CACV 154/2002

IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
COURT OF APPEAL

CIVIL APPEAL NO 154 OF 2002
(ON APPEAL FROM HCIA NO. 3 OF 2001)

BETWEEN

CHEUNG WAH KEUNG Appellant

and

COMMISSIONER OF INLAND REVENUE Respondent

Before: Hon Woo, Cheung and Yeung JJA
Date of Hearing: 7 November 2002
Date of Judgment: 19 November 2002

J U D G M E N T

Hon Woo JA (giving the judgement of the Court):

1. This is an appeal against the judgment dated 21 January 2002 of Deputy High Court Judge Poon. In his judgment, the Judge dismissed an appeal by way of case stated brought by the Appellant Taxpayer pursuant to s 59 of the Inland Revenue Ordinance, Cap 112 ("the Ordinance") against the decision No D39/00 of the Board of Review ("the Board") dated 6 July 2000.

Agreed facts

2. As recorded in the stated case dated 20 August 2001, certain facts were agreed by the parties.

(1) Sun Ling

3. Sun Ling Motors Company Limited ("Sun Ling") is a motorcar dealer. The shareholders and directors of Sun Ling do not have any relationship with either the Taxpayer or First-Rate Company Limited ("First-Rate"). For the years 1991 to 1995, Sun Ling as principal and First-Rate as manager entered into annual service contracts entitled "Contract for the Manager". The contracts invariably made the following provisions:

(1) The manager was to provide manpower and resources to provide service for the principal. Any manpower or resources engaged directly or indirectly by the manager should not constitute any employer and employee relationship or any legal responsibility with the principal. The duty of the manager covered all matters with regard to car dealership and the matters between the principal and its client.

(2) The manager represented the principal in the capacity as its sales manager but this capacity was to facilitate the manager in representing the principal dealing in motor vehicle transactions and other matters. It did not constitute employer and employee relationship.

(3) First-Rate agreed to authorize the Taxpayer to be fully responsible for observing and performing the contract.

(4) Service hours were between 9:30 am to 7:00 pm, Monday to Saturday.

(5) Monthly service fees were $7,000 for the 1991 contract; $8,500 for the 1992 contract; $9,000 for the 1993 contract; $11,000 for the 1994 contract and $12,300 for the 1995 contract, with additional telephone allowance of $1,000 per month and commission for motor vehicle transactions. The principal would at the end of the year give a special remuneration to the manager having regard to the business performance. The minimum amount of special remuneration should be at least one month of the service fees.

(6) Both parties could terminate the contract by giving one month's notice or one month's service fees of the manager. If the notification period was under one month, then the rate should be computed pro rata.

(7) All labour and medical insurance of persons engaged by the manager should be paid for by the principal.

4. For the years of assessment 1992/93 to 1994/95, Sun Ling paid to First-Rate commission and fees in the respective sums of $451,397, $495,578 and $358,155. In the year of assessment 1995/96, the total service fee, commission and fees, and allowance and compensation amounted to $199,162.

(2) First-Rate

5. First-Rate is a private company incorporated in Hong Kong on 26 November 1982. The Taxpayer has since 12 July 1985 been its director and been holding 80% of the issued capital of $100,000.

6. First-Rate closed its rented office in May 1989 and has since maintained a registered business address with its company's secretary and tax representatives.

7. First-Rate reported in its financial statement for the years of assessment 1992/93 to 1995/96 that its principal activity was acting as a commission agent. During the five years ended 31 March 1993 to 1997, First-Rate reported the following commission income:

Year of Assessment	1992/93	1993/94	1994/95	1995/96	1996/97
	$	$	$	$	$
Sun Ling	451,397	495,578	358,156	199,162	-
Set Wing Trading Co. Ltd.	44,000	-	-	-	-
Kar Wo Electric Work	12,667	-	-	-	-
Auto Trade Centre	30,000	-	-	-	-
England Motors and Trading Ltd.	-	-	-	-	63,462
Suttgart Auto Centre	-	-	-	5,000	-
Miscellaneous	-	-	-	94,530	-
Total as per audited accounts	538,064	495,578	358,156	298,692	63,462

8. The assessable profits/(adjusted loss) before set-off of the loss brought forward as per First-Rate's tax returns for the years of assessment 1992/93 to 1995/96 were respectively $15,150, ($13,666), $15,197 and ($61,204). First-Rate did not have any assessable profits for the years of assessment 1992/93 to 1995/96 after set-off of loss brought forward. The assessor issued computations showing the loss positions of First-Rate for those years as per its returns.

(3) The Taxpayer

9. In his salaries tax return or tax returns - individuals for the years of assessment 1992/93 to 1995/96, the Taxpayer's only declared income was that received from First-Rate. The assessor raised salaries tax assessments in accordance with the income reported in the tax returns submitted. The figures included income and quarters value and after deducting allowance. The net chargeable income was $20,000 for 1992/93, $43,000 for 1993/94, $20,000 for 1994/95 and $22,000 for 1995/96. The tax payable was respectively $400, $2,470, $400 and $400.

10. On 23 March 1999, an Assistant Commissioner raised on the Taxpayer the

following additional salaries tax assessments for the years of assessment 1992/93 to 1995/96 under s 61A of the Ordinance:

Year of Assessment	1992/93	1993/94	1994/95	1995/96
	$	$	$	$
Income from First-Rate	95,000	90,000	92,000	90,000
Sun Ling via First-Rate	451,397	495,578	358,155	199,162
	546,397	585,578	450,155	289,162
Quarters value	9,500	9,000	-	9,000
	555,897	594,578	450,155	298,162
Less: Allowances	-	-	-	79,000
Net Chargeable Income ("NCI")	555,897	594,578	450,155	219,162
Less: NCI already charged	20,000	43,000	20,000	20,000
Additional NCI	535,897	551,578	430,155	199,162
Tax Payable on NCI	83,384	89,186	67,523	36,032
Less: Tax charged	400	2,470	400	400
Additional Tax payable	82,984	86,716	67,123	35,632

11. There was an "Assistant Commissioner's Note" in the notice of additional salaries tax assessments, which reads:

> "It is my view that the interposition of First Rate Company Limited between Sun Ling Motors Company Limited and your goodself is a scheme entered into for the sole or dominant purpose of enabling you to obtain a tax benefit. It is a form of disguised employment. As such, the scheme is challengeable by authority of Section 61A of the Inland Revenue Ordinance and the income allegedly received by First Rate Company Limited from Sun Ling Motors Company Limited is now treated as your income from the employment with the later."

12. The notice of the additional salaries tax assessments had the name of the Commissioner of Inland Revenue printed on it.

Objection and determination

13. The Taxpayer duly raised objection against the additional tax assessments on the grounds that the assessments were excessive, unrealistic and not in accordance with the tax returns previously filed and that the Taxpayer had no relationship or employment with Sun Ling.

14. The Acting Deputy Commissioner did not accept the objection. On 20 August 1999, he issued his determination to the Taxpayer under s 64(4) of the Ordinance. Further, pursuant to s 64(2) of the Ordinance, he increased the additional salaries tax assessment for 1994/95 to $68,503 by adding $9,200 for quarters value which was omitted in the original additional assessment.

Appeal to the Board

15. On 2 September 1999, the Taxpayer appealed against the Determination pursuant to s 66 of the Ordinance. The grounds of appeal were that the additional salary tax assessments were incorrect, excessive and not in accordance with the tax returns previously submitted. Further, none of the income of the additional assessments was accrued to the Taxpayer and the Taxpayer did not receive such income. In addition, both the assessor and the Commissioner failed to identify the transaction to which s 61 and 61(A) of the Ordinance were applied.

Findings by the Board of additional facts

16. The Board made the following findings of additional facts relevant to the case:

(1) At all material times, First-Rate had three directors: the Taxpayer, the Taxpayer's son and one Au Yu Lan. Au resigned in September 1995.

(2) The Taxpayer's son was born in 1973. He was a student in 1992 and was wholly maintained by the parents.

(3) The Taxpayer admitted in evidence that First-Rate was controlled and operated by him.

(4) First-Rate entered into the five contracts with Sun Ling according to which First-Rate was to assign the Taxpayer to render services to Sun Ling.

(5) The five addresses which the Taxpayer gave on his name card with Sun Ling were all Sun Ling's addresses, including showroom, service centres and workshops.

(6) For services rendered by the Taxpayer, the following payments were made by Sun Ling to First-Rate, being a fixed rate of remuneration, commission based on transactions completed, and special bonus based on the overall performance of Sun Ling. In addition, Sun Ling agreed to pay for the labour insurance and the medical insurance in respect of the Taxpayer.

(7) As per his tax returns, the Taxpayer received director's salaries from First-Rate, namely, $95,000 for 1992/93, $90,000 for 1993/94, $92,000 for 1994/95 and $90,000 for 1995/96. Although First-Rate reported director's salaries to be $141,000 and $146,000 for 1992/93 and 1993/94 respectively, the balance of $46,000 for 1992/93 and the balance of $56,000 for 1993/94 were salaries purportedly given to the Taxpayer's son. In his evidence, the Taxpayer said he did not know the details of the figures. But the Board found that these salaries were conveniently pitched at $46,000 and $56,000 for the relevant years so that the Taxpayer's son could claim his full personal allowance. These salaries were nothing more than a book entry.

(8) Except for the director's salaries aforesaid, First-Rate did not pay any wages or salaries, indicating strongly that no one other than the Taxpayer was available from First-Rate to render services to Sun Ling. Further, as one of the conditions of the contracts, First-Rate specially assigned the Taxpayer to render services to Sun Ling.

(9) The terms of the contracts between Sun Ling and First-Rate pointed to an employer and employee relationship between Sun Ling and the Taxpayer but for the interposition of First-Rate.

The Board's decision

17. The Board identified two main issues for its decision:

(a) whether s 61 or s 61(A) was applicable to the interposition of First-Rate between Sun Ling and the Taxpayer; and

(b) whether the income paid by Sun Ling should be assessed as the Taxpayer's income from employment.

18. The Board dismissed the appeal. In essence the reasons are as follows:

(1) Without the interposition of First-Rate, the Taxpayer would not be able to claim as deductions his personal and private expenses. When First-Rate was interposed between Sun Ling and the Taxpayer, the Taxpayer's expenses would be disguised as director's benefits of First-Rate and claimed by First-Rate as deductible and as a result the Taxpayer's ultimate salaries tax liabilities were reduced. There was no commercial reality in the transaction (consisting of the five contracts between Sun Ling and First-Rate and the interposition of First-Rate between Sun Ling and the Taxpayer) which was aimed at procuring the services of the Taxpayer to Sun Ling and reducing the Taxpayer's tax liabilities. It was commercially unrealistic and therefore artificial within the meaning of s 61 and should be disregarded. Accordingly, the payments made by Sun Ling to First-Rate should be treated as the Taxpayer's income.

(2) As to s 61A, the Board drew the inference that the Assistant Commissioner had had regard to the seven elements in s 61A before forming his view. If there should be any doubt about the Assistant Commissioner's compliance with s 61A, the Acting Deputy Commissioner, in his determination, showed clearly that he had duly considered the seven elements before endorsing the view of the Assistant Commissioner. Having examined the seven elements in the light of the circumstances of the case, the Board also concluded that the transaction was entered into for the sole or dominant purpose of obtaining a tax benefit.

(3) The Board was not persuaded that the Taxpayer had discharged the

burden imposed upon him by s 68(4) of the Ordinance of proving that the assessments appealed against were incorrect or excessive.

Questions of law stated

19. By the case stated dated 20 August 2001, the Board raised the following questions of law for the determination of the Court of First Instance pursuant to s 69 of the Ordinance:

(a) Did the Board err in law in invoking s 61A of the Ordinance when it had concluded that the Taxpayer's transaction, consisting of the five contracts between Sun Ling and First-Rate and the interposition of First-Rate between Sun Ling and the Taxpayer, should be disregarded under s 61 of the Ordinance?

(b) Did the Board err in law in concluding that s 61 and s 61A were both applicable to the Taxpayer's said transaction?

(c) Did the Board err in law in concluding on the facts as found by the Board that the Taxpayer's said transaction was artificial or fictitious?

(d) Did the Board err in law in concluding on the facts as found by the Board that the Taxpayer's said transaction was entered into or carried out for the sole or dominant purpose of enabling the Taxpayer to obtain a tax benefit?

(e) Did the Board err in law in failing to impose on the Commissioner the burden of proving that a case had been made out for invoking s 61 and s 61A?

The appeal to the Court of First Instance

20. The appeal was heard by the Judge and on 21 January 2002 he gave judgment dismissing the Taxpayer's appeal and answered all the five questions raised in the stated case in the negative.

The present appeal

21. By a Notice of Appeal dated 16 February 2002, the Taxpayer now appeals to this Court against the Judge's decision. He seeks an order from this Court to set aside the Judge's judgment and for an order that the additional salaries tax assessments for the four years in question be allowed.

22. A number of grounds are raised. They will be dealt with in turn below, but before doing so, it is to be noted that a number of these grounds were not raised before the Board or the Judge. The point to be resolved first is whether such grounds could or should be entertained by this Court now. In *Rico Internationale Ltd v CIR* [1965] 1 HKLR 493 @ 506-507 Scholes J said:

> "... I would however say that in my opinion this court may consider newly raised points of law, and the position in my opinion is clearly stated in the case of the **Attorney General v Avelino and Co.** in which Atkin L.J. (as he then was) said:--
>
> 'Nevertheless upon the facts found by the special Commissioners in the case it is apparent that their decision was wrong in point of law, and that is all that is necessary to enable this Court to give effect to the point of law. As I read the statutory procedure, which at that time depended on s. 59 of the Taxes Management Act, 1880, the Court is not limited to particular questions raised by the Commissioners in the form of questions on the case. All that the section provides is that if the appellant is dissatisfied with the determination as being erroneous in point of law he may require the Commissioners to state and sign a case, and the case shall set forth the facts and the determination, and upon that being done the Court has to decide whether or not the determination was or was not erroneous in point of law, and any point of law that can be raised properly upon the facts found by the Commissioners the Court can decide. No doubt there may be a point of law in respect of which the facts have not been sufficiently found, and if that point of law was not raised below at all and cannot be raised without further facts on either side, the Court may very well refuse to give effect to it, and either party may have precluded themselves by their conduct from raising in the Court of Appeal the point of law which they deliberately refrained from raising down below. Those questions, of course, have to be considered. But apart from that, if the point of law or the erroneous nature of the determination of the point of law is apparent from the case as stated, and there are no further facts to be found, the Court can give effect to the law.' "

Blair-Kerr J also had this to say at p 522:

> "In my view, the fact that the Board were not asked to, and did not, include the specific questions of law raised before this court and before the learned judge, is not fatal to this appeal."

23. In *CIR v Emerson Radio Corp* [1999] 2 HKLRD 671, at 680A-C, Rogers JA said:

> "... s 69(5) [of the Inland Revenue Ordinance] reads:
>
> Any judge of the High Court shall hear and determine any question of law arising on the stated case and may in accordance with the decision of the court upon such question confirm, reduce, increase or annul the assessment determined by the Board, or may remit the case to the Board with the opinion of the court thereon. Where a case is so remitted, the Board shall revise the assessment as the court may require.
>
> The Recorder below considered that on its own, the wording of s. 69 would preclude the High Court from considering any question of law were it not

> contained in the case stated. I consider however that the words of s. 69(5) should be given a more liberal interpretation and that the Court would be empowered to determine a question of law which it considered arose from the case stated.
>
> On the basis of authority however, the Recorder held that it was open to the Court to determine a question of law if it arose out of the case stated. For my part, I would also agree with this and I do not consider it necessary to go through those authorities or to comment further thereon other than to say that if the matter be a new point not argued before the Board, there may be problems caused by the fact that sufficient facts have not been found by the Board which would preclude a court from hearing and determining a question or would dictate that the case be remitted for further consideration. Be that as it may, in my view, the point raised fails."

23. The terms of s 69(5) referred to in the cited passage above remain the same as at present save that "the High Court" has been altered to read "the Court of First Instance". It can be seen, therefore, both our courts and the English courts have allowed points of law to be raised although they had not been raised in the Board or in the case stated by the Board, save where the facts which forms the foundation of the point have not been found by the Board or cannot be established by the evidence adduced before the Board. S 69(7) of the Ordinance provides:

> "Appeals from decisions of the Court of First Instance under this section shall be governed by the provisions of the High Court Ordinance (Cap. 4), the Rules of the High Court (Cap. 4 sub. Leg.), and the Orders and Rules governing appeals to the Court of Final Appeal."

24. While there are no provisions in the High Court Ordinance or Rules as to how a new point of law should be dealt with in the Court of Appeal, what Bokhary PJ said in *Flywin Co Ltd v Strong & Associates Ltd*, FACV No 15/2001, applies equally to the Court of Final Appeal as to the this Court. After referring to Lord Herschell's judgment at p 225 of *The Tasmania* (1890) 15 App Cas 223, Bokhary PJ had the following to say:

> "38. ... What is involved in a general principle. Where a point is taken at the trial, the facts pertaining to it are open to full investigation at the evidence-taking stage of the litigation. That is as it should be. Therefore where a party has omitted to take a point at the trial and then seeks to raise that point on appeal, the position is as follows. He will be barred from doing so unless there is no reasonable possibility that the state of the evidence relevant to the point would have been materially more favourable to the other side if the point had been taken at the trial.
>
> 39. Clearly the foundational imperative of the 'state of the evidence' bar, as I propose to call it, is fairness. ..."

25. The authorities clearly establish that a point of law, which was not raised in the Board or in the court below, can and should be considered by this Court save where the "state of the evidence bar" applies. We now turn to consider the grounds of appeal

seriatim.

Ground 1a

26. Ground 1a contends that the Judge erred in finding that the Board had invoked s 61 and s 61A in the alternative when the reasoning of the Board clearly shows that the Board had applied the sections simultaneously. The basis of the argument is that while the Judge held that the Board had applied s 61 and s 61A in the alternative, the Board in fact ruled that s 61 applied to the transaction in question and then went on to find that s 61A applied. Nowhere in the case stated did the Board use the word "alternative" in relation to the application of the two sections. It is therefore contended that the Board applied both sections simultaneously without choosing one of them.

27. The matter arose in the following manner. When the Assistant Commissioner made the additional assessments for the four years, his Note referred to in para 11 above shows clearly that he relied on s 61A to hold that the contracts in those four related years between Sun Ling and First-Rate were entered into for the sole or dominant purpose of enabling the Taxpayer to obtain a tax benefit and on that basis he treated the income allegedly received by First-Rate from Sun Ling as the Taxpayer's income from the employment with Sun Ling. However, when the Taxpayer objected to the assessment, the Acting Deputy Commissioner by his determination not only affirmed the assessments but also increased that for the year of assessment 1994/95 (see para 14 above). According to the Taxpayer's case before the Board, set out in para 8.2 of the stated case:

> "... when the Acting Deputy Commissioner made his Determination, he relied on an additional section, i.e. section 61 of the Ordinance."

The Board held that it was not improper for him to invoke s 61 in his determination. The Board then went on to consider issues relating to s 61A as raised by the Taxpayer. It is now convenient to set out the relevant provisions of these two sections:

> 61. Where an assessor is of opinion that any transaction which reduces or would reduce the amount of tax payable by any person is artificial or fictitious or that any disposition is not in fact given effect to, he may disregard any such transaction or disposition and the person concerned shall be assessable accordingly.
>
> 61A. (1) This section shall apply where any transaction has been entered into or effected ... and that transaction has, or would have had but for this section, the effect of conferring a tax benefit on a person (in this section referred to as 'the relevant person'), and having regard to –
>
> (a) the manner in which the transaction was entered into or carried out;
>
> (b) the form and substance of the transaction;
>
> (c) the result in relation to the operation of this Ordinance that, but for this section, would have been achieved by the transaction;

(d) any change in the financial position of the relevant person that has resulted, will result, or may reasonably be expected to result, from the transaction;

(e) any change in the financial position of any person who has, or has had, any connection (whether of a business, family or other nature) with the relevant person, being a change that has resulted or may reasonably be expected to result from the transaction;

(f) whether the transaction has created rights or obligations which would not normally be created between persons dealing with each other at arm's length under a transaction of the kind in question; and

(g) the participation in the transaction of a corporation resident or carrying on business outside Hong Kong,

it would be concluded that the person, or one of the persons, who entered into or carried out the transaction, did so for the sole or dominant purpose of enabling the relevant person, either alone or in conjunction with other persons, to obtain a tax benefit.

(2) Where subsection (1) applies, the powers conferred upon an assessor under Part X shall be exercised by an assistant commissioner, and such assistant commissioner shall, without derogation from the powers which he may exercise under that Part, assess the liability to tax of the relevant person –

(a) as if the transaction or any part thereof had not been entered into or carried out; or

(b) in such other manner as the assistant commissioner considers appropriate to counteract the tax benefit which would otherwise be obtained.

(3) In this section –

"tax benefit" means the avoidance or postponement of the liability to pay tax or the reduction in the amount thereof; ...

28. Having looked at the case stated by the Board carefully, we are not at all persuaded that the Board had applied s 61 and s 61A simultaneously as alleged by the Taxpayer. In our judgment, the Board considered the applicability of s 61 first and went on to deal with the applicability of s 61A in response to the arguments raised by the Taxpayer that there was no evidence that the Assistant Commissioner had considered the seven elements of s 61A.

29. Anyhow, we are unable to see how the point raised by ground 1a can have any significant bearing on the case for the Taxpayer. The appeal to the Board was against the determination of the Acting Deputy Commissioner who relied on s 61 although that determination arose out of the assessment made by the Assistant Commissioner who relied on s 61A. What seems to us to be the contention is that since s 61 had been applied, whereby the transaction in question had been treated as void, s 61A cannot have any further application to a void transaction. This is one of the most unattractive arguments we have ever come across. The disregarding provision in s 61 does not mean that the transaction is void: it is simply to be disregarded when the conditions in s 61 are satisfied. The provision in s 61A(2)(a) also gives similar power to disregard the transaction. There is no indication in the two sections, both aiming at tax-avoidance schemes, or indeed in other provisions of the Ordinance that the application of the two sections is mutually exclusive.

30. During the course of argument before us, the parties by consent produced the Determination of the Acting Deputy Commissioner dated 20 August 1999 which, for reasons unknown, was not made available to the Judge. This document shows that in giving the reasons for his determination to confirm the additional assessments, the Acting Deputy Commissioner referred to s 61 at one instance. After stating the terms of the section, he said:

> "In this case, it is commercially unrealistic for the Taxpayer to draw a meagre salary which is incommensurate with the product of his efforts – the commission received by First-Rate."

31. He then went on to deal with s 61A (the provision relied on by the Assistant Commissioner in making the additional assessments) and considered the seven factors mentioned in subsections (a) to (g) of the section resulting in his endorsing the view of the Assistant Commissioner. This is clear indication that the additional assessments were confirmed by the determination on the basis of s 61A, but the Acting Deputy Commissioner merely expressed the view that s 61 would also apply.

32. This reinforces our view that this ground has no merit.

Ground 1b

33. Ground 1b alleges that the Judge erred in not setting aside the s 61 assessment, which was made by the Acting Deputy Commissioner in the course of his duty of considering the objection of the Taxpayer to the assessments made under s 61A, thus being made by the Acting Deputy Commissioner in excess of his jurisdiction.

34. The argument runs as follows. The terms of s 61 are clear that the assessment under it is to be made by the assessor. By s 3(4) of the Ordinance, the assessor's powers may be exercised by an assistant commissioner, and not a deputy commissioner. Under s 64(2) of the Ordinance, in respect of an objection the Commissioner "may confirm, reduce, increase or annul the assessment objected to". As there is no provision in s 64(2) for the Acting Deputy Commissioner to make a further assessment in the course of the determination it was not open to him to invoke s 61.

35. In view of the contents of the Determination disclosed to this Court, Mr Thomson, for the Taxpayer, abandons this ground. It is therefore unnecessary for us to deal any further with it.

Ground 1c

36. Ground 1c alleges that the Judge erred in concluding that the term "artificial or fictitious" which is synonymous with sham might be equated with, or inclusive of, the term "commercially unrealistic".

37. This ground takes the relevant part of the Judge's judgment out of context. The judge was referring to the holding of the Board in para 22 of his judgment in the process of answering question (a) raised by the stated case [see para 19 above] before him:

> "It [the Board] first held that the transaction was artificial within the meaning of section 61 in that it was commercially unrealistic and should be disregarded."

38. Mr Cooney, for the Commissioner, points out that it was not argued before the Judge that the Board was wrong in equating "artificial" with "commercially unrealistic". Since the point is now raised, Mr Cooney submits that the Board did not make any mistake in this regard.

39. The meaning of "artificial or fictitious" has been dealt with in *Seramco Trustees v Income Tax Commissioners* [1977] AC 287, where Lord Diplock giving the judgment of the Privy Council stated at p 298:

> "'Artificial' is an adjective which is in general use in the English language. It is not a term of legal art; it is capable of bearing a variety of meanings according to the context in which it is used. In common with all three members of the Court of Appeal their Lordships reject the trustees' first contention that its use by the draftsman of the subsection is pleonastic; that is, a mere synonym for 'fictitious.' A fictitious transaction is one which those who are ostensibly the parties to it never intended should be carried out. 'Artificial' as descriptive of a transaction is, in their Lordships' view a word of wider import. Where in a provision of a statute an ordinary English word is used, it is neither necessary nor wise for a court of construction to attempt to lay down in substitution for it, some paraphrase which would be of general application to all cases arising under the provision to be construed. Judicial exegesis should be confined to what is necessary for the decision of the particular case. Their Lordships will accordingly limit themselves to an examination of the shares agreement and the circumstances in which it was made and carried out, in order to see whether that particular transaction is properly described as 'artificial' within the ordinary meaning of that word."

40. The term "commercially unrealistic" appears in *CIR v Howe* (1977) 1 HKTC 936 at p 952 in the sense of "unrealistic from a business point of view". We are of the view that whether a transaction which is commercially unrealistic must necessarily be

regarded as being "artificial" depends on the circumstances of each particular case. We agree with the submission of Mr Cooney, however, that commercial realism or otherwise can be one of the considerations for deciding artificiality. In the present case, the Board found as a fact that there was no "commercial reality in the transaction" and that there "simply was no commercial sense in the transaction"; thus it was open to the Board to reach the conclusion that the transaction was artificial under s 61.

41. The Acting Deputy Commissioner in his Determination had also made the point succinctly when he dealt with the considerations under s 61(1)(f):

> "... In other words, First-Rate which by itself did nothing to earn the income, was allowed to receive 75% of the remuneration from Sun Ling. This arrangement had no commercial justification and obviously was not made on an arm's length basis. If not because the Taxpayer has the control of First-Rate, I doubt whether he would agree to the arrangement. The transaction has thus created rights or obligation which would not normally be created between persons dealing with each other at arm's length."

42. Nothing that Mr Thomson has shown to us persuades us that the Determination or the Board's decision was wrong. Mr Cooney points out that the method by which an assessment was made by the Revenue is quite irrelevant at the stage of proceedings before the Board, and that the crux is whether the assessment is correct. He refers us to *ex pate Herald International Ltd* [1964] HKLR 224 as to how the Board should deal with an appeal against an assessment. Blair-Kerr J in the Full Court said at p 237:

> "The question for the Board of Review is not whether the Commissioner erred in some way, but whether the assessment is excessive. As Mr Sneath so aptly put it: --
>
> 'The question is: "Did the Commissioner 'get the correct answer'; not 'did the Commissioner get the correct answer by the wrong method.'"
>
> And the onus of proving that the assessment is excessive lies on the taxpayer-appellant."

43. Ground 1c fails.

Ground 2a

44. Ground 2a alleges that the Judge erred in determining the "sole or dominant purpose" of the transaction by considering its effect. The relevant part of the Judge's judgment dealing with s 61A reads as follows:

> "Both sections 61 and 61A are anti-avoidance provisions. Their **effect**, however, is different. Under section 61, ... the focus of enquiry is whether a transaction is artificial or fictitious. ... Section 61A, on the other hand, applies where any transaction has, or would have had but for this section the **effect** of conferring a tax benefit on a person (the relevant person) and

> having regard to the seven elements listed therein, it would be concluded that the transaction was entered into or carried out for the sole or dominant purpose of enabling the relevant person to obtain a tax benefit. Here, the question is not whether the transaction is artificial or fictitious. What is called in question is its **effect**, namely, whether it had the sole or dominant purpose of enabling the relevant person to obtain a tax benefit. If it has such an **effect**, the liability to tax of the relevant person may be assessed as if the transaction or any part thereof had not been entered into or carried out or in such manner as the assistant commissioner considers appropriate to counteract the tax benefit which would otherwise be obtained." (emphasis added)

45. Mr Cooney submits that the Taxpayer has misread the judgment. He suggests that the Judge was highlighting the difference between s 61 and s 61A and the reference to "effect" is a reference to the effect of the transaction "namely, whether it had the sole or dominant purpose of enabling the relevant person to obtain a tax benefit." Either Mr Cooney is right or the "effect" means the "effect" of each of the two sections. Or alternatively, the "effect" mentioned the third time in the cited passage refers to "the effect of conferring a tax benefit on" the relevant person as provided for in the body of s 61A(1). Or the word indicates that the Judge was looking at the effect as the intended effect to get at the purpose of the transaction. Anyhow, while the language used by the Judge could be improved to enhance clarity, in the context where the statutory provision of "the sole or dominant purpose" was uttered in the same breath, the contention in this ground would unjustifiably put a different meaning to what the Judge said. Ground 2a has no merit.

Ground 2b

46. Ground 2b alleges that the Judge erred in determining that there was a tax benefit when the definition of tax benefit in s 61A(3) predicates that there must either be (i) some pre-existing liability to tax which is being avoided, or (ii) some pre-existing circumstances which would give rise to, or might be expected to give rise to, a liability to pay tax, when neither of such circumstances were present.

47. The argued "pre-existing" liability to tax or circumstances do not appear in s 61A(3) or anywhere else in the Ordinance having any bearing on the meaning of the "transaction" referred to in that section. We do not think it is necessary to deal with this ground except to say that it has no substance whatsoever.

Ground 2c and 4

48. Ground 2c asserts that the Judge erred in accepting that the Board was correct to draw a reasonable inference that the Assistant Commissioner had regard to the seven factors enumerated in s 61A when forming his view despite (i) the complete absence of evidence before the Board that the Assistant Commissioner had paid regard to the seven factors, or the manner in which he had such regard, and (ii) the transaction which was purportedly under consideration had not been identified. Point (i) is connected with ground 4 which can be conveniently dealt with together.

49. Ground 4 states that the Judge erred in not holding that the assessment under s 61 is predicated upon impugning a transaction as "artificial or fictitious" (and therefore sham) which requires the Commissioner to prove the allegation of sham.

50. First, both the Acting Deputy Commissioner in his Determination and the Board were of the view that the transaction was artificial. They did not say that the transaction was fictitious or sham as now alleged.

51. Secondly, s 68(4) of the Ordinance makes it crystal clear that "the onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant." Judicial utterances to the same effect can also be found in *Herald International Ltd* referred to in para 42 above and *CEC v Comptroller of Income Tax* [1971] SLR Lexis 68, at [*19].

52. As to ground 2c(i), it was for the Taxpayer to prove that the additional assessments were wrong or excessive and not until the Taxpayer had gone some way to establish that (such as a prima facie case) did any necessity arise for the Commissioner to adduce evidence before the Board to show how and how properly the Assistant Commissioner had made such assessments. This contention of the Taxpayer is anyway of no consequence in view of the passage of the judgment in *Herald International Ltd* cited in para 42 above. In any event, the seven factors provided for in s 61A had been dealt with, in our view correctly and satisfactorily, both in the Determination and by the Board.

53. The point made by ground 2c(ii) is that the transaction under consideration had not been identified. This is far from the truth. In the part of the Determination cited in para 41 above, the transaction was described. It was the arrangements (ie, the contracts) ostensibly made between Sun Ling and First-Rate, whereby the remuneration for the efforts and exertions of the Taxpayer as the sales manager of Sun Ling was paid to First-Rate which had done nothing to earn it. The Board also specifically identified the transaction in paragraph 10.1 of the case stated as "(consisting of the 5 contracts between Sun Ling and First-Rate and the interposition of First-Rate between Sun Ling and the Taxpayer)".

54. Both grounds 2c and 4 fail.

Ground 3

55. Ground 3 alleges that the Judge erred in concluding that the Ordinance permits income belonging to one person to be attributed to another person despite there being no such deeming provisions in the Ordinance.

56. This ground relates to the manner in which the assessment is to be made after the transaction has been found to infringe s 61. Mr Thomson presents his argument in two limbs. First, he equates "disregard" in s 61 with the word "annihilate" or "void" used in s 260 of the Income Tax Assessment Act of Australia, and argues that once the transaction, meaning the annual contracts, is annihilated or treated as void, then no remuneration would be due from Sun Ling to First-Rate. Secondly, even if there was remuneration accrued to or received by First-Rate under the transaction, after the

transaction is annulled by s 61 the remuneration still belongs to First-Rate and no income whatsoever has accrued to or been received by the Taxpayer. There is no provision in the Ordinance, so the argument continues, to allow income not accrued to a person to be deemed income of that person to give rise to a tax liability.

57. In his skeleton argument, Mr Thomson also attempts to raise the point that First-Rate had other sources of income, apart from the payments from Sun Ling (see para 7 above), but no additional assessment was raised by the Revenue, which helps show that there was no justification for the Revenue to make the additional assessments against the Taxpayer on Sun Ling's payments. This point was not argued before the Board or the Judge, and no evidence was adduced before the Board to form the factual basis upon which this point could properly be considered. It is subject to the "state of evidence bar" referred to above and we do not think it appropriate for us to consider it now.

58. Mr Cooney suggested in his skeleton argument that the proviso in s 11D(a) of the Ordinance was the relevant deeming provision, but he withdrew that submission at the hearing. We do not think we need express any opinion on whether that section applies to the present circumstances because we are of the view that s 61 itself provides the answer.

59. The relevant word used in s 61 is "disregard" and not "annihilate", "avoid" or "annul". Where a transaction is found by the assessor to contravene s 61, he may "disregard" it and "the person concerned shall be assessable accordingly". The "person concerned", as can be seen in the earlier part of the section, is the person "the amount of tax payable by" whom is reduced or would be reduced by the transaction. We think the meaning of "accordingly" is clear enough, which is the situation where the transaction is disregarded. The Taxpayer in the present case is the person whose tax was reduced by intervention of the contracts and the interposition of First-Rate. When the transaction was disregarded by the assessor pursuant to s 61, the real nature of the remuneration that had been paid by Sun Ling to First-Rate was exposed. The remuneration was paid for the provision of the services that the Taxpayer, and he alone to the exclusion of First-Rate and anyone else, made to Sun Ling, and as such, is assessable as his own income. Indeed, the transaction apart, the real relationship between Sun Ling and the Taxpayer in the circumstances of this case has been well demonstrated to be that between employer and employee. It is unnecessary to deem the remuneration as the Taxpayer's income. It suffices where the transaction has been disregarded to look at the reality of the remuneration and the relationship. Mr Cooney draws our attention to passages in the judgments of the judges in the majority in *Bunting v FCT* (1989) 20 ATR 1579, at 1585 per Beaumont J and at 1590 per Gummow J. The judges were considering what the Revenue was entitled to do where arrangements that offended s 260 of the Income Tax Assessment Act had been annihilated. They held that "the exercise is necessarily a hypothetical one" and the fact was exposed that the income had been earned by the appellant's own exertions and that the Revenue was entitled to "treat the taxpayer as having derived the income which was the return from his own activities." Support can also be found in *Seramco* at p 300 where a similar method was employed by Lord Diplock.

60. Once the transaction in the present case was disregarded by the Revenue, it was open to the Revenue to assess the Taxpayer on the basis as if the remuneration paid by Sun Ling to First-Rate had been received by him as an employee of Sun Ling.

61. This ground also fails.

Conclusion

62. In the result, we dismiss the appeal with an order nisi that the Appellant Taxpayer do pay the costs of this appeal to the Respondent. We also order that the Appellant Taxpayer's own costs be taxed in accordance with the Legal Aid Regulations. We have to say, however, that all members of this Court wonder as to the reason why legal aid was granted in a case like this which is so devoid of merit.

(K H Woo)	(Peter Cheung)	(Wally Yeung)
Justice of Appeal	Justice of Appeal	Justice of Appeal

Representation:

Mr Neil Thomson, instructed by Messrs Massie & Clement, for the Appellant (Taxpayer).

Mr Nicholas Cooney, instructed by the Department of Justice, for the Respondent (the Commissioner).