Case No. D2/14

Profits tax – capital or trading/business – sections 2, 14, 66(3), 68(4), 68(7) and 68(9) of the Inland Revenue Ordinance (Chapter 112).

Panel: Kenneth Kwok Hing Wai SC (chairman), Cheng Chung Hon Nevillie and Ha Suk Ling Shirley.

Date of hearing: 20 January 2014.
Date of decision: 9 April 2014.

The Appellant, a company incorporated in Hong Kong, acquired a shop situated at a 48-year old building ('the Shop') with a sitting tenancy at the price of $31,480,000. The sitting tenancy provided for a monthly rental of $55,000 during the first year after acquisition and $60,000 during the second year.

The acquisition of the Shop was funded entirely by borrowed fund. Of the acquisition price, $22,000,000 was funded by a term loan of which the interest rate was 1% above 1-month HIBOR rates, while the balance of $9,480,000 was funded by the shareholder.

In less than a year, the Appellant sold the Shop at a gain. However, it contended that its original intention was to acquire the Shop as a long term investment for rental income purpose and the profits derived from the sale of the Shop were capital in nature and not subject to profits tax.

Held:

1. The *gross* annual rate of return (i.e. *before* the deduction of any fees or expenses) at the rental income of $55,000 and $60,000 was 2.1% and 2.29% respectively, which would take 47.62 years and 43.67 years respectively to recoup the acquisition price of the Shop even assuming full occupancy of the Shop during the whole period.

2. Further, the annual rate of return would be reduced by the following factors:

   (1) Given the Building was a 48-old building completed in 1962, looking at the matter objectively, the building would be affected by further wear and tear as time goes by and maintenance costs would come in.

(2) The minimum interest rate was 1% with monthly rests. The HIBOR interest rates could fluctuate over the decades ahead.

(3) There was no basis for assuming full occupancy of the Shop or that the current tenant will remain the tenant for decades.

3. The Board was not persuaded that the shareholder would spend $9,480,000 on an investment with nil return for decades.

4. The provisional acquisition agreement provided for completion in 4 months. 4 months was a bit longer than normal completion periods. Speculators tend to favour long completion periods to give themselves more time for sub-sale before completion so as to reduce the costs of stock. The Appellant offered no explanation for the 4 months completion period.

5. Monthly repayment of principal under the Term Loan was $30,000 for the first 18 months and $132,500 thereafter. The Appellant was asked whether the Term Loan repayments were structured in this away so as to reduce the costs of stock during the initial 18 months for it to try to sub-sell. The Appellant failed to give any innocuous explanation, and gave no direct response in fact.

6. The sale by the Appellant to the Purchaser was documented in such a way as to hide a substantial part of the sale price from the documents submitted for registration at the Land Registry under the Land Registration Ordinance, Chapter 128. The Appellant offered no explanation for their less than candid approach in drawing up conveyancing documents designed for public access and reference.

7. Having further considered the 'badges of trade', upon a holistic consideration of the circumstances, the Board concluded that the Appellant was 'doing a deal'.

Appeal dismissed.

Cases referred to:

Kim Eng Securities (Hong Kong) Ltd v CIR (2007) 10 HKCFAR 213
Wing Tai Development Co Ltd v CIR [1979] HKLR 642
Real Estate Investments (NT) Limited v Commissioner of Inland Revenue (2008) 11 HKCFAR 433
Shui On Credit Company Limited v Commissioner of Inland Revenue (2009) 12 HKCFAR 392
Simmons v IRC [1980] 1 WLR 1196

Marson v Morton [1986] WLR 1343
All Best Wishes Limited v CIR (1992) 3 HKTC 750
Lee Yee Shing v The Commissioner of Inland Revenue (2008) 11 HKCFAR 6 [1913] HKLR 52
Kwok Siu Lau v Kan Yang Che

Roy Lau, Counsel instructed by Wise-Link CPA Limited for the Appellant.
Jonathan Chang, Counsel instructed by Department of Justice for the Commissioner of Inland Revenue.

Decision:

Introduction

1. The Appellant bought and sold the Shop at a gain. The issue is whether the gain is chargeable to profits tax. Particulars of the acquisition and sale of the Shop are as follows:

1962	The Building where the Shop formed part completed
5 June 2009	Date of tenancy agreement leased to Tenant for 3 years at a monthly rental of: (a) $55,000 for 1 May 2009 to 30 April 2011; and (b) $60,000 for 1 May 2011 to 30 April 2012
13 May 2010	Date of provisional acquisition agreement, at the acquisition price of $31,480,000, with a deposit of $1,000,000 paid on signing of provisional acquisition agreement, for completion by 13 September 2010
28 May 2010	Date of formal acquisition agreement, with a further deposit of $2,148,000 paid on signing of formal acquisition agreement
26 August 2010	Date of Bank facility letter for a term loan of $22,000,000 repayable 180 months after date of drawdown: (a) For the first 18 months, monthly repayment of principal of $30,000, plus monthly interest at 1% per annum over

	HIBOR based on an interest period of 1 month; and (b) For the 19th month and thereafter, monthly repayment of principal of $132,500, plus monthly interest at 1% per annum over HIBOR based on an interest period of 1 month
13 September 2010	Date of acquisition assignment with balance of purchase price of $28,332,000 paid
30 September 2010	In the audited financial statements for the year ended 30 September 2010, the auditors[1] noted that: '*Fundamental Uncertainty* "As described in note 1 to the financial statements, there has been concern as to the availability of adequate short term future funding to the company and consequently as to the appropriateness of the going concern basis as the company's current liabilities exceeded its current assets by HK$11,907,764 at the balance sheet date. In forming our opinion regarding such inherent uncertainty, we have considered the adequacy of disclosures in connection therewith, our discussion with the directors and other information of which we have become aware during our audit. Our opinion is not qualified in this respect." '
3 November 2010	Alleged Associated Company of the Agent, the Appellant's property agent, became a tenant of part of the Building
14 February 2011	Date of application to Lands Tribunal under Land (Compulsory Sale for Redevelopment) Ordinance, Chapter 545
3 March 2011	Date of provisional sale agreement at the *alleged* price of $40,000,000
3 March 2011	Date of supplemental agreement by which

[1] Wise-Link CPA Limited.

	Purchaser agreed to pay a further sum of $59,980,000 as part of the purchase consideration, with the Appellant undertaking to keep the supplemental agreement in the strictest confidence and not to submit the supplemental agreement to the Land Registry for registration
8 April 2011	Date of sale assignment, at the *alleged* consideration of $40,000,000 according to the documents presented to the Land Registry for registration

2. By a Determination dated 28 May 2013 the Deputy Commissioner of Inland Revenue confirmed the profits tax assessment dated 31 July 2012 showing net assessable profits of $65,304,809 (after set-off of loss brought forward of $361,760) with tax payable thereon of $10,763,293 (after tax reduction).

Agreed facts

3. The Appellant has agreed the following facts as stated in paragraph 1(1) to (16), inclusive, of the Determination and we find them as facts, see paragraphs 4 to 20 below.

4. The Appellant has objected to the Profits Tax Assessment for the year of assessment 2011/12 raised on it. The Appellant claims that the gain on disposal of a property was capital in nature and should not be chargeable to Profits Tax.

5. (a) The Appellant is a private company incorporated in Hong Kong in April 2004.

(b) The Appellant's issued and fully paid up share capital increased to $100 divided into 100 ordinary shares of $1 each on 31 January 2011.

(c) At all relevant times, the Shareholder was the Appellant's sole shareholder and director. During the period ended 30 September 2005, the Assistant was also the Appellant's director.

(d) The Appellant closed its financial statements annually on 30 September.

6. In its profits tax returns for the years of assessment 2005/06 to 2006/07, the Appellant described its principal business activity as 'property dealing'.

7. (a) By a sale and purchase agreement dated 13 August 2004, the Appellant purchased the Kowloon Property at $3,190,000. The Kowloon Property was assigned to the Appellant on 31 December 2004.

(b) By a sale and purchase agreement dated 10 April 2006, the Appellant sold the Kowloon Property at $3,080,000. The property was assigned to the buyer on 30 June 2006.

8. The Appellant filed its profits tax returns for the years of assessment 2005/06 to 2006/07 together with its audited financial statements, detailed profit and loss accounts and tax computations.

(a) In the returns, the Appellant declared the following adjusted loss:

Year of Assessment	2005/06	2006/07
	$	$
Adjusted Loss	(35,648)	(239,248)

(b) The Appellant's detailed profit and loss accounts showed the following particulars:

Year ended	30-09-05	30-09-06
	$	$
Revenue		
Loss on property dealing	-	(196,147)
Less:		
Accountancy fee	5,200	5,700
Audit fee	4,500	9,000
Bank charges	150	-
Building management fee	8,776	9,873
Business registration fee	2,600	5,200
Government rent and rates	3,888	6,016
Office administration fee	9,800	6,300
Preliminary expenses	2,600	-
Sundry expenses	734	1,012
	38,248	43,101
Loss before tax	(38,248)	(239,248)

Note: There was no break-down on the loss on property dealing.

9. In its profits tax returns for the years of assessment 2007/08 to 2009/10, the Appellant claimed that it was dormant.

(a) In the returns, the Appellant declared the following adjusted loss:

Year of Assessment	2007/08	2008/09	2009/10

	$	$	$
Adjusted Loss	Nil	(555)	(6,855)

(b) The Appellant's detailed profit and loss accounts showed the following particulars:

Year ended	30-09-07	30-09-08	30-09-09
	$	$	$
Revenue	-	-	-
Less:			
Accountancy fee	-	-	1,000
Audit fee	-	-	3,000
Bank charges	-	-	-
Business registration fee	2,600	450	2,450
Sundry expenses	105	105	405
	2,705	555	6,855
Loss before tax	(2,705)	(555)	(6,855)

10. In its profits tax returns for the years of assessment 2010/11 to 2011/12, the Appellant described its principal business activity as 'property investment'.

11. (a) By a provisional sale and purchase agreement dated 13 May 2010, the Appellant purchased the Shop at $31,480,000. The property was part of the Land [and] the Building. The Agent was the property agent in the transaction. An agreement for sale and purchase was entered into on 28 May 2010 and the Shop was assigned to the Appellant on 13 September 2010.

(b) The Shop was purchased with a sitting tenancy as follows:

Date of tenancy agreement:	5 June 2009
Name of tenant:	The Tenant
Rent and term:	(i) $55,000 per month for 1 May 2009 to 30 April 2011
	(ii) $60,000 per month for 1 May 2011 to 30 April 2012

(c) The Appellant partially financed the acquisition of the Shop by a term loan of $22,000,000 ('the Term Loan') from the Bank repayable by 180 monthly instalments. For the first 18 months, the monthly principal repayable to the Bank was $30,000. For the 19th month and thereafter,

the monthly principal repayable to the Bank increased to $132,500. The Term Loan was secured by a first legal charge over the property and an irrevocable and unconditional personal guarantee of the Shareholder.

(d) By a provisional agreement for sale and purchase dated 3 March 2011, the Appellant sold the Shop with the sitting tenancy at $40,000,000 to the Purchaser which was a subsidiary of the Purchaser's Holding Company.

(e) By a supplemental agreement dated 3 March 2011, the Purchaser agreed to pay a further sum of $59,980,000 as part of consideration for the sale and purchase of the Shop. In the agreement, the Appellant undertook to keep the supplementary agreement in the strictest confidence and should not submit the agreement to the Land Registry for registration.

(f) The Shop was assigned to the Purchaser on 8 April 2011.

12. The Appellant filed its profits tax returns for the years of assessment 2010/11 to 2011/12 together with its audited financial statements, detailed income statements and tax computations.

(a) In the returns, the Appellant declared the following assessable profits/adjusted loss:

Year of Assessment	2010/11	2011/12
	$	$
Assessable Profits/(Adjusted Loss)	98,064	68,480

(b) The Appellant's detailed income statements showed the following particulars:

Year ended	30-09-10	30-09-11
	$	$
Revenue	31,269	344,667
Gain on disposal of property	-	65,976,026
Less:		
Accountancy fee	20,500	27,800
Audit fee	9,000	9,500
Business registration fee	450	450
Depreciation	366,737	-
Office administration fee	70,000	98,000
Professional fees	-	35,000
Sundry expenses	5,605	2,097
	472,292	172,847
Interest on bank loan	12,578	139,540

Year ended	30-09-10	30-09-11
	$	$
Profit/(Loss) before tax	(453,601)	66,008,306

(c) The assessable profits/adjusted loss were computed as follows:

Year of Assessment	2010/11	2011/12
	$	$
Profit/(Loss) before tax	(453,601)	66,008,306
Add:		
Depreciation	366,737	-
Professional fees	-	25,000
Balancing charge	-	11,200
	(86,864)	66,044,506
Less:		
Commercial building allowance	11,200	-
Gain on disposal of property	-	65,976,026
Assessable Profits/(Adjusted Loss)	(98,064)	68,480

Note: The commercial building allowance, balancing charge and the gain on disposal were all related to the Shop.

(d) The gain on disposal of the Shop was computed as follows:

	$	$	$
Sale proceeds			99,980,000
Less: Cost	33,173,290		
Less: accumulated depreciation	366,737	32,806,553	
Valuation fee		146,681	
Commission		999,800	
Legal fee		50,940	34,003,974
Gain on disposal			65,976,026

(e) The Appellant's balance sheet as at 30 September 2010 recorded, among the others, the following asset and liabilities:

Non-current asset	$
The Shop	32,806,553
Current liabilities	
Bank loan due within 12 months, secured	360,000
Amount due to a related party	11,573,323
(unsecured, interest-free, no fixed terms of repayment)	

Non-current liabilities	$
Bank loan, secured	21,640,000

(f) The auditor's report for the year ended 30 September 2010 recorded that there had been concern as to availability of adequate short-term future funding to the Appellant and consequently as to the appropriateness of the going concern basis as the Appellant's current liabilities exceeded its current assets by $11,907,764 at the balance sheet date.

13. On divers dates, the Assessor issued statements of loss to the Appellant for the years of assessment 2005/06 to 2010/11 in accordance with the loss returned. The Appellant did not disagree with the statements.

14. In response to the Assessor's enquiry about the gain on disposal of the Shop, Wise-Link CPA Limited, the Appellant's representative, put forward the following contentions:

(a) The Appellant's original intention for the acquisition of the Shop was for rental purposes. There was no written evidence to record the intention.

(b) No formal feasibility report was prepared. The director understood that the rental income received was enough for repayment of the Term Loan and interest.

(c) The purchase was financed by the Term Loan and funding from the Shareholder.

(d) The amounts of rental income received, principal and interest paid on the Term Loan were as follows:

Year ended	Rental Income	Principal	Interest
	$	$	$
30 September 2010	31,269	-	12,578
30 September 2011	344,667	180,000	139,540

The outstanding principal of $21,820,000 was repaid after disposal of the Shop.

(e) The Appellant was forced to sell the Shop under the Lands (Compulsory Sale for Redevelopment) Ordinance.

(f) The Appellant received the Notice of Application to the Lands Tribunal for an Order for Sale under the Lands (Compulsory Sale for

Redevelopment) Ordinance ('Notice of Application to the Lands Tribunal') dated 14 February 2011.

(g) The selling price was ascertained after negotiation between the Appellant and the Purchaser.

(h) Part of the sales proceeds was used to repay liabilities. The Appellant's shareholder kept the surplus fund for future business whenever there was good investment opportunity.

15. Wise-Link CPA Limited provided copies of the following documents:

(a) Notice of Application to the Lands Tribunal.

(b) List of majority owners of the Building. They were the applicants before the Lands Tribunal:

1	The Purchaser
2 – 17	[Names not disclosed here]

(c) List of tenants in the Building. One of the tenants was the alleged Associated Company.

(d) Valuation report issued by Valuer to the Purchaser on 11 February 2011. According to the report, the market value of the Shop as at 17 January 2011, disregarding any redevelopment potential, was $33,230,000.

16. Having considered the available information, the Assessor considered that:

(a) The Appellant's expenses for the years of assessment 2008/09 and 2009/10 should be disallowed since the Appellant was dormant during the years.

(b) The gain on disposal of the Shop in the year of assessment 2011/12 should be chargeable to profits tax and the Appellant should not be entitled to commercial building allowance in the year of assessment 2010/11 in respect of the property.

17. On divers dates, the Assessor issued revised statements of loss and raised Profits Tax Assessment for the years of assessment 2008/09 to 2011/12 as follows:

Year of assessment	2008/09	2009/10	2010/11	2011/12
	$	$	$	$

Year of assessment	2008/09	2009/10	2010/11	2011/12
	$	$	$	$
Profit/(Loss) per return	(555)	(6,855)	(98,064)	68,480
Add:				
Commercial building allowance	-	-	11,200	-
Gain on disposal of property	-	-	-	65,609,289
Expenses disallowed	555	6,855	-	-
Less:				
Balancing charge	-	-	-	11,200
Assessable Profits/(Adjusted Loss)	-	-	(86,864)	65,666,569
Less: Loss set-off				(361,760)
Net Assessable Profits				65,304,809
Tax Payable thereon	Nil	Nil	Nil	10,763,293
Statement of Loss				
Loss brought forward	274,896	274,896	274,896	361,760
Add: Adjusted Loss for the year	-	-	86,864	-
Less: Loss set-off	-	-	-	(361,760)
Loss carried forward	274,896	274,896	361,760	-

Note: The gain on disposal of property was the sum of the amount per tax computation of $65,976,026 and the depreciation charge of $366,737.

18. Wise-Link CPA Limited, on behalf of the Appellant, objected to the above assessment on the ground that the gain on disposal of the Shop was capital in nature and should not be taxable. Wise-Link CPA Limited supplied the following additional information and copies of documents:

(a) The Appellant resumed its operation when there was an investment opportunity.

(b) There was an instruction to the Appellant's auditor to state in the director's report the Appellant's principal activity as property investment.

(c) Property agents gave the Appellant list of properties with good investment potential. The Appellant did not keep any correspondence with the Agent. The Appellant exchanged information with the Agent by phone. Copies of the following documents were provided:

(i) A set of documents dated 3 May 2010 from the Agent to the Assistant about the Shop.

(ii) Invoice no. [number not disclosed here] dated 8 April 2011 issued by the Agent to the Appellant (for attention of the Assistant) in respect of the professional service fee for the Appellant as 'Vendor' of the Shop in the amount of $999,800.

(d) The Appellant did not keep any documents related to the application for the Term Loan.

(e) The Appellant could not object to the Bank's request to increase the monthly repayment of principal of the Term Loan from $30,000 for the first 18 instalments to $132,000 from the 19th instalment.

(f) The Shareholder's source of fund was from his personal savings.

(g) The Appellant was approached by the agent of the Purchaser on 28 January 2011 with an offer to buy the Shop at a price of $70,000,000.

(h) Most of the negotiation with the Purchaser was through the Agent. The Appellant did not keep any correspondence regarding to the negotiation. The engagement letter of the Agent could not be found.

(i) As the property agent informed the Appellant that in case over 90% of the shares in the Building agreed for the redevelopment, it was compulsory for the rest of the owners to sell their properties for redevelopment. After careful consideration, the Appellant, instead of spending legal fee on filing an opposition against the redevelopment, favoured to sell the Shop at an optimistic market price.

(j) The Appellant had become dormant after the disposal of the Shop.

19. A company in the Purchaser's listed group, on behalf of the Purchaser, provided the following information and documents to the Assessor:

(a) On 9 August 2010, the Purchaser appointed representatives for handling the acquisition of the undivided shares of the Building erected on the Land.

(b) By the end of year 2010, the Purchaser had already acquired and/or entered into legally binding agreements to acquire over 90% of the undivided shares of the Building.

(c) On 6 January 2011, the Purchaser's solicitor sent a letter to the Appellant informing the Purchaser's intention to purchase the Shop from the Appellant.

(d) Another letter dated 25 January 2011 was sent to the Appellant informing the Purchaser's intention of making an application to the Lands Tribunal for an order for sale of all the undivided shares of and in the Building and the Land; and the Purchaser's offer to purchase the Shop from the Appellant at $47,500,000 after taking into account the redevelopment potential.

(e) The Purchaser's representatives had contacted the following persons and solicitors of the Appellant in acquiring the Shop:

(i) The Shareholder;

(ii) The Assistant; and

(iii) A named partner of the Appellant's solicitors.

20. In response to the Assessor's draft statement of facts, Wise-Link CPA Limited contended that:

(a) In paragraph 15(c), the reference to alleged Associated Company was irrelevant and should be deleted.

(b) The Appellant was able to secure a cheap finance from the bank at a favourable rate of 1% per annum over HIBOR. For the month ended 12 October 2010, the interest rate was only 1.15929% per annum and the instalment payable for the month was $50,962.50. The Appellant expected that the interest rate would not fluctuate substantially from this rate in future. The balance of the purchase price was financed by the Shareholder interest free.

(c) Since the Shop was already let out and the rent would be increased to $60,000 per month from 1 May 2011, the return would be 2.28% per annum. After 30 April 2012, it would be possible to increase the rent such that the rate of return would be even higher. The rental income would yield a reasonable return after payment of the interest to the bank. The Net return was much better than the return from saving deposit. The Shop was therefore a good long-term investment.

Grounds of appeal

21. By letter dated 13 June 2013, Wise-Link CPA Limited gave notice of appeal on behalf of the Appellant on the following grounds:

' (a) That the original intention of the [Appellant] was to acquire [the Shop] as a long term investment for rental income purpose;

(b) That the profits derived from the sale of the Shop are capital in nature and not subject to profits tax.'

Authorities

Onus of proof, shifting burden of proof, accounting treatment, sparsity of evidence and the Board's function

22. Whether the Commissioner gave correct reasons for his determination is a matter of historical interest. The Board considers the matter *de novo* to decide whether the assessment appealed against is shown by the taxpayer to be incorrect or excessive:

(1) Section 68(4) of the Ordinance, Chapter 112, ('the Ordinance') provides that:

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

(2) In Kim Eng Securities (Hong Kong) Ltd v CIR (2007) 10 HKCFAR 213, Bokhary PJ referred in paragraph 5 to counsel for the taxpayer's citation of Wing Tai Development Co Ltd v CIR [1979] HKLR 642 on section 68(4) and his Lordship stated at paragraph 50 that a taxpayer is not entitled to benefit from sparsity in evidence as it bears the burden of showing that the assessments are wrong:

' *In relation to dealings on the other foreign stock exchanges, the evidence is sparse. The Taxpayer is not in the position to benefit from such sparsity. After all, it bears the burden of showing that the assessments are wrong.*'

(3) In Real Estate Investments (NT) Limited v Commissioner of Inland Revenue, (2008) 11 HKCFAR 433, Bokhary and Chan PJJ said at paragraphs 32 to 35 that the notion of a shifting onus, is seldom if ever helpful and certainly it cannot shift the onus of proof from where section 68(4) places it:

' *32. ... It is natural and appropriate to strive to decide on something more satisfying than the onus of proof. And it should generally be possible to do so. But tax appeals do begin on the basis that, as s.68(4) of the Inland Revenue Ordinance provides, "[t]he onus of proving that the assessment appealed against is excessive or incorrect shall be on the Appellant". And it is possible although rare for such an appeal to end – and be disposed of – on that basis.*

33. As noted above, the Property had 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.

35. As for the notion of a shifting onus, such a notion is seldom if ever helpful. Certainly it cannot shift the onus of proof from where s.68(4) of the Inland Revenue Ordinance places it, namely on a taxpayer who appeals against an assessment to show that it is excessive or incorrect.'

(4) In Shui On Credit Company Limited v Commissioner of Inland Revenue, (2009) 12 HKCFAR 392, Lord Walker NPJ said at paragraphs 29 and 30 that the Board's function is to consider the matter de novo and the appeal is an appeal against an assessment:

' *29. As the Board correctly observed, by reference to the decisions in Mok Tsze Fung v. CIR [1962] HKLR 258 and (after the amendment of s.64 of the IRO) CIR v. The Hong Kong Bottlers Ltd [1970] HKLR 581, the Commissioner's function, once objections had been made by the taxpayer, was to make a general review of the correctness of the assessment. In Mok Mills-Owens J said at pp 274-275:*

> *"His duty is to review and revise the assessment and this, in my view, requires him to perform an original and administrative, not an appellate and judicial, function of considering what the proper assessment should be. He acts de novo, putting himself in the place of the Assessor, and forms, as it were, a second opinion in substitution for the opinion of the Assessor."*

> *30. Similarly the Board's function, on hearing an appeal under s.68, is to consider the matter de novo: CIR v. Board of Review ex parte Herald International Limited [1964] HKLR 224, 237. The taxpayer's appeal is from a determination (s.64(4)) but it is against an assessment (s.68(3) and (4)). The taxpayer's counsel drew attention to the fact that when Part XI was amended in 1965, the wording of s.68(4) was altered to refer to the onus of proving that the assessment was "excessive or incorrect" (rather than simply "excessive"). This, it was argued, showed that the amount of an assessment was no longer always the essential issue. Counsel for the Commissioner could not suggest any particular reason for the alteration, other than a general tidying-up of the language. Whatever the explanation, I am satisfied that the alteration was not intended, by what is sometimes called a side-wind, to make a major change in the scheme and effect of Part XI of the IRO.'*

The importance of the grounds of appeal

23. The grounds of appeal govern the scope of the admissible evidence and they define the issues on appeal, section 68(7).

24. Unless permitted by the Board under section 66(3), the appeal is confined to the original grounds of appeal and applications for the Board's consent to amend the grounds of appeal 'should be sought fairly, squarely and unambiguously'[2].

> *' 9. By its representative, each of the Taxpayers put forward the grounds of appeal that the profits in question "were capital in nature and were not assessable to Profits Tax or alternatively that the assessment was excessive". None of the Taxpayers pursued its alternative ground that the assessments were excessive. That left only one question raised by the grounds of appeal given in accordance with s.66(1). Did the profits in question arise from the sale of capital assets? But at the hearing before us, Mr Patrick Fung SC for the Taxpayers contended that there was an antecedent question. Were the profits in question from the carrying on of a trade, profession or business?*
>
> *10. No such question is raised by the Taxpayers' grounds of appeal given in accordance with s.66(1). But Mr Fung contended that the Board is to be treated as having consented under s.66(3) to the Taxpayers relying on a fresh ground which raised such a question. For this contention, Mr Fung relied on an exchange between the Board's chairman and the Taxpayers' counsel (not Mr Fung or his junior Ms Catrina Lam). That exchange took place after the close of the evidence and during final*

[2] See China Map Limited v CIR (2008) 11 HKCFAR 486 at paragraphs 9 and 10.

> *speech. By its nature, such a question is fact-sensitive and its answer inherently dependent on evidence. For a tribunal of fact to entertain such a question after the close of the evidence would be unusual and plainly inappropriate if done without offering the party against whom the question is raised an opportunity to call further evidence. No such opportunity was offered to the Revenue. We do not think that the Board is to be treated as having consented under s.66(3) to the Taxpayers relying on a fresh ground which raised the antecedent question for which Mr Fung now contends. If and whenever s.66(3) consent is sought, it should be sought fairly, squarely and unambiguously. Nothing of that kind occurred in this case.*'

Capital or trading/business issue

25. Section 2 of the Ordinance defines:

- '*business*' as including '*agricultural undertaking, poultry and pig rearing and the letting or sub-letting by any corporation to any person of any premises or portion thereof, and the sub-letting by any other person of any premises or portion of any premises held by him under a lease or tenancy other than from the Government*' and

- '*trade*' as including '*every trade and manufacture, and every adventure and concern in the nature of trade*'.

26. Section 14 is the charging provision on profits tax. Sub-section (1) 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.*'

Onus of proof

27. Section 68(4) provides that the '*onus of proving that the assessment appealed against is excessive or incorrect shall be on the Appellant*'. See also paragraphs 29 and 36 below.

Costs

28. Section 68(9) provides that:

> ' *Where under subsection (8), the Board does not reduce or annul such assessment, the Board may order the Appellant to pay as costs of the Board a sum not exceeding the amount specified in Part 1 of Schedule 5, which shall be added to the tax charged and recovered therewith.*'
>
> The amount specified in Part 1 of Schedule 5 is $5,000.

Simmons

29. Lord Wilberforce stated in Simmons v IRC [1980] 1 WLR 1196 at page 1199 that the relevant question is whether the stated 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? His Lordship recognised that intention may be changed (at page 1199) and that a sale of an investment does not render its disposal a sale in the course of trade unless there has been a change of intention (at page 1202):

> ' *One must ask, first, what the commissioners were required or entitled to find. 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. If findings of this kind are to be made precision is required, since a shift of an asset from one category to another will involve changes in the company's accounts, and, possibly, a liability to tax: see Sharkey v. Wernher [1956] A.C. 58. 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. It must be one or other, even though, and this seems to me legitimate and intelligible, the company, in whatever character it acquires the asset, may reserve an intention to change its character. To do so would, in fact, amount to little more than making explicit what is necessarily implicit in all commercial operations, namely that situations are open to review.*' (at page 1196)
>
> ' *Finally as to the decision of the Court of Appeal, the judgment, delivered by Orr L.J., contains a clear account of the facts, and, in my respectful opinion, a generally correct statement of the law. In particular, it is rightly recognised*

> *that a sale of an investment does not render its disposal a sale in the course of trade unless there has been a change of intention.*' (at page 1202)

In the Court of Appeal, Orr L J accepted that it was clearly established that on appeal to the Commissioners[3] the burden is on the taxpayer to displace the assessment and in the circumstances the burden was clearly on the taxpayers to establish that the sales in question gave rise to a surplus on capital account and not to a trading profit. His Lordship stated the general principles in these terms:

> ' *It is also clearly established that on appeal to the Commissioners the burden is on the taxpayer to displace the assessment, and in these circumstances the burden in the present case was clearly on the taxpayers to establish that the sales in question gave rise to a surplus on capital account and not to a trading profit (Norman v Golder 26 TC 293, at page 297, and Shadford v H Fairweather & Co Ltd 43 TC 291, at page 300). On the other hand it is also clear that if an asset is acquired in the first instance as an investment the fact that it is later sold does not take it out of the category of investment or render its disposal a sale in the course of trade unless there has been a change of intention on the part of the owner between the dates of acquisition and disposal (Eames v Stevnell Prouerties Ltd 43 TC 678). The question, moreover, whether an item is held as capital or as stock-in-trade is not concluded by the way in which it has been treated in the owner's books of account (CIR v Scottish Automobile and General Insurance Co Ltd 16 TC 381, at page 390) or by the Revenue in past years (Rellim Ltd v Vise 32 TC 254).'* [l980] 53 TC 461 at paragraphs 488 and 489.

Marson v Morton

30. In Marson v Morton [1986] 1 WLR 1343 at pages 1347 – 1349, Sir Nicholas Browne-Wilkinson VC thought that the only point which was as a matter of law clear was that a single, one-off transaction can be an adventure in the nature of trade and the question is whether the taxpayer was investing the money or was he doing a deal. His Lordship stated that:

- Only one point is as a matter of law clear, namely that a single, one-off transaction can be an adventure in the nature of trade.
- The purpose of authority is to find principle, not to seek analogies on the facts.
- The question whether or not there has been an adventure in the nature of trade depends on all the facts and circumstances of each particular case and depends on the interaction between the various factors that are present in any given case.

[3] In Hong Kong, the appeal is to the Board.

- The most that his Lordship had been able to detect from the reading of the authorities is that there are certain features or badges which may point to one conclusion rather than another and that the factors are in no sense a comprehensive list of all relevant matters, nor is any one of them decisive in all cases. The most they can do is provide common sense guidance to the conclusion which is appropriate. The matters which are apparently treated as a badge of trading are as follows:

  ' *(i) The transaction in question was a one-off transaction. Although a one-off transaction is in law capable of being an adventure in the nature of trade, obviously the lack of repetition is a pointer which indicates there might not here be trade but something else.*

  (ii) Is the transaction in question in some way related to the trade which the taxpayer otherwise carries on? For example, a one-off purchase of silver cutlery by a general dealer is much more likely to be a trade transaction than such a purchase by a retired colonel.

  (iii) The nature of the subject matter may be a valuable pointer. Was the transaction in a commodity of a kind which is normally the subject matter of trade and which can only be turned to advantage by realisation, such as referred to in the passage that the chairman of the commissioners quoted from Inland Revenue Commissioners v. Reinhold, 1953 S.C. 49. For example, a large bulk of whisky or toilet paper is essentially a subject matter of trade, not of enjoyment.

  (iv) In some cases attention has been paid to the way in which the transaction was carried through: was it carried through in a way typical of the trade in a commodity of that nature?

  (v) What was the source of finance of the transaction? If the money was borrowed that is some pointer towards an intention to buy the item with a view to its resale in the short term; a fair pointer towards trade.

  (vi) Was the item which was purchased resold as it stood or was work done on it or relating to it for the purposes of resale? For example, the purchase of second-hand machinery which was repaired or improved before resale. If there was such work done, that is again a pointer towards the transaction being in the nature of trade.

(vii) Was the item purchased resold in one lot as it was bought, or was it broken down into saleable lots? If it was broken down it is again some indication that it was a trading transaction, the purchase being with a view to resale at profit by doing something in relation to the object bought.

(viii) What were the purchasers' intentions as to resale at the time of purchase? If there was an intention to hold the object indefinitely, albeit with an intention to make a capital profit at the end of the day, that is a pointer towards a pure investment as opposed to a trading deal. On the other hand, if before the contract of purchase is made a contract for resale is already in place, that is a very strong pointer towards a trading deal rather than an investment. Similarly, an intention to resell in the short term rather than the long term is some indication against concluding that the transaction was by way of investment rather than by way of a deal. However, as far as I can see, this is in no sense decisive by itself.

(ix) Did the item purchased either provide enjoyment for the purchaser, for example a picture, or pride of possession or produce income pending resale? If it did, then that may indicate an intention to buy either for personal satisfaction or to invest for income yield, rather than do a deal purely for the purpose of making a profit on the turn. I will consider in a moment the question whether, if there is no income produced or pride of purchase pending resale, that is a strong pointer in favour of it being a trade rather than an investment.'

- In order to reach a proper factual assessment in each case it is necessary to stand back, having looked at those matters, and look at the whole picture and ask the question – and for this purpose it is no bad thing to go back to the words of the statute – was this an adventure in the nature of trade? In some cases perhaps more homely language might be appropriate by asking the question, was the taxpayer investing the money or was he doing a deal?

All Best Wishes

31. Mortimer J (as he then was) pointed out in All Best Wishes Limited v CIR (1992) 3 HKTC 750 at page 770 and page 771 that – 'was this an adventure and concern in the nature of trade' is a decision of fact and the fact to be decided is defined by the Statute.

> ' *Reference to cases where analogous facts are decided, is of limited value unless the principle behind those analogous facts can be clearly identified.*' (at page 770)

> ' *The Taxpayer submits that this intention, once established, is determinative of the issue. That there has been no finding of a change of intention, so a finding that the intention at the time of the acquisition of the land that it was for development is conclusive.*
>
> *I am unable to accept that submission quite in its entirety. I am, of course, bound by the Decision in the Simmons case, but it does not go quite as far as is submitted. This is a decision of fact and the fact to be decided is defined by the Statute - was this an adventure and concern in the nature of trade? 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. Having said that, I do not intend in any way to minimize the difficulties which sometimes arise in drawing the line in cases such as this, between trading and investment.*' (at page 771)

Lee Yee Shing

32. Lee Yee Shing v The Commissioner of Inland Revenue (2008) 11 HKCFAR 6 is a case on share dealing activities.

33. Bokhary PJ and Chan PJ emphasised at paragraph 38 that the question whether something amounts to the carrying on of a trade or business is a question of fact and degree to be answered by the fact-finding body upon a consideration of all the circumstances. McHugh NPJ thought that ultimately, the issue is one of fact and degree[4].

34. On the question of 'trade', McHugh NPJ pointed out that the intention to trade referred to by Lord Wilberforce in Simmons was not subjective, but objective, to be inferred from all the circumstances of the case. His Lordship stated that:

> (a) No principle of law defines trade. Its application requires the tribunal of fact to make a value judgment after examining all the circumstances involved in the activities claimed to be a trade. (at paragraph 56)

[4] See paragraph 35(c) below.

(b) The intention to trade to which Lord Wilberforce referred in Simmons is not subjective but objective: Iswera v Commissioner of Inland Revenue [1965] 1 WLR 663 at 668. It is inferred from all the circumstances of the case, as Mortimer J pointed out in All Best Wishes Ltd v Commissioner of Inland Revenue (1992) 3 HKTC 750 at 771. A distinction has to be drawn between the case where the taxpayer concedes that he or she had the intention to resell for profit when the asset or commodity was acquired and the case where the taxpayer asserts that no such intention existed. If the taxpayer concedes the intention in a case where the taxing authority claims that a profit is assessable to tax, the concession is generally but not always decisive of intention: Inland Revenue Commissioners v Reinhold (1953) 34 TC 389. However, in cases where the taxpayer is claiming that a loss is an allowable deduction because he or she had an intention to resell for profit or where the taxpayer has made a profit but denies an intention to resell at the date of acquisition, the tribunal of fact determines the intention issue objectively by examining all the circumstances of the case. It examines the circumstances to see whether the 'badges of trade' are or are not present. In substance, it is 'the badges of trade' that are the criteria for determining what Lord Wilberforce called 'an operation of trade'. (at paragraph 59)

(c) What then are the 'badges of trade' that indicate an intention to trade or, perhaps more correctly, the carrying on of a trade? An examination of the many cases on the subject indicates that, for most cases, they are whether the taxpayer:

1. has frequently engaged in similar transactions?

2. has held the asset or commodity for a lengthy period?

3. has acquired an asset or commodity that is normally the subject of trading rather than investment?

4. has bought large quantities or numbers of the commodity or asset?

5. has sold the commodity or asset for reasons that would not exist if the taxpayer had an intention to resell at the time of acquisition?

6. has sought to add re-sale value to the asset by additions or repair?

7. has expended time, money or effort in selling the asset or commodity that goes beyond what might be expected of a non-trader seeking to sell an asset of that class?

8. has conceded an actual intention to resell at a profit when the asset or commodity was acquired?

9. has purchased the asset or commodity for personal use or pleasure or for income? (at paragraph 60)

(d) In some cases, the source of finance for the purchase may also be a badge of trade, particularly where the asset or commodity is sold shortly after purchase. But borrowing to acquire an asset or commodity is usually a neutral factor. (at paragraph 61)

35. On the question of 'business', it has long been recognised that business is a wider concept than trade, per Bokhary PJ and Chan PJ at paragraph 17. McHugh NPJ is of the same view, stating in paragraph 68 that business is a wider term than trade. McHugh NPJ went on to state that:

(a) What then is the definition or ordinary meaning of 'business'? The answer is that there is no definition or ordinary meaning that can be universally applied. Nevertheless, ever since Smith v. Anderson (1880) 15 Ch D 247, common law courts have never doubted that the expression 'carrying on' implies a repetition of acts and that, in the expression 'carrying on a business', the series of acts must be such that they constitute a business: Smith v Anderson (1880) 15 Ch D 247 at 277 – 278 per Brett LJ. Much assistance in this context is also gained from the statement of Richardson J in Calkin v Commissioner of Inland Revenue [1984] 1 NZLR 440 at 446 where he said 'that underlying … the term "business" itself when used in the context of a taxation statute, is the fundamental notion of the exercise of an activity in an organised and coherent way and one which is directed to an end result'. In Rangatira Ltd v Commissioner of Inland Revenue [1997] STC 47, the Judicial Committee said that it found these words of Richardson J 'of assistance'. (at paragraph 69).

(b) Ordinarily, a series of acts will not constitute a business unless they are continuous and repetitive and done for the purpose of making a gain or profit: Hope v Bathurst City Council (1980) 144 CLR 1 at 8 – 9 per Mason J; Ferguson v Federal Commissioner of Taxation (1979) 79 ATC 4261 at 4264. However, as Lord Diplock pointed out in American Leaf Blending Co Sdn Bhd v Director-General of Inland Revenue (Malaysia) [1979] AC 676 at 684 'depending on the nature of the business, the activity may be intermittent with long intervals of quiescence in between'. Exceptionally, a business may exist although the shareholders or members cannot obtain any gain or profit from the activities of the business: Inland Revenue Commissioners v Incorporated Council of Law Reporting (1888) 22 QBD 279 (law reporting body prohibited by its

constitution from dividing profits among members). It may exist even though the object of the activities is to make a loss: c.f. Griffiths v JP Harrison (Watford) Ltd [1963] AC 1 (dividend stripping operation). And a corporation, firm or business may carry on business in a particular country even though its profits are earned in another country: South India Shipping Corp Ltd v Export-Import Bank of Korea [1985] 2 All ER 219. (at paragraph 70)

(c) While engaging in activities with a view to profit making is an important indicator, and in some cases an essential characteristic, of a business, a profit making purpose does not conclude the question whether the activities constitute a business. Whether or not they do depends on a careful analysis of all the circumstances surrounding the activities. Some may indicate the existence of a business; some may indicate that no business exists. Ultimately, the issue is one of fact and degree. But, as Edwards v Bairstow [1956] AC 14, Hope v Bathurst City Council (1980) 144 CLR 1 and Lewis Emanuel & Son Ltd v White (1965) 42 TC 369 show, the issue becomes one of law and not fact where the only reasonable conclusion to be drawn from the facts found or admitted is that the activities in question did or did not constitute the carrying on of a business. In such a case, an appellate court, although debarred from finding facts, may reverse the finding of the tribunal of fact and hold that a business was or was not being carried on. (at paragraph 71)

Real Estate Investments

36. In Real Estate Investments (NT) Limited v The Commissioner of Inland Revenue (2008) 11 HKCFAR 433, Bokhary PJ and Chan PJ stated that, given section 68(4), it is possible although rare for such an appeal to end – and be disposed of – on the basis of burden of proof and that the onus cannot be shifted:

> ' *It is natural and appropriate to strive to decide on something more satisfying than the onus of proof. And it should generally be possible to do so. But tax appeals do begin on the basis that, as s.68(4) of the Inland Revenue Ordinance provides, "[t]he onus of proving that the assessment appealed against is excessive or incorrect shall be on the Appellant". And it is possible although rare for such an appeal to end – and be disposed of – on that basis*', at paragraph 32.

> ' *As for the notion of a shifting onus, such a notion is seldom if ever helpful. Certainly it cannot shift the onus of proof from where s.68(4) of the Inland Revenue Ordinance places it, namely on a taxpayer who appeals against an assessment to show that it is excessive or incorrect)*', at paragraph 35.

37. Their Lordships went on to state that:

- the badges of trade are no less helpful here than in the United Kingdom;
- they do not fall to be considered separately from the issue of intention or any assertion made by Taxpayer or on its behalf as to intention; and
- 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.

‘ *It is clear that question (ii)(b) uses the expression "badges of trade" to mean the circumstances that shed light on the issue of intention. Those circumstances simply do not fall to be considered separately from the issue of intention or any assertion made by Taxpayer or on its behalf as to intention*’, at paragraph 40.

‘ *Suppose a tax assessment is made on the footing that the position is X and the taxpayer appeals against the assessment by contending that the position is Y. The taxpayer will have to prove his contention. So his appeal to the Board of Review would fail if the Board positively determines that, contrary to his contention, the position is X. And it would likewise fail if the Board merely determines that he has not proved his contention that the position is Y. Either way, no appeal by the taxpayer against the Board's decision could succeed on the "true and only reasonable conclusion" basis unless the court is of the view that the true and only reasonable conclusion is that the position is Y*’, at paragraph 47.

‘ *... 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*’ at paragraph 53.

‘*In regard to one of the badges of trade which he listed in Marson v. Morton, the Vice-Chancellor said this (at p.1348 F-G):*

> *"What was the source of finance of the transaction? If money was borrowed that is some pointer towards an intention to buy the item with a view to its resale in the short term; a fair pointer towards trade."*

That is as far as it goes, which is not very far when taken on its own. At p.1349 C-D the Vice-Chancellor emphasised that his list is not comprehensive, that no single item is in any way decisive and that it is always necessary to look at the whole picture.

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' at paragraphs 54 to 55.

Shop – trading stock or capital asset

38. The Appellant's case, as stated in its grounds of appeal, is that:

' the original intention of the [Appellant] was to acquire [the Shop] as a long term investment for rental income purpose.'

39. The acquisition price was $31,480,000.

(1) For the period between the time of acquisition in September 2010 to 30 April 2011, the monthly rental was $55,000. The *gross* annual rate of return, i.e. the total annual rate of return *before* the deduction of any fees or expenses, is 2.10%. At this rate and assuming *full* occupancy during the whole period, it would take 47.62 years to recoup the acquisition price.

(2) For the period from May 2011 to 30 April 2012, the monthly rental was $60,000. The *gross* annual rate of return, i.e. the total annual rate of return *before* the deduction of any fees or expenses, is 2.29%. At this rate and assuming *full* occupancy during the whole period, it would take 43.67 years to recoup the acquisition price.

40. The Shareholder opined that monthly rental could increase by 30% above $60,000 as from 1 May 2012, i.e. $78,000. Taking it at its face value, the *gross* annual rate of return, i.e. the total annual rate of return *before* the deduction of any fees or expenses, is 2.97%. At this rate and assuming *full* occupancy during the whole period, it would take 33.67 years to recoup the acquisition price.

41. In our decision, it requires a lot of convincing to persuade us that the Appellant and the Shareholder genuinely intended to invest in a property with at best 2.97% *gross* annual return.

42. The 30% increase was a bare assertion which we reject. In the absence of convincing evidence in support, and there is nothing more than bare assertion. In our decision, the rental for the Shop in the 48-year old Building tends to drop instead of rise.

43. We have been looking at gross annual returns in paragraphs 39 and 40 above, i.e. *before* the deduction of any fees or expenses. In our decision, the Appellant will have to incur at least maintenance expenses in the decades ahead. The objective fact is that the Building was a 48-old building completed in 1962. Looking at the matter objectively, the

Building would be affected by further wear and tear as time goes by and maintenance costs would come in.

44. There is the question of costs of funds. The acquisition of the Shop was funded *entirely* by borrowed fund. The interest rate for the Term Loan was 1% above 1-month HIBOR rates. So, the minimum interest rate is 1% with monthly rests. This would reduce the 2.10%, 2.29% and 2.97% returns.

45. Further, HIBOR rates can and do fluctuate. It is a pure assumption that it would remain low for decades. The Shareholder merely opined that rates would remain low for at least 3 years. How about the decades ahead?

46. The balance of $9,480,000 for the acquisition was funded by the Shareholder. Irrespective of whether he could afford it to fund it on a long term basis, we are not persuaded that he would spend $9,480,000 on an investment with nil return for decades.

47. The consideration and analysis above proceeds on the assumption of *full* occupancy of the Shop for decades. That the Tenant is a good or reputable tenant only means that he will not default in payment of rent. That by itself does not increase the return. There is no basis for assuming that it will remain the tenant for decades. There is no basis for assuming *full* occupancy of the Shop for decades. The inherent probabilities are against both assumptions.

48. (1) The provisional acquisition agreement provided for completion in 4 months. 4 months was a bit longer than normal completion periods. Speculators tend to favour long completion periods to give themselves more time for sub-sale before completion so as to reduce the costs of stock. The Appellant offered no explanation for the 4 months completion period.

(2) Monthly repayment of principal under the Term Loan was $30,000 for the first 18 months and $132,500 thereafter. The Appellant was asked whether the Term Loan repayments were structured in this away so as to reduce the costs of stock during the initial 18 months for it to try to sub-sell. The Appellant failed to give any innocuous explanation. In fact, it gave no direct response.

(3) The sale by the Appellant to the Purchaser was documented in such a way as to hide a substantial part of the sale price from the documents submitted for registration at the Land Registry under the Land Registration Ordinance, Chapter 128.

The preamble to that Ordinance, provides that:

> ' *WHEREAS it is expedient to prevent secret and fraudulent conveyances, and to provide means whereby the title to real and immovable property may be easily traced and ascertained*'.
>
> In [1913] HKLR 52 at page 66, Havilland De Sausmarez, Presiding Judge, said:
>
> ' *The effect of the Ordinance, as I read it, is to make registration the test of priority, and by imposing harsh terms on persons failing to register to compel them to do so, and, further, to remove the doctrine of notice from transactions in land in the Colony. For this course I can see excellent reasons. The Colony in 1844 was in the first year of its existence, it was of small extent, and it was possible to secure a perfect system of registration for there were no existing difficulties in the way; moreover to open a way amongst an Oriental people to avoid registration by proof of notice whether actual or constructive would be to encourage fraud.'*
>
> The Appellant offered no explanation for their less than candid approach in drawing up conveyancing documents designed for public access and reference.

49. If there was an explanation for matters referred to in paragraph 48 above, the Appellant chose not to offer any. This is a matter for it but it is not in the position to benefit from lack or sparsity in evidence. As Bokhary PJ said in Kim Eng Securities (Hong Kong) Ltd v CIR (2007) 10 HKCFAR 213 at paragraph 50:

> ' *The bulk of the evidence relates to dealings on the Singapore Stock Exchange. In relation to dealings on the other foreign stock exchanges, the evidence is sparse. The Taxpayer is not in the position to benefit from such sparsity. After all, it bears the burden of showing that the assessments are wrong.*'

Badges of trade

50. For the reasons given above, this appeal fails and must be dismissed.

51. For completeness, we turn to the badges of trade summarised by McHugh NPJ in Lee Yee Shing:

> (1) Whether the appellant has frequently engaged in similar transactions: The Appellant had traded in property once before.
>
> (2) Whether the appellant has held the asset or commodity for a lengthy period: less than 1 year.

(3) Whether the appellant has acquired an asset or commodity that is normally the subject of trading rather than investment: The Shop can be the subject of trading or investment.

(4) Whether the appellant has bought large quantities or numbers of the commodity or asset: No.

(5) Whether the appellant has sold the commodity or asset for reasons that would not exist if the taxpayer had an intention to resell at the time of acquisition: No.

(6) Whether the appellant has sought to add re-sale value to the asset by additions or repair: No.

(7) Whether the appellant has expended time, money or effort in selling the asset or commodity that goes beyond what might be expected of a non-trader seeking to sell an asset of that class: No.

(8) Whether the appellant has conceded an actual intention to resell at a profit when the asset or commodity was acquired: No.

(9) Whether the appellant has purchased the asset or commodity for personal use or pleasure or for income: Not for personal use or pleasure. The claim of purchase for rental income has been considered and analysed above.

(10) Source of finance: Entirely on borrowed funds.

52. Upon a holistic consideration of the circumstances of this particular case, we conclude that the Appellant was doing a deal. In other words, it carried on an adventure in the nature of trade and acquired the Shop as a trading stock.

53. The appeal fails and falls to be dismissed.

54. For completeness, we record that we have told the Appellant that there was no need to deal with the matters objected to in paragraph 20(a) above. We do not think we could draw the inference of the alleged Associated Company tipping off the Agent and draw the further inference of the alleged Agent tipping off the Appellant.

Disposition

55. We confirm the assessment appealed against and dismiss the appeal.