX

Respondent

In the Matter of District Court Appeal
No. 39 of 1979

10

B E T W E E N

THOMSON HILL LTD

Appellant

- and -

COMPTROLLER OF INCOME TAX

Respondent

In the Matter of Income Tax Board of Review
Appeal No. 2 of 1978

JUDGMENT

BEFORE THE HONOURABLE, THE CHIEF JUSTICE
MR JUSTICE WEE CHONG JIN, THE HONOURABLE
MR JUSTICE KULASEKARAM AND THE HONOURABLE
MR JUSTICE A P RAJAH

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THE 4TH DAY OF MARCH, 1982

IN OPEN COURT

UPON the appeal of the abovenamed
Appellant made by way of Notice of Appeal
dated the 12th day of February 1981 coming on
for hearing on the 12th and 13th day of
October 1981 AND UPON HEARING Counsel for the
Appellant and State Counsel for the Respondent,
IT IS ADJUDGED THAT:

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- 1) The Appeal be dismissed with costs.
- 2) The sum of \$500 deposited by the
Appellant by way of security for the
Respondent's costs of the Appeal be
paid to the Respondent.

Given under the hand and Seal of the
Supreme Court, Singapore on the 22nd day of
June, 1982.

(Sgd)

ASSISTANT REGISTRAR

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No. 11
Order of
Court of
Appeal
granting
leave to
appeal to
the Judicial
Committee

No. 11
Order of Court of Appeal granting
leave to appeal to the Judicial Committee

IN THE COURT OF APPEAL OF THE REPUBLIC OF
SINGAPORE

Civil Appeal No. 10 of 1981

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent 10

(In the Matter of D.C. Appeal No. 39 of
1979)

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

ORDER OF COURT

CORAM:

THE HONOURABLE THE CHIEF JUSTICE MR. JUSTICE
WEE CHONG JIN 20
THE HONOURABLE MR. JUSTICE LAI KEW CHAI
THE HONOURABLE MR. JUSTICE F.A. CHUA
IN OPEN COURT

THIS 16TH DAY OF AUGUST 1982

UPON reading the Notice of Motion on
behalf of the abovenamed Appellants dated
the 29th day of June 1982 And Upon Reading
the affidavit of Andrew Ang filed herein on
the 29th day of June 1982 and the affidavit
of Lucy Hangchi filed herein on the 11th day
of August 1982 and the exhibit therein referred
to And Upon Hearing Counsel for the above-
named Appellants and State Counsel for the
Respondent THIS COURT DOTH ORDER that the
Appellants be and are hereby granted leave
to appeal to the Judicial Committee of Her
Britannic Majesty's Privy Council against
the whole Judgment of the Court of Appeal 30

given on the 4th day of March.1982,
notwithstanding that the application
herein has not been made within three months
after the date on which the said Judgment
was given.

Given under my hand and seal of this
Court on the 1st day of September 1982.

(Sgd)

Asst. Registrar

No. 11
Order of
Court of
Appeal
granting
leave to
appeal to
the Judicial
Committee

(continued)

No. 12
Certificates
for security
for costs

No. 12
Certificates for security for costs

IN THE COURT OF APPEAL OF THE REPUBLIC OF
SINGAPORE

Civil Appeal No. 10 of 1981

B E T W E E N

Thomson Hill Limited Appellants

- and -

The Comptroller of Income Tax Respondent

(In the Matter of D.C. Appeal No. 39 of
1979)

10

B E T W E E N

Thomson Hill Limited Appellants

- and

The Comptroller of Income Tax Respondent

CERTIFICATE FOR SECURITY FOR COSTS

This is to certify that Thomson Hill Limited of 15th Floor, Far East Shopping Centre, No. 545 Orchard Road, Singapore 0923, the abovenamed Appellants have deposited the sum of Dollars Three thousand only (\$3,000/-) by way of security for the Respondent's costs of the Appeal to the Judicial Committee of Her Britannic Majesty's Privy Council with the Accountant-General, Singapore.

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Dated the 30th day of August 1982.

(Sgd)

Asst. Registrar

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

O N A P P E A L

FROM THE COURT OF APPEAL OF THE REPUBLIC OF SINGAPORE

B E T W E E N:

THOMSON HILL LIMITED

Appellants

- and -

THE COMPTROLLER OF INCOME TAX

Respondent

(IN THE MATTER OF CIVIL APPEAL NO. 10 OF 1981)

RECORD OF PROCEEDINGS

PART I

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Solicitors for the
Respondent