

Case No. D23/16

Profits tax – sale of property – whether receipt capital in nature – sections 2(1), 14(1), 68(4) and (9) of Inland Revenue Ordinance, Chapter 112 ('IRO')

Panel: Chui Pak Ming Norman (chairman), Ha Suk Ling Shirley and William M F Wong SC

Dates of hearing: 16 and 17 May 2016.

Date of decision: 23 August 2016.

The Appellant acquired a property ('Property B') allegedly with an intention to hold the property as an investment for long term basis at the time of signing the formal agreement for sale and purchase. However, only 15 days after the signing of the agreement for acquisition and 13 days after the completion of the sale and purchase, Property B was sold at a price of about 46% higher than the acquisition price.

The Appellant claimed that the gain it had derived from the sale of Property B was capital in nature and should not be subject to profits tax.

Held:

1. Taking a holistic consideration of the circumstances of the appeal, the objective facts were not consistent with the Appellant's stated intention that Property B was acquired for long term investment purpose.
2. The Appellant's intention at the time of selling Property B was to sell it for trading purpose. There was no change in the Appellant's intention that Property B was for trading purpose between the time of acquisition and the time of sale.
3. The Appellant failed to discharge the onus of proof under section 68(4) of the IRO that the assessments were excessive or incorrect.
4. The Appellant sold the property in question within 15 days after its completion and made a profit of 46%. It required a lot of convincing evidence to support its claim that the property was acquired by it for long term investment purposes. The evidences adduced by the Appellant to support its reasons for the disposal of the property within a very short period of time after its acquisition were flimsy, vague and contradictory and hard to believe. There was no reasonable prospect of success in the appeal. This appeal was frivolous and vexatious.

Appeal dismissed and costs order in the amount of \$25,000 imposed.

Cases referred to:

Church Body of the Hong Kong Sheng Kung Hui & Anor v Commissioner of Inland Revenue, FACV 16/2015 (unreported, 4 February 2016)
Lee Yee Shing v Commissioner of Inland Revenue (2008) 11 HKCFAR 6
Simmons v IRC [1980] 1 WLR 1196
Wing On Cheong Investment Co Ltd v Commissioner of Inland Revenue (1987) 3 HKTC 1
Real Estate Investments (NT) Ltd v Commissioner of Inland Revenue [2007] 1 HKLRD 198
Real Estate Investments (NT) Ltd v Commissioner of Inland Revenue (2008) 11 HKCFAR 433
Commissioner of Inland Revenue v Reinhold (1953) 34 TC 389
Commissioner of Inland Revenue v Quitsubdue Ltd [1999] 2 HKLRD 481
D74/91, IRBRD, vol 7, 16
Jones v Leeming [1930] AC 415
Commissioner of Taxes v British Australian Wool Realization Association [1931] AC 224
Beautiland Co Ltd v Commissioner of Inland Revenue [1991] 5 STC 467
Shui On Credit Co Ltd v Commissioner of Inland Revenue (2009) 12 HKCFAR 392
All Best Wishes Ltd v Commissioner of Inland Revenue (1992) 3 HKTC 750
Marson (Inspector of Taxes) v Morton [1986] 1 WLR 1343
Hong Kong Oxygen & Acetylene Co Ltd v CIR [2001] 1 HKLRD 489
Taylor v Good [1974] 1 WLR 556
Kelner v Baxter (1866) LR 2 C.P. 174
In Re Empress Engineering Co., (1880) 16 Ch. D. 125

Jonathan Chang instructed by Messrs Tony Kan & Co, for the Appellant.

Paul H M Leung, Counsel, instructed by Department of Justice, for the Commissioner of Inland Revenue.

Decision:

Introduction

1. This is an appeal brought by the Appellant against the Determination of the Deputy Commissioner of Inland Revenue dated 24 April 2015 ('Determination') whereby:

- (i) Profits Tax Assessment for the year of assessment 2007/08 under Charge Number X-XXXXXXXX-XX-X, dated 21 July 2010, showing

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Assessable Profits of \$1,174,003 with Tax Payable thereon of \$180,450 is confirmed; and

- (ii) Additional Profits Tax Assessment for the year of assessment 2008/09 under Charge Number X-XXXXXXXX-XX-X, dated 21 July 2010, showing Additional Assessable Profits of \$55,531,534 with Tax Payable thereon of \$9,162,703 is confirmed.

2. By the letter of Messrs Tony Kan & Co dated 22 May 2015 which was received by the Board of Review on the same date, the Appellant lodged a Notice of Appeal against the Determination together with a Statement of Grounds of Appeal.

3. The grounds of the appeal raised by the Appellant in the Notice of Appeal were as follows:

- (a) The Commissioner erred in determining that the gains from the disposal of the landed property acquired by the Taxpayer, namely, Address A ('Property B') was chargeable to profits tax, when in fact and in law the sale of Property B was a disposal of a capital asset, the proceeds of which should be excluded from profits tax.
- (b) The Commissioner further erred in determining that the Taxpayer was not entitled to commercial building allowance in respect of Property B.
- (c) The Commissioner erred in confirming the Profits Tax Assessment against the Taxpayer for the year of assessment 2007/08 under Charge Number X-XXXXXXXX-XX-X dated 21 July 2010 showing assessable profits of \$1,174,003 with tax payable thereon of \$180,450 when, for the reasons set out above and in the Statement of Grounds of Appeal, such an assessment is excessive and incorrect.
- (d) The Commissioner also erred in confirming the Additional Profits Tax Assessment against the Taxpayer for the year of assessment 2008/09 under Charge Number X-XXXXXXXX-XX-X dated 21 July 2010 showing additional assessable profits of \$55,531,534 with tax payable thereon of \$9,162,703 when, for the reasons set out above and in the Statement of Grounds of Appeal, such an assessment is excessive and incorrect.

4. The Statement of Grounds of Appeal dated 22 May 2015 further elaborated the grounds of appeal.

5. In essence, Company C ('the Appellant') has objected to the Profits Tax Assessment for the year of assessment 2007/08 and Additional Profits Tax Assessment for the year of assessment 2008/09 raised on it. The Appellant claims that the gain it derived from the sale of a property is capital in nature and should not be subject to Profits Tax.

Background Facts

6. In the absence of any contrary evidence adduced by the Appellant, we find the following facts referred to in paragraph 7 to paragraph 20 below upon which the Determination was arrived at as relevant facts of this appeal.

7. (a) The Appellant was incorporated as a private company in Hong Kong in October 2007.
- (b) In its Profits Tax Returns, the Appellant declared its principal activity as property investment.
- (c) At all relevant times, the Appellant's authorized and issued share capital were \$10,000 and \$1 respectively. Its sole shareholder was Company D, which had its address in Territory E.

(d) The directors of the Appellant were:

	<u>Date of appointment</u>
Mr F	06-11-2007
Ms G	01-09-2008
Ms G is the mother of Mr F	

(e) The Appellant closed its accounts on 31 March annually.

8. (a) At all relevant times, Mr F was also a director of Company H and Company J.
- (b) Company H is a private company incorporated in Hong Kong in January 1996. Its principal business activities were described as 'trading of raw plastic materials and investment holding'. At all relevant times, the shareholders of Company H were:

	<u>Address</u>	<u>No. of shares held</u>
Company K	in Hong Kong	31,800,000
Company L	in Country M	<u>21,533,334</u>
		<u>53,333,334</u>

(c) Company J is a private company incorporated in Hong Kong in December 1997. Its principal business activity was described as 'property investment'. As all relevant times, the shareholders of Company J were:

	<u>Address</u>	<u>No. of shares held</u>
Company D	In Territory E	99
Ms G	In Hong Kong	<u>1</u>

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Address No. of shares held
100

9. (a) By a provisional agreement for sale and purchase dated 21 August 2007, Company J agreed to purchase Property B (i.e. the properties located at Address A) and Address N ('Property P') at a total consideration of \$298,500,000. The agreement contained, among others, the following terms:

- (i) Both Property B and Property P were sold subject to existing tenancies as follows: (Term 9(d) of and Appendix 2 to the said agreement)

	<u>From</u>	<u>To</u>	<u>Monthly rent</u>
Property B			\$
- Room B1	01-05-2006	30-04-2009	59,360.00
- Room B2	15-07-2006	14-07-2008	47,376.00
- Rooms B3 and B4	vacant		
- Room B5 - B7	22-04-2006	21-04-2009	279,720.00
Property P	07-07-2006	07-06-2009	631,090.50

- (ii) Company J should be entitled to appoint its nominee to take up one or all of the floors and complete the transaction. (Clause 1 of Appendix 1 to the said agreement)
- (iii) At the request of Company J, the vendor should on the completion date serve a written notice to the existing tenant of Rooms B5 - B7 of Property B informing them that the tenancy would be terminated on 21 April 2009. (Clause 3 of Appendix 1 to the said agreement)
- (b) Company J and Company H entered into separate agreements for sale and purchase, both dated 12 November 2007, to purchase Property B and Property P at considerations of \$135,500,000 and \$163,000,000 respectively.
- (c) By a nomination also dated 12 November 2007, Company J nominated the Appellant to take up and execute the assignment of Property B from the vendor and the Appellant should become the legal and beneficial owner of Property B. In the nomination, it was stated that:
- (i) Initial and further deposits of \$13,550,000 paid to the vendor under the agreement for sale and purchase were in fact money belonging to and provided by the Appellant.

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- (ii) Property B was in fact agreed to be purchased by Company J as agent for and on behalf of the Appellant.
- (d) Property B was assigned to the Appellant on 14 November 2007.
- (e) By a provisional agreement for sale and purchase dated 29 November 2007, the Appellant agreed to sell Property B, subject to existing tenancies, to Company Q at a consideration of \$197,654,600.
- (f) By a tenancy agreement dated 20 December 2007, the Appellant leased Rooms B3 and B4 of Property B to Company R for a term of 9 months and 11 days, i.e. from 21 December 2007 to 30 September 2008, at monthly rent of \$144,240.
- (g) The Appellant's sale of Property B was completed on 28 August 2008.

10. Apart from the purchase and sale of Property B, the Appellant purchased the following two properties:

	<u>Location</u>	<u>Date of provisional agreement</u>	<u>Date of formal agreement</u>	<u>Date of assignment</u>	<u>Purchase price</u>
(a)	Address S ('Property T')	07-05-2008	-	30-06-2008	\$52,500,000
(b)	Address U ('Property V')	01-09-2008	17-09-2008	24-10-2008	\$169,500,000

11. The Appellant filed its Profits Tax returns for the years of assessment 2007/08 and 2008/09 together with audited financial statements for the period from 8 October 2007 (date of incorporation) to 31 March 2008 and year ended 31 March 2009 and proposed tax computations.

- (a) In its returns, the Appellant declared the following:

	<u>2007/08</u>	<u>2008/09</u>
Assessable profits/ (Adjusted loss)	<u>(\$841,054)</u>	<u>\$5,235,251</u>

- (b) In arriving at the above assessable profits and adjusted loss, the following adjustments were made:

	<u>2007/08</u>	<u>2008/09</u>
	\$	\$
<u>Exclusion from assessment</u>		

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	<u>2007/08</u>	<u>2008/09</u>
	\$	\$
(i) Gain on disposal of investment property, i.e. Property B	-	56,992,072
<u>Deduction</u>		
(ii) Commercial building allowance ('CBA')	2,015,057 ¹	2,960,000 ²
<u>Addition</u>		
(iii) Balancing charge	-	2,015,057 ¹

Notes :

1. In respect of Property B
2. In respect of Property T and Property V

- (c) The gain on disposal of Property B [Paragraph 11(b)(i)] was computed as follows:

	\$
Sales proceeds	197,654,600
Less: Legal cost	988,273
Agency commission paid	<u>31,500</u>
Net sale proceeds	196,634,827
<u>Less: Net book value¹</u>	<u>139,642,755</u>
Gain	<u><u>56,992,072</u></u>

Note 1:

Purchase price	135,500,000
Stamp duty	5,081,250
Legal fee	<u>128,500</u>

	\$
Total cost	140,709,750
<u>Less : Accumulated depreciation</u>	<u>1,066,995</u>
Net Book value	<u><u>139,642,755</u></u>

- (d) It was stated in Note 19 to the financial statements for the period ended 31 March 2008 that the directors decided to sell Property B, which had been held for long-term purpose, for the reason that the yield of the rental income of Property B was decreasing based on current market value.
- (e) In the balance sheets, all of the Appellant's properties were classified as investment properties under non-current assets.

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12. (a) On divers dates, the Assessor issued to the Appellant a statement of loss for the year of assessment 2007/08 and raised on the Appellant a Profits Tax Assessment for the year of assessment 2008/09 as follows :

<u>2007/08</u>	\$
Loss per return [Paragraph 11(a)]	<u>841,054</u>
<u>2008/09</u>	
Profits per return [Paragraph 11(a)]	5,235,251
<u>Less</u> : Loss brought forward and set-off	<u>841,054</u>
Net Assessable Profits	<u>4,394,197</u>

- (b) The Appellant did not object to the Profits Tax Assessment for the year of assessment 2008/09, which then became final and conclusive in terms of section 70 of the Inland Revenue Ordinance ('the Ordinance').

13. In reply to the Assessor's enquiries about the gain on disposal of Property B, the Appellant stated the following:

Purchase

- (a) The gross floor area of Property B was 13,822 square feet and its estimated age at the time of purchase was 19 years.
- (b) The original intention of purchasing Property B was long-term investment.
- (c) Mr F owned 51% of the shares of Company H. In July 2007, Company H decided to purchase an office for its own use and the budget was set at \$160,000,000. Mr F was responsible for looking for the appropriate property. The Target building was Building W.
- (d) In about early August 2007, Property P was offered for sale at a price not less than \$170,000,000. In the course of negotiation with the owner of Property P, it was known that such owner had other five whole floor offices in Building W for sale. One of them, with the lowest floor number and lowest selling price offered (i.e. \$145,000,000), was Property B.
- (e) The estate agent suggested to the Appellant that a better price could be obtained by making a combined offer to purchase two to three floor units.
- (f) It was proposed that Company H would offer to purchase Property B at \$135,500,000 and Mr F would offer to purchase Property P at \$163,000,000.

- (g) Mr F analyzed the yield of Property P and found that it was 4.65% per annum. He considered that such was a fair return and therefore agreed to purchase Property P as a long-term investment.
- (h) On 21 August 2007, Mr F entered into a provisional agreement to purchase both Property B and Property P at the price of \$298,500,000 for Company H and himself under the name of one of his companies, i.e. Company J. The two properties were purchased in the name of one company because of the estate agent's advice that the arrangement would increase the bargaining power of the buyers.
- (i) In October 2007, the overseas directors of Company H held a board meeting in Hong Kong and they took the opportunity to view the two properties. They were impressed by the superb sea view of Property P and liked to buy it instead of Property B. The board of directors of Company H then gave authority to increase the mandate of the purchase price from \$160,000,000 to \$163,000,000 and asked Mr F to swap the properties, i.e. Company H to purchase Property P and Mr F to purchase Property B.
- (j) Mr F analyzed the yield of Property B. According to the existing tenancies and assuming that the vacant units, namely Rooms B3 and B4, could be leased out at the then market rate of \$38 per square foot, the yield would be 4.7% per annum. This was considered to be an acceptable return. Although Mr F preferred Property P to Property B, in order to accommodate the wish of his business partners, he agreed to swap the properties, i.e. to purchase Property B instead of Property P.
- (k) Mr F made use of the Appellant to take up Property B. Therefore, a nomination was made by Company J in favour of the Appellant on 12 November 2007.

Disposal

- (l) The Appellant did not take any action to offer Property B for sale. In mid-October 2007, the Appellant received a number of unsolicited calls from an estate agent, Ms X of Company Y. She told Mr F that her client was willing to purchase Property B at the price of \$11,000 per square foot (comparing with the unit purchase price of Property B at \$9,803 per square foot). Mr F rejected the offer.
- (m) At the end of October 2007, Ms X informed Mr F that her potential purchaser was willing to increase the offer to \$12,000 per square foot. Sometime later, the offer was increased to \$13,000 per square foot. Again, Mr F rejected the offers.

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- (n) Subsequently, Ms X told Mr F that her client would offer \$14,300 per square foot and Mr F was a bit moved by the sincerity of that potential purchaser.
- (o) At the same time, an estate agent from Company Z recommended that a unit, i.e. Address AA ('Property AB'), with full sea view might be bought at \$14,500 per square foot.
- (p) Mr F then decided to sell Property B after considering the following :
 - (i) The yield of Property B based on the price offered by the potential purchaser and the existing rent became about 3% per annum, which was low. The proceeds got from sale could be used to invest in properties with a better yield.
 - (ii) The sale of Property B could entail the purchase of Property AB, which possessed a full sea view.
 - (iii) The view of Property B would be blocked by the new Building AC which was then under planning of construction.
 - (iv) The vacant units of Property B were difficult to lease out due to its irregular shape and odd partition and their untenable condition.
- (q) The purchaser finally offered the price of \$197,654,600 but requested a long completion period of 9 months. This was acceptable to Mr F as he all along intended a long-term investment and not a quick sale.
- (r) Mr F did not purchase Property AB because its owner kept on increasing the asking price.
- (s) In pursuance of his long-term investment plan, Mr F purchased Property T and Property V in 2008.

Finance

- (t) Mr F operated a very large business. He was able to finance the acquisition of Property B at ease. There was no need to make any formal feasibility study.
- (u) 70% of the purchase price, i.e. \$94,850,000, was financed by a mortgage loan borrowed from Bank AD for a term of 15 years and repayable by 180 monthly instalments.
- (v) During the period of ownership from December 2007 to August 2008,

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the amount of monthly instalments exceeded the rental income by about \$1 million. The shortfall was financed by Mr F by his own means.

Capital gains claim

(w) Mr F's intention to acquire Property B as a long-term investment was genuinely held, realistic and realizable. If he had intended a quick resale, he would have sub-sold Property B as a confirmor in late October or early November 2007 and avoided the payment of stamp duty in the sum of \$5,081,250 on 14 November 2007.

14. The Appellant provided, among others, copies of the following documents:

<u>Date</u>	<u>Document</u>
'12 November August 2007'*	Resolution of the sole director (i.e. Mr F) of the Appellant authorizing the purchase of Property B as a long-term investment at the price of \$135,500,000.
29-11-2007	Resolution of the sole director (i.e. Mr F) of the Appellant authorizing the disposal of Property B at a consideration of \$197,654,600. It was stated in the resolution that the sale decision was made after considering the factors as mentioned in Paragraph 13(p) above.

*According to the Appellant, the date was wrongly printed and it should be 12 November 2007.

15. Having considered the information available, the Assessor was of the view that Property B was a trading asset of the Appellant and the gain on disposal of it should be chargeable to Profits Tax. He raised on the Appellant the following Profits Tax Assessment for the year of assessment 2007/08 and Additional Profits Tax Assessment for the year of assessment 2008/09:

	<u>2007/08</u>	<u>2008/09</u>
	\$	\$
Profit / (Loss) per return [Paragraph 11(a)]	(841,054)	5,235,251
<u>Add:</u> CBA in respect of Property B withdrawn [Paragraph 11(b)(ii)]	2,015,057	-
Gain on disposal of Property B ¹	-	55,925,077
CBA in respect of Property T and Property V overclaimed ²	-	<u>780,460</u>
	1,174,003	61,940,788
<u>Less:</u> Balancing charge in respect of Property B not to be assessed [Paragraph 11(b)(iii)]	-	<u>2,015,057</u>
Assessable Profits	<u>1,174,003</u>	59,925,731

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	<u>2007/08</u>	<u>2008/09</u>
	\$	\$
<u>Less:</u> Amount previously assessed [Paragraph 12(a)]		<u>4,394,197</u>
Additional Assessable Profits		<u>55,531,534</u>
Tax Payable thereon	<u>180,450</u>	<u>9,162,703</u>
Notes :		
		\$
1. Gain on disposal per tax computation [Paragraph 11(b)(i)]		56,992,072
<u>Less:</u> Accumulated depreciation [Paragraph 11(c)]		<u>1,066,995</u>
Gain on disposal of Property B		<u>55,925,077</u>
2. The method of calculation of the CBA was agreed by the Appellant subsequent to the filing of Profits Tax return.		

16. Company AE ('the Representative'), on behalf of the Appellant, objected to the above assessments on the grounds that Property B was acquired for long-term investment purposes and the gain on its disposal should be capital in nature and not taxable. The Representative put forward the following contentions:

- (a) Property B was acquired with existing tenancy (except Rooms B3 and B4) in August 2007. Although no formal feasibility study was carried out, the Appellant purchased Property B on the basis that it could be expected to produce a satisfactory rental income yield of approximately 4.7% per annum. Rooms B3 and B4 were let out in December 2007 and the actual rental income yield met the Appellant's estimation. The rental details and the rental yield were as follows:

<u>Unit</u>	<u>Monthly rent</u>	<u>Tenancy</u>
	\$	
B1	59,360	Existing
B2	47,378	Existing
B3 and B4	144,240	New (at \$40 per square foot)
B5 – B7	<u>279,720</u>	Existing
	<u>530,698</u>	
Rental yield	<u>4.7%</u>	[\$530,698 x 12 / \$135,500,000 (purchase price of Property B)]

- (b) Although the monthly rental income received during the period from December 2007 to August 2008 was slightly less than the Appellant's monthly interest payment and loan repayment, the Appellant considered that Property B would generate net cash inflow after the leasing of Rooms B3 and B4 and the expiry of the existing tenancy

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agreements in early 2009. The Appellant originally intended to increase the monthly rent when renewing the tenancy agreements in view of the trend of the property rental market and the good location of Property B. The monthly rental income generated would be higher than the monthly repayment in the long run. Therefore, the Appellant considered that Property B was a suitable property for long-term investment purposes.

- (c) Property B was shown as a fixed asset and the 15-year bank loan was shown as a long-term liability in the Appellant's audited accounts. This demonstrated that the Appellant intended to hold Property B as a long-term investment for deriving rental income.
- (d) During the period of ownership of the Appellant, Property B was intended to be used and was used for deriving rental income.
- (e) Based on the sale price of \$197,654,600 (i.e. \$14,300 per square foot), the yield of Property B became about 3% per annum. The Appellant considered that there would be a lot of investment opportunities in the market which could generate a yield of about 5% per annum. As a result, the Appellant decided to sell Property B in late November 2007 so as to switch the investment to Property AB.
- (f) The proceeds from sale of Property B were utilized to acquire Property V and Property T. Property V was purchased at \$14,000 per square foot and it had a much more open view than Property B. It was let to Company H for use as its office at a monthly rent of \$726,480. The rental yield was 5.14% ($\$726,480 \times 12 / \$169,500,000$, i.e. purchase price of Property V), which was much higher than that of Property B.
- (g) It was the Appellant's strategy to acquire good quality properties for long-term investment purposes. Property B was sold to facilitate the purchase of a more superior long-term investment property (i.e. Property AB under the Appellant's original plan and finally Property V). The Appellant had never changed its intention in acquiring good quality properties. The disposal of Property B represented as investment decision to replace the existing property with a higher quality property which was considered to have a better long-term potential growth for investment purposes. This was part of a process of upgrading the quality of the Appellant's long-term property investment portfolio.

17. The Assessor maintained his view that Property B was trading asset of the Appellant and invited the Appellant to consider withdrawing the objections. The Appellant refused to withdraw the objections and the Representative put forth the following contentions:

Property B

- (a) Both Company J and the Appellant were wholly owned by Mr F. There was no doubt that Mr F made a decision to buy both Property B and Property P on 21 August 2007, the date of the provisional agreement to purchase the properties.
- (b) In today's fast-changing business world, rational investor had to evaluate / review his investment decision and portfolio based on the market value of his investment. Using the market value to compute the rental yield was a fair and common approach for property investor to assess if a fair long-term return rate was achieved or not. If the effective rental yield, i.e. annual rental income / market value of the property, was higher than the investor's benchmark, the investor would keep the property. Otherwise, the investor had to consider whether he should sell out the property. In a volatile property market, investor had to monitor the market value of the property portfolio closely in order to safeguard his investment.
- (c) The Appellant was aware that the construction plan of Site AW would affect the view of Property B. However, it was originally intended on 21 August 2007 that Company H would purchase Property B as its offices whereas Company J (subsequently changed to the Appellant) would purchase Property P as a long-term investment. Therefore, the potential impact of Site AW was not considered by Company J or the Appellant at the time of purchase.
- (d) Although the Appellant had not formally appointed property agents for acquisition of property, the Appellant did receive numerous unsolicited offers from different property agents by email, fax and phone during the period.
- (e) It was the Appellant's intention to utilize the funds realized from the sale of Property B to acquire a better property in late 2007. However, the acquisition was not successful in 2007. The Appellant spent additional time and effort in locating another superior investment property in early 2008.
- (f) The Appellant adopted a selective and prudent strategy for its property investment in Hong Kong. Only high quality property with good long-term potential growth for investment would be held and kept by the Appellant. As such, the Appellant spent a few months to review and screen the numerous offers provided by the property agents. After due and careful consideration, the Appellant finally decided to acquire Property T and Property V in May and September 2008 respectively. Both of them provided steady and attractive

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rental income to the Appellant. It was unquestionable that these two properties were better than Property B.

- (g) Room B3 was let to Company R, a business acquaintance of Company Q, the buyer of Property B. Company R was urgently in need of an office accommodation. The lease was due to expire on 30 September 2008, which was set to match the expected completion date of purchase of Property B by Company Q, i.e. 28 August 2008.
- (h) Given Room B3's conditions, if Company R was not an acquaintance of Company Q, it would not rent Room B3 from the Appellant. The Appellant did have difficulties in renting out Room B3 in the market during the period of ownership.
- (i) If Property B was acquired by the Appellant as a trading asset for resale purpose, the Appellant would not sell Property B on 29 November 2007 at \$14,300 per square foot as it should be able to be sold at a higher price based on the market trend. Information from the market showed that a property at Address AF was sold at \$19,341 per square foot on 23 November 2007, and a property at Address AG was sold at \$16,800 per square foot on 19 December 2007. Copies of the transaction records of Tower 2 of Building W for the period from November to December 2007 are at Appendix F of the Determination.
- (j) Based on the purchase price, the rental yield of Property V and Property T at the time of acquisition were 5.14% and 4.57% respectively. If based on the current market price, the revised rental yield of Property V and Property T were around 4% and 3.75% respectively. Both properties maintained attractive rental yields as compared with that of Property B (being 3% at the time of disposal) and other investment properties available in the market.
- (k) The disposal of Property B only represented a commercial decision for the Appellant to eliminate less superior property from its investment portfolio. For good and desirable property like Property V and Property T, the Appellant had held them for nearly two years and would continue to hold them as long-term investments.
- (l) The Appellant accepted a nine-month completion period when selling Property B because
 - (i) A long completion period would not impact negatively on its ability to find a suitable replacement property, and
 - (ii) The purchaser agreed to rent Rooms B3 and B4 of Property B, which provided additional rental income to the Appellant during the ownership period.

Property AB

- (m) It was never the intention of the Appellant to sell Property B initially. It was probably a culmination of events and specific information provided to the Appellant by Company Y and Company Z that led the Appellant to the conclusion that its long-term needs would be better served by securing a different property, which was Property AB.
- (n) However, by the time the Appellant approached the seller of Property AB, the seller showed no interest as Property AB had been sold and the time was too close to the completion date. The Appellant continued to search until it found Property V, which met its investment criteria.

Property V

- (o) Property V was let to Company H from 25 October 2008 for a term of three years. Company H agreed to rent Property V at \$60 per square foot per month before the Appellant's signing of the provisional agreement for acquisition of Property V.

Property P

- (p) Property P was acquired and managed by Company H and was leased to Company AH up to July 2009. Due to the financial crisis of 2008/09, Company AH decided to relocate to smaller and cheaper premises. Since then, Company H was not able to find a suitable tenant. Property P was left vacant and subsequently sold in November 2010.

18. In response to the Assessor's further enquiries, the Representative stated the following:

Company H and Property P

- (a) Company H was a joint venture company held by Mr F and Company L, a business partner in Country M. Company L was a wholly owned subsidiary of Company AJ, a company listed on City AK and City AL Stock Exchange, while Mr F was the major shareholder of Company K. Directors were appointed from both Company AJ and Company K.
- (b) In 2007, Company H's office was located at Address AM, with gross floor area of 9,838 square feet. It was rented from a related company and had been used for more than ten years.

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- (c) Company H originally intended to acquire Property P, with gross floor area of 15,331 square feet, as its office in Hong Kong. It submitted an offer in July 2007 to purchase Property P through Mr AN of Company Z. The offer was rejected as it was lower than the vendor's asking price.
- (d) Subsequently, Mr AN advised Company H that the vendor also held other five floors, including Property B, and the vendor had intention to sell these floors. Therefore, Company H considered acquiring the Property B at a lower price as an alternative.
- (e) Meanwhile, Mr F was approached to acquire a floor in Building W personally as a long-term investment by bundling a deal together for two properties, i.e. Property B and Property P, in order to reduce the overall purchase price for both properties.
- (f) Mr F personally considered that both properties were good properties for long-term investment. He had no objection to let Company H pick its preferred property first and acquire the remaining floor through his own property holding company.
- (g) Under point 3 of Appendix 1 of the provisional agreement for sale and purchase dated 21 August 2007, the vendor was required to serve a written notice to the exiting tenant of Rooms B5-B7 informing it that the tenancy must be terminated on 21 April 2009. It clearly indicated that Company H intended to use Property B as its office.
- (h) After the directors of Company L visited Hong Kong and inspected both Property B and Property P in October 2007, they decided to acquire Property P instead of Property B.
- (i) It was Company H's original plan to use Property P as its office in 2009. However, Company H's business expansion was faster than originally expected. Coincidentally, Mr F, through the Appellant, acquired Property V, which was under vacant possession, in September 2008. To cope with the business expansion in 2008, Company H resolved to rent Property V, with gross floor area of 12,108 square feet, as a fair market rate of a term of 3 years.

Property AB and Property B

- (j) Mr F was one of the owners of the properties in Building W. Company Z kept contacting Mr F regularly to provide information about Building W.
- (k) The Vendor of Property B and Property P had a total of six floors for sale, one of them being Property AB. Therefore, Mr F realized that

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Property AB was offered for sale.

- (l) The Appellant could not retrieve the advertisements / offers provided by other estate agents in 2007. However, it could retrieve a leaflet issued by Company Z regarding the sale of Property B in 2007.
- (m) Mr F offered to acquire Property AB (at a price of \$150 million) under the name of Company J through Mr AN on 22 August 2007. The relevant draft provisional agreement for purchase of Property AB showed that Company Z was appointed as Company J's agent and Mr AN received a cheque of \$5 million from Company J as the deposit for acquisition of Property AB.
- (n) After the offer for Property AB made on 22 August 2007 was rejected by the vendor, Mr F sent another offer to the vendor on 5 October 2007, which increased the purchase price from \$150 million to \$162 million.
- (o) The offer was rejected by the vendor again. The vendor executed a provisional agreement for sale and purchase with another buyer, Company AP, on 15 October 2007, at a price of \$165 million.
- (p) Although Property AB was sold, the Appellant understood from Mr AN that Company AP had an intention to sub-sell Property AB as a confirmor at a price around \$196.98 million, i.e. \$14,000 per square foot. The Appellant considered this price too high and did not offer to purchase Property AB from Company AP.
- (q) As the buyer introduced by Ms X offered a price of \$14,300 per square foot for Property B and that was close to the asking price for Property AB, the Appellant considered it a good opportunity to upgrade its investment portfolio by swapping Property B for Property AB.
- (r) Therefore, the Appellant confirmed to sell Property B on 29 November 2007 and contacted Mr AN on the same date to secure the purchase of Property AB.
- (s) Company AP rejected the offer from the Appellant on about 29 November 2007 evening or 30 November 2007 morning.
- (t) As the Completion date for Company AP's acquisition of Property AB was 8 December 2007, there were only six working days to complete the transaction. Company AP considered that there was not enough time and refused to sell Property AB to the Appellant in the capacity of a confirmor.

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- (u) After the completion date, Company AP further increased the selling price of Property AB and the Appellant gave up the purchase.
- (v) It was clear that the Appellant had an intention to swap Property B for Property AB and did approach the sellers many times but in vain.
- (w) It was never the intention of the Appellant to acquire Property B for sale. The Appellant decided to sell Property B simply because there was an opportunity for the Appellant to upgrade its property to Property AB without incurring substantial additional cost. Although Company AP finally rejected the Appellant's offer, which was unexpected when the Appellant decided to sell Property B, it did not indicate that the Appellant had a trading intention when acquiring Property B.
- (x) It was not uncommon that a prudent property investor would decide to sell out his property first before acquiring a better replacement property.
- (y) Although the Appellant had the financial ability to hold both Property B and Property AB at the same time, it did not imply that it had to take the risk for acquiring Property AB at a higher price before Property B was sold on 29 November 2007.

19. The Representative, furnished, among others, copies of the following further documents:

<u>Date</u>	<u>Document</u>	<u>Reference</u>
Undated	Advertisement sheet issued by Company Z for sale of Property B	Paragraph 18(l)
22-08-2007	Draft provisional agreement for sale and purchase showing Company J as the purchaser of Property AB and purchase price of \$150 million, together with Company J's cheque issue instruction and acknowledgment by Mr AN in respect of \$5 million as initial deposit	Paragraph 18(m)
05-10-2007	Draft provisional agreement for sale and purchase showing Company J as the purchaser of Property AB, purchase price of \$162 million and total monthly rent of \$423,343.50 in respect of the existing tenancies, together with a copy of a cheque issued by Company J in the amount of \$5 million as initial deposit	Paragraph 18(n)

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<u>Date</u>	<u>Document</u>	<u>Reference</u>
15-10-2007	provisional agreement for sale and purchase of Property AB by Company AP at a price of \$165 million (with fax header showing that the agreement was transmitted at 19:02 on 29-11-2007)	Paragraph 18(o) and (r)

20. In reply to the enquiries of the Assessor, Company AQ, on behalf of Company Q, provided the following information in relation to the purchase of Property B from the Appellant:

- (a) Ms X of Company Y approached Company Q on her own initiative in November 2007.
- (b) Property B was intended to be acquired for long-term investment purpose. Company Q did not particularly choose Property B. It was selected because it was available in the market by that time and the various conditions met the investment strategy of Company Q.
- (c) As the investment involved a significant sum and Company Q required adequate time to structure the investment and its finance, it requested for a longer completion period.

Authorities submitted by the parties

21. The Appellant relies on the following authorities:

- (a) Inland Revenue Ordinance (Chapter 112): Sections 14, 33A, 40 and 68
- (b) Church Body of the Hong Kong Sheng Kung Hui & Anor v CIR, FACV 16/2015 (unreported, 4 February 2016)
- (c) Lee Yee Shing v CIR (2008) 11 HKCFAR 6
- (d) Simmons v IRC [1980] 1 WLR 1196
- (e) Wing On Cheong Investment Co Ltd v CIR (1987) 3 HKTC 1
- (f) Real Estate Investments (NT) Ltd v CIR [2007] 1 HKLRD 198
- (g) Real Estate Investments (NT) Ltd v CIR (2008) 11 HKCFAR 433
- (h) CIR v Reinhold (1953) 34 TC 389
- (i) CIR v Quitsubdue Ltd [1999] 2 HKLRD 481

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- (j) D74/91, IRBRD, vol 7, 16
- (k) Jones v Leeming [1930] AC 415
- (l) Commissioner of Taxes v British Australian Wool Realization Association [1931] AC 224
- (m) Beutiland Co Ltd v CIR [1991] 5 STC 467
- (n) Shui On Credit Co Ltd v CIR (2009) 12 HKCFAR 392

22. The Respondent, in turn, relies on the following authorities:

- (a) All Best Wishes Ltd v CIR (1992) 3 HKTC 750
- (b) Marson (Inspector of Taxes) v Morton [1986] 1 WLR 1343
- (c) Hong Kong Oxygen & Acetylene Co Ltd v CIR [2001] 1 HKLRD 489
- (d) Taylor v Good [1974] 1 WLR 556
- (e) Kelner v Baxter (1866) LR 2 C.P. 174
- (f) In Re Empress Engineering Co., (1880) 16 Ch. D. 125

Relevant Provisions of the Inland Revenue Ordinance, Chapter 112 ('Ordinance')

23. The following provisions of the Ordinance are relevant and applicable in this appeal:

- (a) Section 2(1) defines 'trade' to include '*every trade and manufacture, and every adventure and concern in the nature of trade*'.
- (b) Section 14(1) provides:

'Subject to the provisions of this Ordinance, profits tax shall be charged for each year of assessment at the standard rate 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'.
- (c) Section 68(4) provides that '*The onus of proving that the assessment appealed against is excessive or incorrect shall be on the Appellant*'.

(d) 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 \$25,000.

Relevant Authorities on Trade, Intention and Manner to ascertain the Intention

24. Trading requires an intention to trade. Lord Wilberforce stated in Simmons¹ that *‘normally the question to be asked is whether the intention existed at the time of acquisition of the asset’*. In Simmons, his Lordship set out the principle at page 1199 as follows:

‘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] AC 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)

25. In Church Body of The Hong Kong Sheng Kung Hui², Tang PJ said *‘in determining whether an activity amounts to trading, the fact-finding tribunal must*

¹ Simmons v IRC [1980] 1 WLR 1196

² Church Body of the Hong Kong Sheng Kung Hui & Another v CIR, FACV 16/2015 (unreported, 4 February 2016)

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consider all the circumstances involved in the activity. It will have to make a ‘value judgment’ as to whether this constitutes trading and whether the requisite intention to trade can be inferred. Regardless of what is claimed to be the intention subjectively, the question falls to be determined objectively having regard to all the surrounding circumstances’ (at paragraph 50).

26. In Lee Yee Shing³, Bokhary and Chan PJJ emphasized in 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 said in paragraph 56 that *‘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.’* His Lordship also pointed out in paragraph 59 that *‘the intention to trade to which Lord Wilberforce referred is not subjective but objective’*. It is inferred from all the circumstances of the case to see whether the ‘badges of trade’ that indicate an intention to trade, or perhaps more correctly, the carrying on of a trade are present. Specifically, they are whether the taxpayer:

- (a) has frequently engaged in similar transactions
- (b) has held the asset or commodity for a lengthy period
- (c) has acquired an asset or commodity that is normally the subject of trading rather than investment
- (d) has bought large quantities or numbers of the commodity or asset
- (e) 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
- (f) has sought to add re-sale value to the asset by additions or repair
- (g) 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
- (h) has conceded an actual intention to resell at a profit when the asset or commodity was acquired
- (i) has purchased the asset or commodity for personal use or pleasure or for income.

27. The Taxpayer’s own declaration of intention is inconclusive and has to be tested against all objective facts and circumstances. In All Best Wishes⁴ Mortimer J (as he

³ Lee Yee Shing v CIR (2008) 11 HKCFAR 6

⁴ All Best Wishes Ltd v CIR (1992) 3 HKTC 750

then was) said at page 771

‘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.’

28. In Marson⁵, Sir Nicolas Browne-Wilkinson V-C said at H, page 1347 that ‘a single, one-off transaction can be an adventure in the nature of trade’ and continued at B, page 1348 that ‘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.’ Nonetheless, the list of factors was in no sense comprehensive, nor was any one of those decisive in all cases. They would provide common sense guidance to an appropriate conclusion. The matters which are apparently treated as a badge of trade referred to by Sir Nicolas Browne-Wilkinson V-C are summarized as follows:

- (a) That the transaction was a one-off transaction although a one-off transaction is in law capable of being an adventure in the nature of trade.
- (b) Is the transaction in some way related to the trade which the taxpayer otherwise carries on?

⁵ Marson (Inspector of Taxes) v Morton [1986] 1 WLR 1343

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- (c) 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 realization?
- (d) Was the transaction carried through in a way typical of the trade in a commodity of that nature?
- (e) What was the source of finance of the transaction?
- (f) 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?
- (g) Was the item purchased resold in one lot as it was bought, or was it broken down into saleable lots?
- (h) What were the purchasers' intentions as to resale at the time of purchase?
- (i) Did the item purchased either provide enjoyment for the purchaser or pride of possession or produce income pending resale?

29. His Lordship at page 1349C emphasized that the matter he has mentioned are not a comprehensive list and no single item is in any way decisive. In his words, *'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?'*

30. In Real Estate Investment⁶, Bokhary and Chan PJJ said the accounting treatment gives some evidence, but the onus of proof that the assessment is excessive or incorrect does not shift from the Taxpayer to the Respondent:

'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 assessment 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

⁶ Real Estate Investment (NT) Ltd v CIR (2008) 11 HKCFAR 433

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 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.'*

The Evidence of Mr F

31. The Appellant called two witnesses, Mr F, its director and Ms X to give evidence at the hearing. Ms X left Company Y since 2014.

32. Mr F signed and filed a witness statement dated 27 April 2016. He confirmed with the Board that the contents of the witness statement were true and correct. Accordingly the same stood as evidence in chief of Mr F and he stood before the Board for cross-examination by counsel for the Respondent.

33. The Board has carefully considered the contents of Mr F's witness statement and the documents annexed therewith as well as his oral testimony.

34. Mr F's witness statement covered most, if not all, the undisputed facts found by the Board as set out in paragraph 7 to paragraph 20 above. In addition to the undisputed facts, his witness statement also covered the following:

- (a) All along his intention and philosophy was for his corporate vehicles, including Company J and the Appellant to hold properties in his portfolio of investment properties for long-term investment, and such intention and philosophy has remained unchanged all through these years.
- (b) Mr F, for and on behalf of Company J entered into a provisional agreement and a formal agreement for Floor AS and Floor AT of Tower AU of Building W (respectively Property B and Property P) with the vendor on 21 August 2007 and 12 November 2007 respectively on the understanding that Company H would take up Property B as a nominee of Company J in due course.
- (c) In October 2007, Company H had a chance of inspecting both Property B and Property P. They were impressed by the superb sea view of Property P and were prepared to increase the mandate of the purchase price to \$163 million and swap for Property P. He considered that Property B at that time was a good long term

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investment. Although no formal feasibility study was carried out, basing on the monthly rental of the existing tenancies at the time, and the expected market rental of the then vacant Room B3 - Room B4 at about \$40 per square foot, he expected that Property B could produce a reasonable yield at about 4.6% per annum. So he agreed with Company H to swap Property P with Property B.

- (d) He decided to use the Appellant (which was a new company incorporated on 8 October 2007) to take up Property B instead of making use of his other companies (including Company J) mainly because of two reasons:
- (1) For better management, internal administration, and risk diversification.
 - (2) To allow for some future flexibility as regards his future estate planning.
- (e) After signing of the provisional agreement of 21 August 2007:
- (1) He never held out or marketed to sell Property B. He intended to hold Property B for long-term investment and realize his return through collecting rental. For the same reason, he turned down all unsolicited enquiries for sale of Property B from estate agents.
 - (2) The acquisition of Property B was financed up to 70% of its purchase price by a mortgage taken out with Bank AD repayable by 180 instalments. The shortfall in rental income towards mortgage repayment was financed by himself by his own means at ease with his huge business and large investment portfolio.
 - (3) Rooms B3 and B4 were not easy to rent out because the shape was irregular and had some odd internal partition and it did not have a good view as it faced another building.
 - (4) He had caused the Appellant to complete the purchase of Property B and had duly paid stamp duty in excess of \$5 million. If he had treated Property B as trading stock as opposed to long-term capital investment, he would certainly have fetched out for a quick sale as confirmor to obtain profit, and would not have completed the transaction to save stamp duty.
 - (5) In the Appellant's audited reports and financial statements, Property B was recorded as 'Investment Properties' under 'Non-Current Assets', which was consistent with his intention

of acquiring it as capital asset for investment.

- (f) Mr F also wanted to acquire Address AA ('Property AB') from the same vendor. His first offer of \$150 million made on 22 August 2007 and his second offer of \$162 million made on 5 October 2007 to acquire Property AB were respectively rejected by the vendor. He gave the third offer in the sum of HK\$163 million on 12 October 2007 which was again declined by the vendor. Based on \$163 million, on a fully let basis, with the then vacant Rooms AB1 and AB2 with full sea view being leased out at the expected rental of about \$50 per square foot, the expected yield would be about 4.64%. Property AB was sold by the vendor to Company AP on 15 October 2007 at HK\$165 million.
- (g) In or around mid-November 2007, Mr AN of Company Z informed him that Company AP decided to sell Property AB at HK\$14,000 per square foot which was a final firm offer, with the condition of a short completion period to meet the original completion date under the provisional agreement dated 15 October 2007 it signed with the vendor. At that time Mr F consider the asking price was too high and had no interest to meet this price even though he did like Property AB and he would have no problem accommodating the short completion period.
- (h) In or about mid-October, Ms X approached Mr F several times and told him she had a client who was willing to offer \$11,000 per square foot to purchase Property B (which he acquired at \$9,803.21 per square foot). Mr F rejected the offer. The offer was improved to \$11,000 per square foot and \$12,000 square foot successively but again was rejected by Mr F. Eventually, in mid-November 2007, Ms X's client (later known as Company Q) further increased the offer to \$14,300 per square foot (in excess of \$197 million) which was by any scale a surprisingly high price and very attractive but Company Q asked for a long completion period in 9 months on or before 28 August 2008. Company Q's business associate (later known as 'Company R') may rent the then vacant Room B3 – Room B4 for its own use at not less than \$38 per square foot per month.
- (i) Mr F distinctly recalled that Ms X's offer at \$14,300 per square foot for Property B came two or three days after Mr AN had told him about Ms AV's final, firm offer for Property AB at \$14,000 per square foot. He saw the offer from Ms X's client as the perfect opportunity for him to revive his interest in the purchase of Property AB:
 - (1) Property AB would have a better rental yield than Property B based on their then market value, respectively at 2.58% and

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2.35% on the then status of the two properties (namely each with vacant units) and respectively at 3.84% and 3.16% on fully let basis.

- (2) The yield from Property B had dropped to 2.35% (or 3.16% on a fully let basis) as compared to his original estimate of 4.6% at the time of his acquisition of the property.
 - (3) The sale proceeds of Property B could be immediately utilized for the purchase of Property AB which has a full sea view on a higher floor level and a better rental yield. In essence, if he could swap Property B with Property AB successfully, he would get a much better property in return and with a better rental yield, at practically no additional costs.
 - (4) The swap also provided a good solution to the vacant Room B3 – Room B4 which had been difficult to rent out and he would be able to receive additional rental income pending completion.
 - (5) He also took into account the fact that the view of Property B would be blocked by the new Building AC which was then under planning of construction, and the future rental price would be adversely affected.
- (j) The swap would upgrade his investment property portfolio and increase the rental yield. If the offer from Company Q and the intended sub-sale by Company AP were not co-existent at the material time, he would not have sold Property B. He had ample financial resources to accommodate both conditions at the same time to complete the purchase of Property AB (within a short period of time) without having to wait until completion of the sale of Property B (in 9-month period).
 - (k) Immediately after he signed the provisional agreement to sell Property B on 29 November 2007, he instructed Mr AN to accept Company AP's asking price for the sub-sale of Property AB and asked him to proceed with finalizing the deal on his behalf. However, the negotiation with Company AP fell through due to insufficient time to complete the deal because there were only 6 business days before Company AP was contractually bound to complete its purchase from the vendor on 8 December 2007.
 - (l) His decision to sell Property B was prompted by the opportunity to swap for Property AB rather than any intention to treat Property B as a trading stock and resell it for a quick profit after its acquisition. Otherwise, he could have kept on to Property B and fetched out for a

higher price based on the market trend.

- (m) Mr F also gave an account of the subsequent purchase of two replacement properties, namely, Address S ('Property T') and Address U ('Property V') upon his failure to acquire Property AB. The profits from the sale of Property B were retained with the Appellant and reinvested in its business, namely the acquisition of Property T and Property V. In the Audited Reports and Financial Statements of the Appellant, Property T and Property V were booked as 'Investment Properties' under 'Non-Current Assets'. It is thus evident that his intention for acquisition of landed properties through various corporate vehicles has all along been for long-term investment and he always treats the properties as capital asset, and not trading stock.
- (n) Mr AN had left Company Z. Mr F had approached him last year and invited him to give a witness statement. Mr AN said to Mr F that he had left Company Z on bad terms and he had been in financial difficulty since then, and he asked to be paid for giving a witness statement. Mr F declined his request which was plainly improper. He had also abandoned the idea of inviting Mr AN to be his witness in this appeal.

35. In the course of giving evidence, Mr F confirmed that he would buy a property if the same could give a rental yield of 4.5%. He seldom purchased property with a rental yield lower than 4%. He had employed 3 part-time staff to do the market research and to manage the rental matter.

36. Upon cross-examination, Mr F denied that he had knowledge that the property market in relation to Building W was very active in or around later part of 2007. Upon production of the news reporting about the transactions of Building W made around October and November 2007, he told the Board that he then knew it was so because he relied on his staff to give him information although two property agents, Mr AN and Ms X could contact him direct and gave him information. Upon further questioning by counsel for the Respondent with reference to the letter dated 28 May 2013 sent by Company AE, the Appellant's tax representative to the IRD⁷, he denied that the property agents gave him the market information relating to Building W on a daily basis or on a weekly basis. Probably the property agents contacted his staff daily which he did not know. He just let the staff communicate with Company AE and he did not study that letter in detail. He was further referred to another letter from Company AE to IRD and dated 10 January 2011⁸.

⁷ Page 307 of the Respondent's Bundle of Documents in which it wrote 'As advised in our letter of 21 October 2010. [Company C] receives offers from different property agents daily...'

⁸ Page 246 of the Respondent's Bundle of Documents in which it wrote 'As a property investor, many agents are constantly providing updates on the actual leasing rates and property values, which in turn assists the Company.....'

He gave an explanation that he did not care about daily matter.

37. He was further referred to another letter from Company AE to IRD and dated 21 October 2010⁹, only then he agreed that in or about October 2007 and November 2007, he received a number of enquiries and information relating to the market of Building W from property agents. He agreed that by then he was very clear about the property market of Building W and the market was heated up.

38. He said his method of investing in landed property was quite different from the Hong Kong people because his decision was made on the basis of rental yield while the others would consider whether the market conditions were right for purchase.

39. Mr F told the Board that it was the intention of Company H to acquire one floor of Building W for self-use. Before the swap made in October 2007, it was Company H to acquire Property B. Upon questioning, Mr F confirmed that he took no steps to find tenants for the vacant units of Property B until after the swap.

40. When asked whether he would sell the property if the price soared up in a short period after he acquired the same, Mr F replied that he would probably not sell the property and explained that although the rental yield might not rise so fast, eventually, the rental yield would also rise so as to give the same return.

41. Mr F agreed with counsel for the Respondent that he knew the value of Property B was about \$13,000 per square foot at the time the Appellant agreed to buy Property B. However he decided to keep this as a long term investment and he had no intention to sell or to sell it for higher price in the future. He also agreed with Respondent's Counsel that based on this price, the return would substantially drop below 4.5%.

42. In the course of giving evidence Mr F stressed many times that he would not sell Property B if he had no opportunity to buy or swap Property AB. The swap was one of the main reasons to sell Property B.

43. Mr F was referred to the audited account of the Appellant for the year ended 31 March 2008 in which it is stated 'On 28 August 2008, the Appellant completed the sales of the investment properties at a total purchase consideration of HK\$197,654,600 with a gain on disposal of HK\$59,146,964. The directors decided to sell the investment property which held for long term purposes for the reason that the yield of the rental income of the property is decreasing based on current market value.' When repeatedly questioned about why he did not put the main reason, the swap from Property B to Property AB, in the audited accounts, he offered no explanation. At last he explained that the report was drafted by the professional and the contents of the audited account were

⁹ Page 225 of the Respondent's Bundle of Documents in which it wrote 'However, our client received various unsolicited offers from a property agent persuading our client to sell [Property B] in October and November 2007.'

also correct. He confirmed that the said audited account was signed by him and that the signing by him meant that the contents were confirmed by him as correct. However, he offered no satisfactory answer as to why he did not put the main reason in the audited report.

44. Apart from these two reasons, he got the impression that the rents from the units of Floor AS might not rise too much in the future because of the odd partition of the units and the view of Property B would be blocked by Site AW. He told the Board that at the time of signing the provisional agreement for Property B and Property AB, he had no knowledge of the erection of Building AC. He knew this fact after signing the agreement. However, he was confronted with the letter from Company AE to IRD dated 21 October 2010¹⁰, he answered that he did not know why Company AE would write in that way.

The Evidence of Ms X

45. Ms X also signed and filed a witness statement dated 27 April 2016. Upon her confirmation that the contents thereof were true and correct, it was tendered as evidence in chief which, together with the documents exhibited, have been carefully considered by the Board.

46. In essence, she understood from market that Mr F had purchased two floors of Building W at below \$10,000 per square foot. Although she knew that Mr F did not have the appetite to do quick sale as other property speculators did, she nevertheless asked him whether he would consider the sale for both floors, or at least one floor. Upon instruction from one of her clients to make enquiries with Mr F, Mr F replied firmly that the 2 floors were for self-use and for rental income respectively, and both were for long term investment. He had no intention for a quick sale. In or about end-October 2007, she offered \$11,000 per square foot to Mr F for acquisition of Property B, Mr F stated that Property B was for rental income and he rejected the offer.

47. She had instructions to increase the offer to \$12,000 per square foot and if not successful, then to increase to \$13,000 per square foot, but Mr F repeatedly rejected both of the offers.

48. In or around mid-November 2007, at the instructions of the potential purchaser, she made a revised offer to Mr F to acquire Property B for the sum of \$14,300 per square foot. When the offer was conveyed to Mr F, he was a bit moved by the sincerity of the potential purchaser and required Ms X to confirm the terms of sale including the period of completion. He raised the concern that Rooms B3-B4 was vacant at that time which was difficult to let because of irregular shape.

49. The potential purchaser would require completion for Property B in 9

¹⁰ Page 226 of Respondent's Bundle of Documents in which it wrote 'our client was aware of the construction plan of Site AW would affect the view of [Property B] at the time of acquiring [Property B] and [Property P].'

months' time because it was a difficult period for corporate lending by the banks. She discussed the terms of sale from the potential purchaser with Mr F. He appeared to be pleased with the offer and negotiation went on well. Finally an agreement was reached with the potential purchaser and Mr F and they signed a provisional agreement for sale and purchase on 29 November 2007. Mr F told her at the time that he sold Property B because he had an opportunity to swap it with Property AB as he put forward an acceptance of the offer previously demanded by the vendor of Property AB, who tried to sub-sell Property AB as Confirmor.

50. Upon enquiry by the IRD, she gave a reply to the IRD dated 20 July 2010 confirming *inter alia*:

- (a) Mr F never instructed her to find a purchaser for him for the sale of Property B.
- (b) Mr F never made any counter-offer on the price to her client for the sale of Property B.
- (c) Her client, the ultimate purchaser, was very keen to purchase Property B and the purchase price was raised voluntarily.
- (d) The ultimate purchaser referred the tenant to fill up Room B3 - Room B4 for the 9 months pending completion.

51. Upon clarification by the Board, Ms X confirmed that she had not heard from the market that Property AB was offered for sub-sale at the material time. Further she confirmed that the purchase price of Property B was agreed about 1 week prior to signing the agreement for sale and purchase and it took about one week for her to finalize the terms of the provisional sale and purchase agreement.

Discussion and Analysis

52. Mr F on behalf of the Appellant repeatedly stated in the witness statement and in his oral evidence that the Appellant's intention was to hold Property B as an investment for long term basis at the time of signing the formal agreement for sale and purchase on 12 November 2007. Such intention was also stated in its audited report for the year ended 31 March 2008.¹¹

53. Such intention, however, did not materialize because Property B was sold by the Appellant on 29 November 2007 to Company Q, respectively, 15 days after the Appellant signed the agreement for acquisition and 13 days after the Appellant completed the sale and purchase with the vendor on 14 November 2007.

54. In our view, the sale of Property B within a very short period, i.e. 13 days,

¹¹ Page 6 and page 21 of the audited report for the year ended 31 March 2008

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after its completion at a price of about 46% higher than the acquisition price is a relevant factor for this Board to take into consideration. Mr F, Counsel for the Appellant, rightly agreed that the burden rests with the Appellant to adduce convincing evidences to make good its case that it genuinely intended that Property B was acquired for investment purpose instead of for trading purpose.

55. When Mr F was asked about his knowledge of the market conditions of Building W at the material time, i.e. from September to November 2007, he was evasive and his answers were vague. He was not forthcoming even when a simple question relating to his knowledge of the property market at the material time was put to him. He would give a lot of explanations relating to other matters without touching on the answers to the questions raised.

56. For example, when he was asked whether he had the impression that around October 2007, there were a number of offers for sale of units/floors of Building W in the market, he would not give a 'yes' or 'no' answer. He gave the explanation that he was the CEO of a joint venture which had 400 to 500 employees. He was responsible for marketing sales, purchases, and financial matters. He needed to manage 7 offices in the Mainland China and he was a very busy person and had no time to speculate property. So he only purchased properties for long term investment purpose. He relied on his 3 part-time staff to take care of his portfolio of investment properties and the rental matters. His decision to purchase a property depended very much on its rental yield. If the property gave a rental return of 4.5% or above, he would buy the property. Seldom did he buy a property with rental return lower than 4%. Before making a decision to buy a property, he would make assessment of the rental return. He also made an internal assessment of the rental yield of Property B and Property P before he decided to buy. He tried very hard to impress the Board that he was very busy and had no time to spend on studying the property market at material time implying that he had no knowledge about the market.

57. The value of Property B and Property P amounted to HK\$298.50 million. At one time, he also decided to purchase Property AB and 'chased' the sale price for 3 times though at the end of the day his final offer of HK\$163 million was not accepted by the vendor. After all, they were deals of several hundred million dollars. It is hardly believable that Mr F would make a decision to buy properties worth several hundred millions solely on the rental yield without regard to the then market conditions of the properties.

58. After a series of questions put by the Respondent's Counsel, Mr F eventually admitted that in or about October 2007, he knew the market of Building W was active and the prices went up since he acquired Property B and Property P. Mr AN and Ms X called him and gave him the market information of Building W several times a week. In fact, from the end of October 2007 until Property B was sold by the Appellant in late November 2007, Ms X had contacted him and gave him her client's revised offers several times, each with a price higher than the previous one. He also instructed Mr. AN to chase the price of Property AB respectively on 5 and 12 October 2007.

59. At first, Property B was acquired by Company H and Property P was

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purchased by Mr F through his company. Around the end of October 2007, Mr F agreed with Company H that he would swap to purchase Property B instead of Property P with Company H so that Company H would purchase Property P.

60. Mr F said that after the signing of the provisional agreement for both Property B and Property P on 21 August 2007, he took steps to rent out Rooms B3 - B4 which was vacant at that time and instructed estate agents to put up advertisement. Upon clarification by the Board, Mr F agreed that he only informed his 3 staff to see if they could find tenants to rent Room B3 – Room B4 after the swap with Company H made in late October 2007. The rental yield of Property B was about 3.378% at that time if Room B3 and Room B4 were vacant and the rental yield would be 4.6% on the fully let basis. Apart from this claim, there was no evidence from any property agents that Mr F had instructed them to lease Room B3 and Room B4. Neither were there any advertisements for leasing as allegedly produced by Mr F. The completion of the sale and purchase was due on 14 November 2007. It took time to locate suitable tenants. If he marketed the two vacant units at the end of October 2007 through property agents, the chance of leasing out those 2 units at an early day were better. It would certainly help to maintain a rental yield of 4.5% as early as possible. In the absence of convincing evidence relating to marketing the rental of Rooms B3 and B4 and advertisement as claimed, we do not accept Mr F's claim as made in paragraph 27(3) of his Witness Statement.

61. It was Mr F's concern that the partition of Room B3 and Room B4 was awful which might make those two units difficult to engage tenants. Mr F agreed that the partitions could be removed and re-erected. If such was his concern, we would expect that he would do something, such as the engagement of or obtaining quotations from contractors to rectify the awful partitions soon after completion of the sale and purchase, to rectify the situation. It would again help him to obtain the decided rental yield as soon as possible. Yet there was no evidence that he had done so.

62. The sale of a property held for trading purpose does not necessarily attract profit tax if it is involved in an exchange (or swap) of another property for trading or investment purpose.

63. Mr F gave evidence that there were two main reasons to justify the sale of Property B only 15 days after completion of the purchase, i.e. (a) the yield of the rental income of the property was decreasing based on the then current market value ('Decrease in Yield Reason'); and (b) an opportunity arose to swap to Property AB, a better quality property with the view not being blocked by Building AC at no additional costs ('Swap Reason'). Further he was worried with the impression that the irregular shape of the vacant Rooms B3 to B4 made it difficult to let out the units and that the sea view might be blocked by the intended Building AC. The swap provided him a good solution to the vacant Rooms B3 – B4 as Ms X's client indicated that its business associate would rent the unit at market rate before completion (collectively 'Other Reasons').

Decrease in Yield Reason

64. Upon cross-examination, Mr F confirmed that he would not sell Property B

if he did not have the opportunity of swapping Property AB which had a better rental yield and better view at no additional cost. Further, he also explained to the Board that he would not sell Property B even at a high price because the rentals would also rise in the near future so that the rental return might become higher as a matter of time. It therefore appeared to the Board that if there was a reason for the Appellant to sell Property B, the Decrease in Yield Reason was not the most important reason.

Swap Reason

65. Turning to the Swap Reason, we note that such reason was not stated in the audited account for the year ended 31 March 2007 at all. Upon clarification, Mr F agreed that the most important reason for selling Property B was the Swap Reason. He agreed that the Swap Reason was not made in the audited report. When questioning about why he chose not to state the Swap Reason, the most important reason in the audited report as he did for the Decrease in Yield Reason, the less important reason, he explained that the audited report was handled by professionals and he relied on professionals to do so. We have no reason to believe that his staff or the professionals were negligent or incompetent to omit the Swap Reason in the audited report if the Decrease in Yield Reason was stated. The audited report was approved and authorized for issue *inter alia* by Mr F. If his staff or professionals were negligent or incompetent, Mr F should rectify the same when he approved and authorized the issue thereof. It follows that Mr F might not mention the Swap Reason to the professionals or staff or Mr F chose not to mention when he approved the audited report or the Swap Reason did not exist.

66. It is noted that the auditor, Company AX stated in the said audited report that ‘as explained in note 11 and 19 to the financial statements, the investment properties which were held for long term purpose sold after year end, we had disagreement on the accounting classification of the properties as investment Properties under non-current assets.’ Although this remark was not binding on the Appellant and was merely the opinion of the auditors, it is fair to say that it was an objective view of the auditors or a third party.

67. Mr. F made the offer of \$14,000 per square foot to acquire Property AB in the afternoon on the date of his signing the provisional agreement for Property B with Company Q (i.e. 29 November 2007), but his offer was turned down by Ms AV, the vendor because according to Mr AN, there were only 6 business days left for completion with the head vendor and it was insufficient time for Ms AV to do the confirmor sale with Mr F.

68. According to Mr F, he needed not rely on bank financing to acquire Property AB and the title deeds was no longer an issue as far as Property AB was concerned. In the circumstances, Mr F could offer to pay a higher deposit than the usual 10% to 20% to Ms AV and confirm that he accepted the title of the property at the time of signing the agreement. The higher deposit could boost the confidence of Ms AV that the purchaser would unlikely be defaulted notwithstanding the fact that there were 6 business days left to do the transaction. The acceptance of title would obviate the time consuming process of proving and checking the title. We are of the view that if Mr F was serious in

the swap, he should take active and aggressive steps to secure the deal. However, there is nothing in evidence that he had done so. If he was serious about the swap, one would expect that he should put forward draft written agreement together with the usual deposit (at least) to Ms AV. To our surprise, he merely instructed Mr AN to orally accept Ms AV's offer. As an experienced property investor, Mr F should know that he would have a better chance to acquire Property AB if he took an active role. We do not understand why he did not do so and why he did not put forward the offer in writing.

69. According to Mr F, the offer of \$14,300 per square foot by Ms X came in mid-November 2007. He distinctly recalled that Ms X's offer at \$14,300 per square foot for Property B came two or three days after Mr AN had told him about the firm offer for Property AB at \$14,000 per square foot. In other words, Mr F should be in a position to take steps to effect the swap in or about mid-November 2007. At that time, there were about 20 days before the scheduled completion of the sale and purchase of Property AB between the head vendor and Ms AV. He should have sufficient time to negotiate with Ms AV for the terms of the confirmor sale. Nothing would bind Mr F unless and until an agreement was signed by the parties. The negotiation with Ms AV would not bind him if he did not sign any agreement. There was no harm whatsoever for him to contact Ms AV through Mr AN in mid-November 2007 if he intended to swap Property B for Property AB. Mr F should not start the negotiation 10 or even more days later until he signed the provisional agreement with Company Q. We do not understand why Mr F refrained from taking steps to effect the swap in or around mid-November if he was serious about the swap.

70. As an experienced property investor, Mr F knew better than anyone that no matter how firm a deal was represented by a party, the terms of the deal would not bind the parties unless an agreement was signed by the parties. Company Q through Ms X gave him the written offer as well as the deposit to acquire Property B on 29 November 2007. As a matter of fact, he needed not immediately sign the agreement. He could keep the written offer from Company Q for a while and in the meantime took all reasonable steps to negotiate with Ms AV for a deal of Property AB. If Ms AV was prepared to sub-sell Property AB on terms agreeable to him, Mr F could sign both the agreement for the sale of Property B and the agreement for the purchase of Property AB simultaneously one or two days thereafter. By doing so, the swap was secure. If he was rejected by Ms AV for whatever reason (including insufficient time to do the confirmor sale) or if Company Q withdrew the offer in the meantime, he could then keep Property B as he intended. It is difficult to explain why an experienced property investor would not do so if his intention was to keep Property B on long term basis but for the swap of Property AB.

71. In order to impress the Board that it was too good an offer that he could purchase Property AB at the price of HK\$14,000 per square foot while he could sell Property B, a property of lesser quality in terms of rental yields and the view of the property, at the price of HK\$14,300, he told the Board that he had ample financial resources to accommodate a short completion period and he had sufficient funds and credit to complete the purchase of Property AB without having to wait until completion of the sale of Property B. While we have no doubt about his financial position to pay the purchase price of HK\$196,980,000 for Property AB, we had a doubt on his ability to do so

within 6 business days. Common sense tells us that if you need to pay a sum of HK\$196,980,000 within a few days, you either have cash with a bank and/or the facility arrangement in an aggregate amount of HK\$196,980,000. It is quite easy to prove Mr F's resources if he chose to do so. He could produce the bank account and/or the banking facilities agreement to the Board for consideration to show that he needed not rely on bank loan to complete the purchase of Property AB. However, none of the same were produced by Mr F to substantiate his claim.

Other Reasons

72. Mr F told the Board that he was worried about the irregular shape of Room B3 to B4 and the difficulty in getting tenants for these two units. As explained in the above, the irregular partitions could be rectified relatively easily. It would need costs to do so but the costs involved in the rectification could, fairly speaking, be minimal when compared with the monthly rental received from those two units. We do not see Mr F had taken any steps to rectify the partition, i.e. by contacting contractors to give quotation for rectification.

73. Regarding the blockage of the view by the new Building AC, Mr F told the Board that he did not know the view of Property B would be blocked by the new building before he acquired Property B and Property P. However, such claim was defeated by Company AE's letter dated 21 October 2010 to the IRD.

74. In our view, these two worries should not be reasons, no matter how slight they were, to affect whether Mr F's intention to keep Property B was for long term investment basis.

Confirmor sale of Property AB

75. As pointed out in previous paragraphs, the account of the confirmor sale of Property AB given by Mr F consists of some inexplicable facts and some contradictions and is not convincing. Although Ms X said in her witness statement that Mr F told her at the time that he sold Property B because he had an opportunity to swap it with Property AB as he put forward an acceptance of the offer previously demanded by the Vendor of Property AB, who tried to sub-sell Property AB as Confirmor, such statement was lack of particulars. The probative value is not high especially Ms X confirmed that at the material times, she had not heard about the offer of Property AB in the market. Mr F confirmed that he did not put Property B for sale at the material time. From the reply given by Company Q's representative to the Inland Revenue Department, Company Q said that it was approached by Ms X and Property B was available in the market at that time (paragraph 20 (a) and (b) above). On the face of it, if there was an offer in the market, the offer had to be from the owner. We do not know why the Appellant did not see fit to clarify this with Ms X.

76. We feel the best person who could assist the Board on Property AB offer was Mr AN, as he dealt with Ms AV and Mr F direct. He was not called to testify or to give a witness statement. According to Mr F it was because he left Company Z in bad

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terms and he had been in financial difficulty since then, and he asked to be paid for giving a witness statement. We do not find this reason believable. Mr F was a big client of Mr AN (at least at the material time). As a property agent, his income depended very much on the transactions put through by him. Mr AN had to maintain good relationships with his clients, no matter they were vendors or purchasers. The purchase of Property B and Property P had brought Company Z or himself millions of dollars of commission no matter such commission was paid by the vendor or Mr F.

77. Mr F was an experienced investor. Few agents could communicate direct with Mr F. Mr AN was a lucky one because Mr F could deal with him direct. In the normal course of event, if Mr AN was requested to assist Mr F to tell the truth, we find it hard to believe that Mr AN would reject such a reasonable request from Mr F. The potential monetary benefit of maintaining a good relationship with Mr F would certainly outweigh the costs and expenses of attending before this Board. His departure from Company Z, in our view, should not have any bearing on his willingness to give evidence for Mr F because he was not asked to give evidence to any confidential information of Company Z. Ms X came forth to act as a witness though she left Company Y in 2014.

78. The agreement for sale and purchase was first signed between the Appellant and Company Q on 29 November 2007. The completion date specified was on 28 August 2008. In other words, the completion period was nine months.

79. In giving evidence, Mr F said that the deposit paid by Company Q was twenty percent. However, the agreement in question showed that Company Q only paid 10 percent deposit to the Appellant.

80. Property speculators would like to use limited companies to enter into agreement for sale and purchase. They would like long completion period because it would give them time to find sub-purchasers. If they could find sub-purchasers prior to the scheduled completion date, they might not need to arrange finance to complete the purchase and could take the difference in price. Long completion periods would maximize their trading profit or their chance of making trading profit. If the market changed at the time, the speculators could limit its loss to the deposit paid if the buyer was a limited company with no substance.

81. Property speculators would like to minimize their risk by paying deposits as low as possible. If there was an adverse change in market prior to the completion, the loss was limited to the deposit so paid.

82. Property speculators would therefore pay a 'higher' purchase price in exchange for a longer completion period as well as a lower deposit payable. Judging from the price paid by Company Q to the Appellant, the completion period and the amount of deposit paid and Mr F's knowledge of the then property market, Mr F should probably know that the Appellant was selling Property B to a property speculator.

Badges of Trade

83. We now turn to the badges of trade as referred to by McHugh NPJ in Lee Yee Shing, which counsel for the Appellant asked us to consider:

- (1) Whether the Appellant has frequently engaged in similar transactions: The Appellant had traded in property once at the material time.
- (2) Whether the Appellant has held the asset or commodity for a lengthy period: less than one month.
- (3) Whether the Appellant has acquired an asset or commodity that is normally the subject of trading rather than investment: Property B 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.

84. We have to say that there is no mechanical calculation of scores of the badges of trade so that a certain score would indicate whether there is an intention to trade or to carry on a trade. As per Bokhary and Chan PJJ said in Real Estate Investments (NT) Limited, *'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....'* (paragraph 55).

Findings

85. Overall, for the reasons stated above, we do not find that the evidences

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given by Mr F are credible or reliable. He tailored his evidence to support his case. Counsel for the Appellant stressed to the Board that Mr F's whole investment history tallied with long-term investment, both before and after the sale of Property B. However, from Mr F's investment portfolio submitted to the Board for consideration, it is not difficult to discover that there were 6 occasions in which Mr F sold properties within several months after he acquired the same. As such, it is quite clear that although overall he holds properties on long term basis, he also did engage in short flaps of properties occasionally. This further adds our doubt on Mr F's creditability on his overall evidences.

86. By reason of the aforesaid analysis, there are no sufficient evidences, not to mention convincing evidences, to persuade us to believe (a) the existence of the offer of Property AB at the material time; (b) that the Decrease in Yield Reason, the Swap Reason and Other Reasons were the reasons for the Appellant to sell Property B and (c) Property B was acquired for long term investment purpose. Taking a holistic consideration of the circumstances of the appeal, we do not find the objective facts consistent with the Appellant's stated intention that Property B was acquired for long term investment purpose.

87. We have carefully considered the very able and comprehensive submissions made by the Appellant's Counsel including those referred to in paragraph 88 to paragraph 91 below. Based on the holistic consideration of all the circumstances of the case, including the matters discussed above and all evidences and documents of the appeal, in particular, the Appellant's board resolutions passed respectively on 12 November 2007 and 29 November 2007 for the purchase and sale of Property B and Company H's board resolutions, we come to the following conclusions:

- (a) At the time of swapping the property with Company H around October 2007 and at the time of signing the formal agreement for sale and purchase on 12 November 2007 by the Appellant, Mr F had sufficient information relating to the property market of Building W and was well aware that the market was very active and the price of Floor AS rose a lot around that time when compared with the price agreed with the vendor in August 2007.
- (b) Around the time of the swap with Company H, he knew Property B could be sold much higher than the original acquisition price. The rental income was fixed until the tenancies in questions were renewed at a higher rental. If he used the rental income to compare with the possible sale price (or the then market value), the rental yield would drop to about 2.35%. This rental yield did not fit his investment philosophy that he seldom bought property with rental yield lower than 4%.
- (c) Coupling with the fact that he took no steps with a view to achieving the rental yield of 4.5% or above as discussed in the previous paragraphs, we find it as facts that (i) at the time of swapping with Company H, Mr F swapped Property B around end of October 2007

for trading purpose; and (ii) Property B was acquired by the Appellant on 12 November 2007 for trading purpose, not for investment purpose as he claimed.

- (d) The Appellant's intention at the time of selling Property B was to sell it for trading purpose to Company Q. There was no change in the Appellant's intention that Property B was for trading purpose between the time of acquisition and the time of sale.
- (e) The Appellant failed to discharge the onus of proof under section 68(4) of the Inland Revenue Ordinance that the assessments were excessive or incorrect.

Other Submissions

88. Counsel for the Appellant submitted that the relevant time to ascertain Mr F's intention was 21 August 2007 when Company C committed to buy Property B and Property P. With due respect, we do not agree. The Appellant was incorporated on 8 October 2007 and was 'activated' by the appointment of Mr F as its director on 6 November 2007. Since we held the view that Mr F swapped Property B with Company H around end of October 2007 and Property B was acquired by the Appellant on 12 November 2007, both for trading purpose, it is irrelevant whatever the intention of Mr F might have for and on behalf of Company J on 21 August 2007 in respect of Property P or Property B because the Appellant did not exist at that time. Even if we were wrong in this aspect, taking into account of the whole circumstances of the case and creditability of the evidences given by the Appellant, we are not certain that Mr F acquired Property P (which was switched to Property B) for long term investment purpose in August 2007. We are still of the opinion that the Appellant fails to discharge its onus of proving that the assessments were excessive and incorrect.

89. It is also the Appellant's submission that the subsequent acquisitions of Property T and Property V for long term investment purpose consequent upon the failure of acquiring Property AB would support the fact that the Appellant's intention of selling Property B was for swapping Property AB for long term investment purpose. Since we held that the Swap Reason was not accepted by us, the subsequent purchases of Property T and Property V, in our view were two separate transactions not connected with the sale of Property B.

90. It is also the Appellant's contention that if Property B was for trading purpose, the Appellant could sell it earlier as a confirmor without paying the stamp duty of more than five millions dollars. We do not accept this argument as a reason that Property B was acquired for long term investment purpose. Whether Property B could be sold by the Appellant as a confirmor within a relatively short time to match the completion date of the head sale has a number of factors. As we can see, the relevant factors include the availability of purchasers who was willing to pay the price asked for and whether the intended purchasers had the financial resources to pay the purchase price within a relatively short time.

91. The Appellant through its counsel also submitted that if Property B was not sold for the swap purpose, the Appellant could keep the same and sell it at a later day bearing in mind of the rising trend of the price of Building W. We do not find this argument attractive because we are not sure if there was a rising trend in price. From the price list produced by the Appellant, it mainly showed the prices of smaller units in Building W. If there was a trend, the trend was only related to the prices of smaller units, which should not have persuasive force that the trend applied to the prices of 'floors'. There were only 2 sales recorded for whole floors around the material time. The sale prices (on per square foot basis) of those two floors were lower than that of Property B. Given the small number of sample data, we do not think that there was a trend in prices for 'floors' of Building W at the material time.

Conclusion and Disposition

92. For the reasons and analysis set out above, we dismiss the appeal and confirm the two assessments appealed against as confirmed by the Deputy Commissioner on 24 April 2015.

Costs

93. If the Appellant fails in its appeal, the Board may order the Appellant to pay as costs of the Board a sum not exceeding the amount of \$25,000 pursuant to section 68(9) of the Ordinance.

94. The Appellant sold the property in question within 15 days after its completion and made a profit of 46%. It requires a lot of convincing evidence to support its claim that the property was acquired by it for long term investment purposes.

95. As analyzed in the above, the evidences adduced by the Appellant to support its reasons for the disposal of the property within a very short period of time after its acquisition were flimsy, vague and contradictory and hard to believe. There is no reasonable prospect of success in the appeal. In our view, this appeal is frivolous and vexatious. Given the tax amount involved being more than \$9 million and the maximum costs which the Board might impose being \$25,000, there was a great temptation for the Appellant to do so even though the appeal was hopeless.

96. In the circumstances we feel it right to order the Appellant to pay a sum of HK\$25,000 as costs of the Board which shall be added to the tax charged and recovered therewith pursuant to section 68(9) of the Ordinance.