Case No. D16/19

Profits tax – whether disposition of property is capital nature and not taxable – whether a property is trading stock or a capital asset – financial position of the Company to acquire the subject property for long term investment purposes – whether accounting treatment is a sufficient factor – appeal unsupported by evidence and is frivolous and vexatious

Panel: Albert T da Rosa, Jr. (chairman), Ha Suk Ling Shirley and Lai Sze Wai Alex.

Date of hearing: 26 November 2018.
Date of decision: 18 October 2019.

The Company purchased a non-residential property subject to an existing tenancy. The purchase transaction was completed on 17 May 2010 and by a provisional agreement for sale and purchase dated 12 July 2011, the Company agreed to sell the said property. The Company objected to the Additional Profits Tax Assessment. The Company claimed that the profits it derived from the disposal of a property should not be chargeable to profits tax. The Company appealed on the ground that the Company intended to acquire the property as a long-term investment for rental income and had the ability to carry it into effect. In essence, the Company contended that the gain on its disposition of property was capital nature and not taxable. The Company's case emphasized on two aspects that the property has been held for a long period and it has been let out for rental throughout. The Company further claimed that the subject property was sold for two reasons, one was to relieve the cash flow problem and the other was to eliminate the discomfort among other sons and daughters.

Held:

1. In deciding whether a property is trading stock or a capital asset, it is crucial to ascertain the intention of the taxpayer at the time of acquisition of the property in question. A mere declaration of intention is of limited value. The intention must be genuinely held, realistic and realizable. Subjective intention has to be tested against objective facts and circumstances (Lionel Simmons Properties Ltd (In Liquidation) and others v Commissioners of Inland Revenue (1980) 53 TC 461 and All Best Wishes Ltd, v Commissioner of Inland Revenue 3 HKTC 750 followed).

2. There is insufficient evidence before us to convince us that the financial position of the Company and those controlling it is so strong that the subject property was acquired for long term investment purposes. The position is ambiguous. The accounting treatment is one aspect to be

considered but not a sufficient factor (Real Estate Investments (NT) Ltd v Commissioner of Inland Revenue (2008) 11 HKCFA 433 followed).

3. The Board is not satisfied that there is sufficient evidence on the treatment of the subject property during the time it was held by the company to convince the Board that it was held as capital asset (Real Estate Investments (NT) Ltd v Commissioner of Inland Revenue (2008) 11 HKCFA 433, Marson (Inspector of Taxes) v Morton and related appeals [1986] STC 463, Lee Yee Shing v Commissioner of Inland Revenue [2008] 3 HKLRD 51 and Sir Alan Huggins VP in Chinachem investment Co Ltd v CIR (1987) 2 HKTC 261 followed).

4. On the evidence tendered on the way the subject property was held and used during the time when it was held by the Company, the Board is not convinced that the subject property was held by the company as capital asset but trading stock of the Company and sold for profit.

5. The appeal is notably unsupported by evidence and is frivolous and vexatious. It is unfair that honest and law compliant taxpayers should bear the costs of the Board in this unmeritorious appeal. Pursuant to section 68(9) of IRO, the Board order the Company to pay a sum of $5,000 as costs of the Board and such costs be added to the tax charged and recovered therewith. The costs order has no reflection on the way in which the company's representative presented the case at the hearing but on the fact of the company having proceeded on the appeal on such grounds with such evidence or rather such absence of evidence.

Appeal dismissed and costs order in the amount of $5,000 imposed.

Cases referred to:

Lionel Simmons Properties Ltd (In Liquidation) and Others v Commissioners of Inland Revenue (1980) 53 TC 461
All Best Wishes Ltd. v Commissioner of Inland Revenue 3 HKTC 750
Real Estate Investments (NT) Ltd v Commissioner of Inland Revenue (2008) 11 HKCFA 433
Marson (Inspector of Taxes) v Morton and related appeals [1986] STC 463
Lee Yee Shing v Commissioner of Inland Revenue [2008] 3 HKLRD 51
Sir Alan Huggins VP in Chinachem Investment Co Ltd v CIR (1987) 2 HKTC 261
Commissioner of Inland Revenue v Crown Brilliance Limited [2016] 3 HKC 140

Lui Siu Leung of International Professional Associates, for the Appellant.
Lee Shun Shan, Leung Hoi Sze and Cheng Po Fung, for the Commissioner of Inland Revenue.

Decision:

Introduction

1. Company A (the 'Company') objected to the Additional Profits Tax Assessment raised on it for the year of assessment 2012/13 by the Inland Revenue Department.

2. By the determination (the 'Determination') dated 27 June 2018, the Deputy Commissioner of Inland Revenue (the 'CIR') upheld the relevant Additional Profits Tax Assessment for the year of assessment 2012/13 of $8,724,315 and levied tax thereon in the sum of HK$1,439,512.

3. By a notice of the Company's representative International Professional Associates (the 'Company's Representative') dated 26 July 2018 and received by the Clerk's Office on the same day, the Company lodged an appeal to this Board from that Determination.

4. By a letter dated 16 August 2018, the Company's Representative informed the Clerk that there would be no witnesses arranged to give evidence on the Company's behalf.

5. Directions (the 'Directions')[1] were issued by this Board by the Clerk's letter dated 19 September 2018 which included, *inter alia*, that

5.1. the hearing shall be in English;

5.2. the Company shall file the following by certain dates before the scheduled hearing date –

(a) documents (together with the English translations of such documents if they are written in Chinese or some other languages) which the Company wishes to rely on;

(b) witness statements, if any;

(c) bundle of authorities;

5.3. the Respondent having to do similar filings; and

5.4. there be liberty to apply.

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[1] See section 40 of the Interpretation and General Clauses Ordinance (Chapter 1).

6. This Board regrets to note that notwithstanding the Directions, no English translation for the various pages in Chinese in the Company's hearing bundle has been provided by the Company.

7. The Respondent has supplied the Board with English translations of the Chinese documents in the Respondent's bundle (being the agreement for sale and purchase used in the disposition of the Subject Property by the Company which is in the same standard form as the provisional agreement for sale and purchase used for the acquisition of the Subject Property by the Company.

Agreed Facts

8. By a Statement of Agreed Facts filed with the Board on 9 November 2018 (as a separate bundle for the hearing, the 'SOAF'), the parties agreed to the following:

> '(1) [Company A] has objected to the Additional Profits Tax Assessment for the year of assessment 2012/13 raised on it. The company claims that the profit it derived from the disposal of a property should not be chargeable to Profits Tax.
>
> (2) (a) The Company is a private company incorporated in Hong Kong in March 2009. At all relevant times, the Company's issued and paid-up share capital was $1,000. Its shareholders and directors were [Mr B] and [Ms C].
>
> (b) The Company closed its accounts on 30 April annually. In its financial statements for the years ended 30 April 2011 and 2012, the Company declared that its principal activity was property investment.
>
> (3) (a) By a provisional agreement for sale and purchase dated 24 February 2010, the Company agreed to purchase a non-residential property known as [Property D] ("the Property"), subject to an existing tenancy, at a consideration of $20,200,000.
>
> (b) The formal agreement for sale and purchase in respect of the Property ("the Formal Agreement") was executed on 10 March 2010. The Formal Agreement provided that the Property was sold subject to an existing tenancy. The tenancy agreement dated 11 April 2009 ("the Tenancy Agreement") attached thereto showed that the tenancy was for a term of 5 years commencing on 22 April 2009 at the following monthly rent:

Period	No. of months which were rent-free	Monthly rent
		$
22-04-2009 – 21-04-2010	4	90,000
22-04-2010 – 21-04-2011	3	92,250
22-04-2011 – 21-04-2012	3	92,250
22-04-2012 – 21-04-2014	0	90,000

(c) The purchase transaction in respect of the Property was completed on 17 May 2010. On the same date, the Company obtained the following mortgage loans from [Bank E] ("the Loans"):

Loan principal	Term of repayment	Monthly repayment
$	Month	$
10,100,000	180	66,810.86
3,900,000	180	25,798.25
14,000,000		92,609.11

(d) By a provisional agreement for sale and purchase dated 12 July 2011, the Company agreed to sell the Property, subject to the existing tenancy, at a consideration of $30,380,000. The formal agreement for sale and purchase was executed on 26 July 2011. The sale transaction was completed on 18 October 2011.

(4) The Company filed its Profits Tax Returns for the years of assessment 2011/12 and 2012/13 together with the audited financial statements and tax computations.

(a) In its tax returns, the Company declared the following assessable profits:

	2011/12	2012/13
	$	$
Assessable profits	105,437	219,565

(b) The above assessable profits were arrived at after making the following adjustments:

	2011/12	2012/13
Deduction:	$	$
- Commercial building allowance ("CBA")	252,000	-
- Gain on disposal of the Property	-	9,863,838

	2011/12	2012/13
Addition:		
- Balancing charge		252,000
- Commission for selling the Property	-	303,800
- Legal and professional fee for selling the Property	-	13,830

(c) The gain on disposal of the Property was computed as follows:

	$	$
Sale proceeds [Fact (3)(d)]		30,380,000
Less: Cost	21,086,055	
Accumulated depreciation	(569,893)	20,516,162
Gain on disposal		9,863,838

(d) The Company's balance sheets showed the following particulars:

As at	30-04-2011 $	30-04-2012 $
Non-current assets -		
Property, plant and equipment	20,516,162	-
Current assets -		
Due from [Mr B]	-	9,286,641
Other current assets	159,131	101,051
	159,131	9,387,692
Less: Current liabilities -		
Bank loan due within 12 months - secured	13,284,973	-
Due to director	7,419,163	-
Other current liabilities	187,997	116,825
	20,892,133	116,825
Net current assets/(liabilities)	(20,733,002)	9,207,867
Net assets/(liabilities)	(216,841)	9,270,867
Equity -	1,000	1,000
Issued share capital	(217,841)	9,269,867
Retained earnings	(216,841)	9,270,867

(5) The Assessor raised on the Company the Profits Tax Assessments for the years of assessment 2011/12 and 2012/13 based on the returned profits. The Company did not object to the assessments.

(6) In the absence of a reply to the Assessor's enquiries concerning the sale and purchase of the Property, the Assessor did not accept that

the gain on disposal of the Property was not chargeable to Profits Tax. The Assessor raised on the Company the following Additional Profits Tax Assessment for the year of assessment 2012/13:

	$
Additional Assessable Profits (i.e. Gain on disposal of the Property [Fact (4)(c)])	9,863,838
Additional Tax Payable thereon	1,627,533

(7) The Company objected to the Additional Profits Tax Assessment in Fact (6) above on the grounds that the assessable profits were excessive and the gain on disposal of the Property was capital in nature, which was not subject to Profits Tax.

(8) Well Gain Accounting & Management Consultants ("the Representatives") claimed the following:

(a) The Company intended to acquire the Property as a long-term investment for rental income.

(b) The Property was built in 1982 and its gross floor area was 9,000 square feet.

(c) In January 2010, [Ms C] sought help from a realty agent, [Ms F] ("the Agent"), to provide advice on the viability of the long-term investment in rental properties in Hong Kong. The Agent accompanied the Company's directors for site visits to several properties and provided them with the information on investment opportunities, rate of return on capital and servicing of loan. Having considered the professional advice and information provided by the Agent, the Company's directors decided to purchase the Property with the existing tenancy, which was a suitable long-term investment.

(d) The acquisition of the Property was financed by the Loans and another loan from the directors of $6,200,000. The monthly rental income of $92,250 derived from the Property was sufficient to cover the monthly repayment of the Loans.

(e) In May 2011, [Mr B]'s sole proprietorship business, [Company G], experienced a cash flow problem. It struggled to ensure that it could maintain its normal operations. Under such critical circumstances, [Mr B] decided to call his loan advanced to the Company and the Company was forced to sell the Property to repay the director's loan. In June 2011, [Ms

C] approached the realty agent, [Ms H], for market information on industrial properties.

(f) It was well settled that one transaction of buying and selling did not make a man a trader. The Company had one property dealing since its incorporation.

(9) By letters dated 11 July 2016 and 27 October 2017, the Assessor requested the Representatives to provide, among others, information showing: the director's source of fund for making a loan to the Company on a long-term basis; and the financial position of [Company G]. Despite the issue of a reminder, neither the Company nor the Representatives responded to the Assessor's letters.

(10) (a) In the absence of a reply to the letters, the Assessor raised on the Company the following Additional Profits Tax Assessment for the year of assessment 2011/2012 to withdraw the CBA previously granted:

	$
Additional Assessable Profits (i.e. CBA [Fact (4)(b)])	252,000
Additional Tax Payable thereon	41,580

(b) The Company did not object to the above additional assessment.

(11) On appeal to the Board of Review against the Deputy Commissioner's determination, the Company through International Professional Associates advised that apart from the Company, [Mr B] and [Ms C] were also the directors and shareholders of [Company J] and [Company K].

(12) [Company J] and [Company K] are private companies incorporated in Hong Kong on 15 October 2004 and 3 November 2006 respectively. Both companies described their principal activity as property investment for rentals in their directors' reports for the year ended 30 April 2011 and 2012.'

9. The parties agreed that the appendices mentioned in the statement of agreed facts are the same as the appendices to the Determination. In this decision, this Board has added in square brackets, after each reference to an appendix to the statement of agreed fact in paragraphs 8 herein, the respective cross-reference pagination number(s) of the Board Bundle for such appendix.

Additional Findings

10. From the documents presented at the hearing this Board also notes and finds:

10.1. On 21 April 2011, Ms C signed an agreement to purchase the property known as Property L at $5,594,000.

10.2. As at 30 April 2011, the total cash and bank balance of the Company and its two related companies, Company J and Company K was $1,689,825[2].

	Entity		Amount
(a)	The Company	:	$151,371
(b)	Company J	:	$1,055,670
(c)	Company K	:	$482,784

Basis Of Appeal

11. The Company's grounds of appeal as filed by the Company's Representative are as follows:

'Our grounds of appeal are:

(i) Section 14 of the Inland Revenue Ordinance exempts gains arising from the sale of capital assets, and also the capital income should not be included in taxable profits.

(ii) In early 2009, [Mr B] and his wife, [Ms C], planned to own one more investment property, via a limited company, as part of their overall wealth portfolio. Their primary goal was to build a larger portfolio of properties for long term rental income, and for passing the assets onto future generations.

With this strategy, [Mr B] and his wife, [Ms C] incorporated [Company A] on 11 March 2009.

In early 2010, [Ms F], a knowledgeable buy-to-let investment properties agent, introduced a non-residential property known as [Property D] ("the property"), it came with an existing tenant, and a

[2] All three companies closed their accounts on 30 April each year and thus the year of assessment 2012/13 covered the period from 1 May 2011 to 30 April 2012.

long-term lease with more than four remaining years. [Company A] bought this property with a clear intention of buy-to-let property investing.

(iii) A binding agreement for purchasing the property was signed on 24 February 2010, and the completion date of disposal of the property was on 18 October 2011 (investment period was about 20 months).

The principal activity of [Company A] was property investment for rentals, [Company A] did not hire any employee to carry out other activities from the date of incorporation till now, and the gains of capital nature are credited to capital reserves and hence not taxable.

(iv) In 2011, [Company G] (File No. XXX-XXXXXXXX), the sole-proprietorship business of [Mr B] encountered a cash flow problem and needed funds to maintain its normal operations. [Mr B] decided to call back his loan advanced to [Company A] which rendered the selling of the property to repay the loan.

(v)[3] [Mr B] and his wife, [Ms C] have a long history of managing their investment property portfolio through limited companies. In the year of assessment 2012/13, [Mr B] and his wife, [Ms C] own more than ten investment properties, via three limited companies, namely:

[Company J] incorporated on 15 OCT 2004 (File No. XX/XXXXXXXX);

[Company K] incorporated on 3 November 2006 (File No. XX/XXXXXXXX); and

[Company A] incorporated on 11 March 2009 (File No. XX/XXXXXXXX).

The principal activities of all the limited companies were property investment for rentals. Each limited company has two directors, namely [Mr B] and his wife, [Ms C]. They are also the only registered shareholders.

Since 2006, [Mr B] (File No. XXX-XXXXXXXX) received director's fee of HK$280,000 annually from [Company J], and his wife, [Ms C] (File No. XXX-XXXXXXXX) received director's fee of HK$280,000 annually from [Company K].

Both [Mr B], [Ms C] and all their jointly owned limited companies

[3] Wrongly numbered as (iv) in the original grounds of appeal as filed.

have no prior history of property dealings.

Furthermore, [Mr B], [Ms C] and all their jointly owned limited companies have never been taxed for any profits they made in their property deals.

In view of the above objective facts and surrounding circumstances, it is clear that the taxpayer was genuinely intended to hold the property for long-term investment, and had the ability to carry it into effect. The gain from disposal of the Property should not be liable to Profits Tax, and we do not accept the written determination saying that the taxpayer acquired the Property for trading purpose.'

12. Section 14(1) of the Inland Revenue Ordinance ('IRO') provides that:

'*Subject to the provisions of this Ordinance, profits tax shall be charged for each year of assessment on every person carrying on a trade, profession or business in Hong Kong in respect of his assessable profits arising in or derived from Hong Kong for that year from such trade, profession or business (excluding profits arising from the sale of capital assets) as ascertained in accordance with this Part.*'

13. In essence, the Company contends that the gain on its disposition of Property D (the 'Subject Property') is capital nature and not taxable.

14. It can be deduced from the grounds of appeal as filed and from the oral submission by the Company's Representative at the hearing that the Company seeks to justify its position that the Subject Property was disposed of as capital asset on the basis that:

14.1. it was acquired as capital assets;

14.2. it has been treated as capital assets in its accounts;

14.3. it has been held for a long time for rental purposes; and

14.4. it is disposed of because of the cash flow needs of the Company and associated companies controlled by the common shareholders.

Intention At The Time Of Acquisition

15. In deciding whether a property is a trading stock or a capital asset, it is crucial to ascertain the intention of the taxpayer at the time of acquisition of the property in question. In Lionel Simmons Properties Ltd (In Liquidation) and Others v Commissioners of Inland Revenue (1980) 53 TC 461, Lord Wilberforce stated the following at pages 491G to 492A:

> '*Trading requires an intention to trade: normally the question to be asked is whether this intention existed at the time of the acquisition of the asset. Was it acquired with the intention of disposing of it at a profit, or was it acquired as a permanent investment? Often it is necessary to ask further questions: a permanent investment may be sold in order to acquire another investment thought to be more satisfactory; that does not involve an operation of trade, whether the first investment is sold at a profit or at a loss. Intentions may be changed. What was first an investment may be put into the trading stock — and, I suppose, vice versa … What I think is not possible is for an asset to be both trading stock and permanent investment at the same time, nor to possess an indeterminate status — neither trading stock nor permanent asset.*'

16. A mere declaration of intention is of limited value. The intention must be genuinely held, realistic and realizable. In All Best Wishes Ltd v Commissioner of Inland Revenue 3 HKTC 750, Mortimer, J (as he then was) said the following at page 771:

> '*The intention of the taxpayer, at the time of acquisition, and at the time when he is holding the asset is undoubtedly of very great weight. And if the intention is on the evidence,* ***genuinely held, realistic and realisable****, and if all the circumstances show that at the time of the acquisition of the asset, the taxpayer was investing in it, then I agree. But as it is a question of fact, no single test can produce the answer. In particular, the stated intention of the taxpayer cannot be decisive and the actual intention can only be determined upon the whole of the evidence. Indeed, decisions upon a person's intention are commonplace in the law. It is probably the most litigated issue of all. It is trite to say that intention can only be judged by considering the whole of the surrounding circumstances, including things said and things done. Things said at the time, before and after, and things done at the time, before and after. Often it is rightly said that actions speak louder than words.*'

17. Subjective intention has to be tested against objective facts and circumstances.

18. As the Respondent put it in the following paragraphs of the Determination:

> '3(2)(b) "Intention" connotes an ability to carry it into effect. It is idle to speak of "intention" if the person so intending did not have the means to bring it about or had made no arrangement or taken no steps to enable such intention to be implemented.'
>
> '3(3)(b) At all relevant times, the Company's paid-up share capital was $1,000. The purchase of the Property was financed by the Loans and a loan from Mr B. According to the Tenancy Agreement [Fact (3)(b)], the monthly rental income during 22

> April 2010 to 21 April 2012 was $92,250. It provided for a 3-month rent free period each year. The annual rental income from letting the Property during the period when the Property was held by the Company was $830,250 ($92,250 x 9), which was insufficient to meet the annual repayment of the Loans of $1,111,308 (i.e. $92,609 [Fact (3)(c) x 12 months]. There was no information to show how the Company could meet the shortfall and the repayment of Mr B's loan. Furthermore, despite the Assessor's requests, the Company failed to provide any information to show that Mr B had the financial ability to advance a loan to the Company on a long-term basis. On the other hand, the loan from Mr B was classified as current liability in the Company's balance sheet as at 30 April 2011 [Fact (4)(d)]. These cast serious doubt on the Company's financial ability to hold the Property on a long-term basis.'

19. By a letter dated 19 October 2018, the Respondent asked for evidence of such ability by the Company's own resources or the alleged ability of its related companies Company G and Company J as well as the banking records of Mr B and his wife Ms C (collectively the 'Couple'). However, the bulk of the information was not provided to the Respondent.

20. When asked by the Board as to the reason for not providing the information, the following exchange took place:

> MISS HA: How do you explain why the taxpayer refused to respond to Revenue's letters despite repeated reminders in those two years?
>
> MR LUI: As you might notice, the appellant has changed the tax representative. In the very beginning, the tax rep. is Well Gain Accounting & Management Consultants. To my understanding, Well Gain Accounting & Management Consultants might have some misunderstanding between the appellant and themselves in regard to the service fee. The appellant thinks that replying the lengthy tax query from the Revenue should be part of the work of the tax reporting already included in the fee that they have paid for it and reluctant to pay further service fee to Well Gain Accounting & Management Consultants, yeah. That was the issue between them. So, the case had been dragged on for a long time and I notice that. We are appointed by the appellant recently around June or July this year for presenting the case in front of the Board of Review. So, we contacted the appellant Mr and Mrs B and gathered the information once again so that- it is slightly different between our reply to the Revenue and the former tax representing. They are more or less the same but

it added some points after we found it out.

21. A historical explanation was given. There is still no direct answer supplying the requested information and the bank statements are still outstanding.

22. There is insufficient evidence before us to convince us that the financial position of the Company and those controlling it is so strong that the Subject Property was acquired for long term investment purposes. The position is ambiguous.

Accounting Treatment

23. The Company claimed that the gain on disposal of the Subject Property was credited to the Company's capital reserve account and thus should not be taxable.

24. However, as shown in the Company's detailed income statement for the year ended 30 April 2012, the gain on disposal of the Subject Property was grouped under other income to compute the Company's profit for that year. There is no information showing that the gain was directly credited to the capital reserve account.

25. In any event, in Real Estate Investments (NT) Ltd v Commissioner of Inland Revenue (2008) 11 HKCFA 433, it was held that an appellant's own accounting treatment is only one of the factors to be taken into account and must be looked at together with other evidence:

> '*33. As noted above, the Property has been described in the Taxpayer's accounts from 1980 to 1995 as a fixed asset. It is argued on the Taxpayer's behalf as follows. Such accounting treatment gave rise to a prima facie case that the profits in question arose from the sale of a capital asset. Consequently, the onus of proof shifted so that the Revenue had to show by evidence that the assessments were correct.*'
>
> '*34. That argument is misconceived. Consistency between a taxpayer's audited accounts and its stance does not go so far as to set up a prima facie case of that stance's correctness in law. Where a taxpayer's audited accounts are consistent with its stance, such consistency is some evidence in support of that stance. Even where accounting treatment amounts to strong evidence, it still falls to be considered together with the rest of the evidence adduced in the case.*'

26. Thus, the accounting treatment is one aspect to be considered but not a sufficient factor.

Holding And Usage Before Disposal

27. We are conscious of the guidance offered by the approach to the concept of 'badges of trade' in Marson (Inspector of Taxes) v Morton and related appeals [1986] STC 463 at pages 470e to 471g and Lee Yee Shing v Commissioner of Inland Revenue [2008] 3 HKLRD 51 38 (especially what Bokhary and Chan PJJ said at paragraphs 38 and McHugh NPJ said at paragraphs 56, 59 to 61 at pages 72 and 73.

28. At the end of the day, it is a holistic assessment. In the Court of Final Appeal decision in Real Estate Investments (NT) Ltd v Commissioner of Inland Revenue (2008) 11 HKCFAR 433, Bokhary and Chan PJJ said at paragraphs 53 and 55, page 452:

> '53. *... the list offered in Marson v Morton is no less helpful in Hong Kong than it is in the United Kingdom. As the Privy Council observed in Beautiland Co Ltd v CIR [1991] 2 HKLR 511 at p.515G, there is no material difference between the Hong Kong and United Kingdom definitions of trade for tax purposes. Both include every adventure in the nature of trade.*'
>
> '*55. The question of whether property is trading stock or a capital asset is always to be answered upon a holistic consideration of the circumstances of each particular case.*'

29. The Company's case places emphasis on two aspects:

29.1. that the Subject Property has been held for a long period; and

29.2. that it has been let out for rental throughout.

Short Period of Holding

30. The Company held the Subject Property for only about 15 months:

	Purchase	Sale	Holding period
Date of provisional agreement	24 February 2010	12 July 2011	14 months & 19 days
Date of assignment	17 May 2010	18 October 2011	15 months & 2 days

31. The Company sought to take the period from the date of the provisional agreement on acquisition to the date of the assignment on disposal for calculation of the period of holding; but even then, it is still only a period of 19 months and 23 days. Such period is not even significantly long.

Letting out

32. It is true that the Subject Property was let out throughout the Company's ownership. Yet, the use of the Subject Property to produce rental income is, however, not decisive and is only one of the objective facts in considering the badges of trade to test the Company's intention[4].

33. In Real Estate Investments (NT) Ltd v Commissioner of Inland Revenue (2008) 11 HKCFAR 433, Bokhary and Chan PJJ held that the facts that the property was producing rent before disposal and a long holding period shed little, if any light on whether the property concerned was trading stock or capital asset and quoted the following judgment made by Sir Alan Huggins VP in Chinachem Investment Co Ltd v CIR (1987) 2 HKTC 261 (at page 311)

> '*... [the taxpayer] may have been waiting for a favourable opportunity to sell and merely have been turning the properties to good account in the meantime. Equally, the fact that the properties were let at full economic rents is consistent with the case of both sides, although if the lettings had been at rents below the economic rents that would clearly have supported [the Revenue's] contention…. These facts may indicate nothing more than that the 'favourable opportunity to sell' had not arrived…*'

Finding

34. We are not satisfied that there is sufficient evidence before us on the treatment of the Subject Property during the time it was held by the Company to convince us that it was held as capital asset.

Reason(s) For Disposal

35. By a letter dated 7 November 2018, the Company claimed that the Subject Property was sold for two reasons, one was to relieve the cash flow problem of Company G and the other was to eliminate the discomfort among the Couple's other sons and daughters because the Couple incorporated the Company and used part of the names of their elder son and their elder son's wife as the Company's name and then made property investment through the Company.

Cash Flow Problem

36. In respect of the cash flow problem, the Company claimed that Company G encountered cash flow problems in the beginning of 2011 and it needed $3 million to relieve its cash flow problem.

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[4] See paragraph 27 herein.

37. Despite the Company's claim that Company G experienced cash flow problem in the beginning of 2011 and it needed $3 million to relieve the cash flow problem, the objective fact shows that Ms C signed an agreement to purchase Property L at a consideration of around $5.59 million on 21 April 2011. This clearly contradicts the Company's claim.

38. The Company claimed that Company G experienced cash flow problem. Yet no document has been provided to support that Company G did experience cash flow problem and that it needed $3 million to relieve the problem. Besides, no explanation was given why Company G suffered from cash flow problem.

39. The Company tried to show the cash flow problem by comparing the financial data of Company G for the year ended 31 December 2011 with those for the year ended 31 December 2012. However, the analysis only shows the sign (if any) of cash flow problem that might be encountered by Company G in the year 2012, not at the beginning of the year 2011 and well after the disposal of the Property in July 2011. The statement of loss of Company G for the year of assessment 2012/13 also could not assist the Company's claim because it only showed that Company G was in a loss position in the year 2012. In contrast, the profit and loss account for the year 2011 showed that Company G made net profits of $301,675. All in all, these documents could not support the Company's contention.

40. No full picture has been provided to show the overall financial position of the Couple. The Couple are the common directors and shareholders of the Company, Company J and Company K. As submitted by the Respondent and we find as follows:

40.1. The total cash and bank balance of the Company, Company J and Company K as at 30 April 2011 was $1,689,825[5], which is more than 50% of cash required by Company G to meet its cash flow problem[6].

40.2. The total cost of properties and the bank mortgage loans of Company J and Company K as at 30 April 2011 were $35,308,762 and $11,359,130 respectively.

40.3. The ratio of loan to the cost of properties was around 32.18%.

40.4. It would not be difficult for the Couple to apply for further mortgage loan of around $1.4 million (i.e. $3 million - $1.6 million) from the bank by re-mortgaging the properties of Company J and Company K.

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[5] Our finding in paragraph 10.2 herein.

[6] Transcript page 28 line 11 Mr Lui '... [Company G] needed only 3 million.'

40.5. As disclosed by the Company, the Couple held the total cost of properties of $3,550,000 in the year 2011.

40.6. All these suggest that the selling of the Property is not the only way to solve the cash flow problem of Company G.

41. No document has been provided to show that the sale proceeds of the Property were actually used to solve Company G's cash flow problem.

To Eliminate the Discomfort Among other Sons and Daughters

42. At the hearing, the Company sought to introduce a new factor namely that the selling of the Subject Property held by the Company had served additional purpose

> ' ... to eliminate the unspoken discomfort among their sons and daughters, as the other three sons and daughters had noticed that [Mr & Mrs B] incorporated a limited company with the names of [Mr M] and [Ms N], and made a property investment through [Company A].'

43. This additional factor was not mentioned in the notice of appeal but only in the subsequent letter of 7 November 2018.

44. In so far as this additional factor is to serve as an additional ground of appeal, it is not allowed because section 66(3) of the Ordinance which reads:

> '*(3) Save with the consent of the Board and on such terms as the Board may determine, an appellant may not at the hearing of his appeal rely on any grounds of appeal other than the grounds contained in his statement of grounds of appeal given in accordance with subsection (1).*'.

45. No application has been made by the Company to this Board for such consent nor was any explanation given for such late introduction.

46. In so far as the new factor is intended to be background information in support of the main ground, then it faces two difficulties:

46.1. Mr and Mrs B were not called to give evidence of their intention and we do not accept the hearsay evidence of the Company's Representative by mere assertion before us; and

46.2. as submitted by the Respondent, since the claimed discomfort among other sons and daughters is due to the name of the Company, this can be easily solved by changing the name of the Company rather than by selling the Subject Property.

47. On the evidence tendered on the way the Subject Property was held and used during the time when it was held by the Company, we are not convinced that the Subject Property was held by the Company as capital asset.

Procedure For Board Hearing

48. Section 68(4) of the IRO provides that –

> '*The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.*'

49. The Company called no evidence.

50. In Commissioner of Inland Revenue v Crown Brilliance Limited [2016] 3 HKC 140, the Court considered the question in the absence of the oral evidence given by the taxpayer during the Board's hearing, whether the Board could rely on the taxpayer's representatives' assertions or representations which were not supported by evidence. The Court held at paragraph 19 of page 149 as follows

> '*In the present context, I accept the submission of Mr Leung, who appeared for the Commissioner on this appeal,* ***that a fact is not proved by its assertion in argument.*** *It is proved by evidence, oral or documentary.* ***The representations and oral submissions made by the tax representative, without more, do not amount to evidence****. This has been the practice of the Board itself: see Board of Review Decisions Nos. D7/08 at §64, D35/10 at §§12-13, D18/13 at §50 and D28/12 at §§16-17. Mr Leung accepted that the contemporaneous documents submitted by the tax representative, at any rate those documents whose authenticity is not in dispute, may be considered by the Board as admissible documentary evidence. But the assertions and submissions that are not supported by the undisputed contemporaneous documents stand on a different footing and ought not, without more, to be treated as evidence.*'

51. We regret to note that the Company's Representative who presented the case on behalf of the Company before this Board did not appear to be conversant with some of the very basic procedures for such hearing and required reminders on, *inter alia*,

51.1. the order of speech;

51.2. the difference between draft statement of agreed facts and the version ultimately agreed;

51.3. the difference between evidence and submission; and

51.4. the onus of proof.

52. However, we also appreciate that he was always courteous and he quickly understood the position when explained to him and proceeded accordingly.

53. We wish to remind those professionals who appear for clients before us to take time and effort to prepare themselves to be competent before taking on such role.

Disposition

54. On a holistic consideration of all the evidence before us, we are of the view that the Subject Property is not capital assets but trading stock of the Company and sold for profit.

55. We dismiss the appeal and confirm the assessment in the Determination.

Costs Order

56. The appeal is notably unsupported by evidence and is frivolous and vexatious. It is unfair that honest and law compliant taxpayers should bear the costs of the Board in this unmeritorious appeal.

57. Pursuant to section 68(9) of IRO, we order the Company to pay a sum of $5,000 as costs of the Board and such cost be added to the tax charged and recovered therewith.

58. We wish to clarify, however, that the cost order has no reflection on the way in which the Company's Representative presented the case at the hearing but on the fact of the Company having proceeded on the appeal on such grounds with such evidence or rather such absence of evidence.