

**American Leaf Blending Co. Sdn. Bhd.**     -     -     -     *Appellant*

v.

**Director-General of Inland Revenue**     -     -     -     *Respondent*

FROM

**THE FEDERAL COURT OF MALAYSIA**

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JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF  
THE PRIVY COUNCIL, DELIVERED THE 18TH JULY 1978

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*Present at the Hearing :*

LORD DIPLOCK

VISCOUNT DILHORNE

LORD EDMUND-DAVIES

LORD RUSSELL OF KILLOWEN

SIR ROBIN COOKE

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*[Delivered by LORD DIPLOCK]*

The appellant taxpayer ("the Company") was incorporated in 1960. The principal object for which it was established was to cut and blend tobacco and to manufacture cigarettes; but, as is usual, its Memorandum of Association incorporated a wide variety of objects including granting licences over and generally dealing with the land rights and other property of the Company.

The Company purchased land in Petaling Jaya whereon it erected a building, which contained a factory in which cigarette-making machinery was installed and a bonded warehouse for storing tobacco and cigarettes. The Company started to manufacture cigarettes there in February 1961; but this proved so unprofitable that the manufacturing business was abandoned in November of the same year and thereafter until 1964 its activities were confined to trading in tobacco. This likewise proved unprofitable and was in turn abandoned in 1964, by which time the Company had accumulated adjusted losses for income tax purposes amounting to \$399,303.00.

With the abandonment of trading in tobacco the Company no longer needed to make use itself of the storage space provided by the bonded warehouse. So in April 1964, it licensed Caxton Press (1957) Ltd. to occupy and use the warehouse for storing paper on what was in effect a monthly tenancy. It is convenient to refer to this and subsequent licences as "lettings" and payments made thereunder as "rents" since they fall within the definition of "rent" in the Income Tax Act, 1967. It does

not appear when this first letting ended; but on 18th January 1965 there was a fresh letting of the warehouse to a new licensee Zuellig Feedmills (Malaya) Ltd. for storing maize. This was a letting until 31st May 1965, terminable then or at any time thereafter on one month's notice. This second letting of the warehouse was followed by a third on 1st October 1966 to Dunlop Malayan Industries Ltd. to store its own goods. This was a three months' letting; it does not appear whether this licensee in fact held over after the expiry of the three months.

In the course of 1967 the cigarette-making machinery which had remained *in situ* in the factory was sold and removed, thus making the factory as well as the warehouse available for letting for storage purposes. On 30th January 1967, the Company let the factory area to Tien Wah Press (Malaya) Ltd. for three months terminable on 30th April 1967 or at any time thereafter on one month's notice.

Finally on 1st October 1968 factory and warehouse were let to Gammon South East Asia Berhad for storage purposes for twelve months terminable on 30th September 1969 or at the end of any subsequent month on six months' notice.

In the years of assessment 1968 and 1970 the Company was assessed to income tax under s.4(d) of the Income Tax Act, 1967, in respect of rents from these lettings. There is no dispute about the figures which amount to \$7,040.00 in 1968 and \$33,234.00 in 1970. The Company, however, claim to be entitled under s.43(1)(a) and (2) to set off against these, and any subsequent assessments, the accumulated adjusted loss of \$399,303.00 until it is exhausted.

The claim was disallowed by the Director-General of Inland Revenue. On appeal it was allowed by the Special Commissioners who, at the request of the Director-General, stated a Case for the opinion of the High Court. The High Court (Sani J.) upheld the Company's claim to be entitled to deduction of the unabsorbed adjusted loss; but Sani J.'s decision on this matter was reversed by the Federal Court (Gill C.J., Ong F.J., Suleiman F.J.). It is from the judgment of the Federal Court that this appeal is brought.

Before the Special Commissioners and in both courts below the Company claimed that it was also entitled to set off against its income from the letting of its property the balance of unabsorbed capital allowances in respect of its tobacco manufacturing business. This claim was rejected by the High Court and the Federal Court. It has been abandoned before their Lordships, who are accordingly concerned only with the appellant's claim under s.43, to have deducted from the assessments on the Company to income tax for 1968 and 1970 the unexhausted balance of adjusted losses incurred in carrying on its tobacco business between 1961 and 1964.

S.43, under which adjusted losses from a business of the taxpayer for previous years of assessment (as ascertained under s.40) are to be deducted from the aggregate of the taxpayer's statutory income for any year for the purpose of ascertaining his chargeable income for that year, draws a distinction between income from "a source consisting of a business" and income from any other source. It is only against income from a source consisting of a business that adjusted losses from a business for previous years of assessment can be set off. The taxpayer's business from which the previous loss was incurred, however, need not be the same business as that from which his statutory income for the year of assessment is derived. So the only question in this appeal is: Were the rents received by the Company for letting its premises or parts thereof to other persons for use for storage, income from "a source consisting of a business" for the purposes of s.43(1)(a) and (2) of the Act?

In support of the contention that they were not, two arguments have been advanced on behalf of the Inland Revenue. The first is general: that as a matter of construction of the Income Tax Act, 1967, income derived from the receipt of rents of premises is incapable of constituting income from a source consisting of a business. The second is special to the instant case: that on the facts found by the Special Commissioners the Company in the years of assessment 1968 and 1970 was not carrying on a business of letting out its premises or, it would seem, any other business at all.

The first and general argument on the construction of the Act failed in both courts below. It can be dealt with shortly by their Lordships. It is based upon the charging section, s.4, which reads as follows:—

“ 4. Subject to this Act, the income upon which tax is chargeable under this Act is income in respect of—

- (a) gains or profits from a business, for whatever period of time carried on;
- (b) gains or profits from an employment;
- (c) dividends, interest or discounts;
- (d) rents, royalties or premiums;
- (e) pensions, annuities or other periodical payments not falling under any of the foregoing paragraphs;
- (f) gains or profits not falling under any of the foregoing paragraphs.”

The contention is that paragraphs (a) to (e) refer to five separate classes of income that are mutually exclusive, in the same way as the various Schedules of the United Kingdom Income Tax Act 1918 were held to be mutually exclusive by the House of Lords in *Fry v. Salisbury House Estate Ltd.* [1930] A.C. 432. As was pointed out by the Judicial Committee in the Jamaican appeal *Commissioner of Income Tax v. Hanover Agencies Ltd.* [1967] 1 A.C.681 the *Salisbury House* case turned on the peculiar structure and provisions of the United Kingdom Act, and threw no light upon the construction of other taxing statutes such as those of Jamaica or Malaysia whose structure and provisions are quite different.

If the words in the various paragraphs of s.4 of the Malaysian Act are given their ordinary meaning—and their Lordships see no reason why they should not be—there is plainly room for overlapping between one paragraph and another. A company may carry on business as an investment or holding company deriving its gains or profits from dividends and interest from the securities it owns. The gains or profit from the business of a bank or moneylender are largely derived from interest received on money lent. A property company or an individual may be carrying on the business of letting premises for rents from which the gains or profits of that business are derived.

That there is potential overlapping between paragraph (a) and paragraphs (c) and (d) is, in their Lordships' view, put beyond doubt by the provisions of s.24. The general rule laid down in ss. 27 and 28 is that income other than income from a business does not become chargeable until it has actually been received. By s.27(1) this is applied specifically to “rent”. The purpose of s.24 is to provide as an exception to the general rule that on computing chargeable income from a business book debts arising in the period of assessment shall be brought into account although not actually received. S.-ss. (4) and (5) apply this exception to dividends and interest on securities held by investment companies and

interest receivable in the course of carrying on a business of lending money; while s.-s. (1)(c) applies the same exception *inter alia* to debts arising "in respect of . . . (c) the use or enjoyment of any property dealt with at any time in the course of carrying on a business."

So it is clear that "rents", despite the fact that they are referred to in paragraph (d) of s.4, may nevertheless constitute income from a source consisting of a business if they are receivable in the course of carrying on a business of putting the taxpayer's property to profitable use by letting it out for rent.

Where premises are let in the course of carrying on the business of putting them to profitable use, s.43(1) in their Lordships' view gives primacy to the classification of the rents receivable as income from a source consisting of a business, notwithstanding that they may also be classified under s.4(d) as "rents". What s.43(1) requires is that one should first determine whether the rents are income from a business. If they are, no further inquiry is necessary; adjusted losses from a business of the taxpayer for previous years of assessment are deductible in ascertaining the taxpayer's aggregate income. Thus on the question of construction of the Act their Lordships are in agreement with the High Court and the Federal Court.

On the question special to the instant case, viz. whether the Company in 1968 and 1970 was carrying on a business of letting out its premises for rents, the Special Commissioners were of opinion that it was. The question is one of fact, and in the High Court Sani J. treated this expression of opinion as a finding of fact by the Commissioners which he should not disturb. Closer analysis of the Stated Case, however, discloses that the opinion expressed by the Special Commissioners was not a finding of fact but a conclusion of law. They accepted the Company's submission that because the letting of its property was one of the objects set out in its Memorandum of Association this was in law conclusive that in making any letting of its premises it was carrying on a business.

So stated this is, in their Lordships' view, too broad a proposition. It derives apparent support from an observation of Pollock M.R. in *Inland Revenue Commissioners v. Westleigh Estates Co.* [1924] 1 K.B. 390, 409, where he said:

"If [a company's] objects are business objects and are in fact carried out it . . . carries on business".

This, however, was said in the context of a company which was carrying out one of the principal objects stated in its Memorandum. Their Lordships would not endorse the view that every isolated act of a kind that is authorised by its Memorandum if done by a company necessarily constitutes the carrying on of a business.

On the other hand their Lordships do not think that the dicta to be found in some of the speeches in the *Salisbury House* case and in particular those of Lords Warrington of Clyffe and Macmillan upon which the Federal Court relied and which suggest that the letting of land does not constitute a "trade", have any relevance to the question whether the letting of land by the Company in the instant case amounted to the carrying on of a "business" within the meaning of the Malaysian Income Tax Act, 1967. "Business" is a wider concept than "trade"; and in the *Hanover Agencies* case the Board uttered a warning against seeking to apply these dicta outside the narrow context of British income tax law and in particular that of Schedule D.

In the case of a private individual it may well be that the mere receipt of rents from property that he owns raises no presumption that he is carrying on a business. In contrast, in their Lordships' view, in the case

of a company incorporated for the purpose of making profits for its shareholders any gainful use to which it puts any of its assets *prima facie* amounts to the carrying on of a business. Where the gainful use to which a company's property is put is letting it out for rent, their Lordships do not find it easy to envisage circumstances that are likely to arise in practice which would displace the *prima facie* inference that in doing so it was carrying on a business.

The carrying on of "business", no doubt, usually calls for some activity on the part of whoever carries it on, though, depending on the nature of the business, the activity may be intermittent with long intervals of quiescence in between. In the instant case, however, there was evidence before the Special Commissioners of activity in and about the letting of its premises by the Company during each of the five years that had elapsed since it closed down its former tobacco business. There were three successive lettings of the warehouse negotiated with different tenants; there was the removal of the machinery from the factory area which made it available for use for storage and a separate letting of that area to a fresh tenant; and as recently as October 1968 there was the negotiation of a letting to a single tenant of both the factory area and the warehouse.

As has been mentioned, the question whether the Company were carrying on a business of letting out their premises for rent was one of fact for the Special Commissioners: but it is one to which they did not apply their minds because of their mistake of law as to the effect of the presence in the Company's Memorandum of power to let their premises or any part thereof. Nevertheless their Lordships do not find it necessary to require the case to be remitted to the Special Commissioners for further consideration; for, in their Lordship's view, upon the evidence to which they have referred there is only one conclusion of fact that any reasonable Commissioners could reach, viz. that there is nothing in the evidence capable of rebutting the *prima facie* inference that in the relevant periods of assessment the Company was carrying on a business of letting out its premises for rent. On the contrary the evidence serves only to reinforce that *prima facie* inference.

Their Lordships will advise His Majesty the Yang di-Pertuan Agong that the appeal be allowed, the order of the Federal Court set aside and the order of the High Court restored. They will further advise that the respondent pay the costs of this appeal but that there be no order as to the costs in the Federal Court or the High Court.

In the Privy Council

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