

**Case No. D8/16**

**Profits tax** – absence of witness by taxpayer – whether adverse inference can be drawn against the taxpayer – whether weight can be attached – section 68(4) of the Inland Revenue Ordinance – stated intention is not decisive – burden to prove the purchase did not amount to an adventure in the nature of trade was on the Appellant

Panel: Chow Wai Shun (chairman), Chan Chak Ming and Tse Ming Yee.

Date of hearing: 24 March 2016.

Date of decision: 24 May 2016.

The Appellant purchased Property 1 from the developer when it was under construction and the assignment was completed on 26 August 2010. The Appellant sold Property 1 by a provisional agreement for sale and purchase agreement on 30 September 2010. The Appellant purchased Property 2 and the assignment was completed on 2 June 2010. The Appellant sold Property 2 by a provisional agreement for sale and purchase on 8 August 2013 and had a loss of sale of Property 2.

The Appellant claimed that Property 1 was purchased as long-term investment. The Assessor was of the view that the profit on sale of Property 1 should be chargeable to Profits tax.

The Appellant claimed that the poor view made Property 1 undesirable as a long-term investment and the quick decision of the Appellant to sell it is justified, consistent with her contention to purchase a flat as a long-term investment. The Appellant also contended that the purchase of Property 2 shortly after Property 1 was put up for sale, and before the sale of Property 1 is a strong indication of her intention to acquire a property for long-term investment and not just for trade.

**Held:**

1. The absence of a witness for a taxpayer may prompt this Board to draw adverse inference against the taxpayer. The Board may draw adverse inference against a taxpayer who is in the best position to provide such relevant information but has refused to do so in the witness box. At the very least, this Board cannot attach much weight, if any, to the allegations and assertions of a taxpayer which are not tested by cross-examination. A taxpayer cannot expect this Board to act on his or her bare allegations (D14/08 (2008-09) IRBRD, vol 23, 244 and D45/10 (2011-12) IRBRD, vol 26, 21 followed). On the basis of section 68(4) of

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the IRO and the authority of the Common Empire case, this appeal can be dismissed.

2. The stated intention of the Appellant is not decisive and must be measured against the whole of the surrounding circumstances of the case, including things said and things done at the time, before and after. The burden of proving that the purchase and sale of Property 1 did not amount to an adventure in the nature of trade was on the Appellant.
3. In light of the way that the Appellant had dealt with what would have been her strongest point, we are not convinced by the reason proffered by the Appellant for the quick disposal of Property 1. The Board also finds that the Appellant purchased Property 1 with an intention to trade.

**Appeal dismissed.**

Cases referred to:

Lionel Simmons Properties Limited (in liquidation) and others v Commissioners of Inland Revenue (1980) 53 TC 461  
Marson v Morton [1986] STC 463  
All Best Wishes Limited v Commissioner of Inland Revenue (1992) 3 HKTC 750  
Commissioner of Inland Revenue v Common Empire Ltd (No 2) [2007] 3 HKLRD 75  
Lee Yee Shing v Commissioner of Inland Revenue [2008] 3 HKLRD 51  
D14/08, (2008-09) IRBRD, vol 23, 244  
D45/10, (2011-12) IRBRD, vol 26, 21

Appellant in person.

Lo Hok Leung, Dickson and Chan Siu Ying, Shirley, for the Commissioner of Inland Revenue.

**Decision:**

1. This is an appeal by the Appellant against the Determination of the Deputy Commissioner of Inland Revenue dated 29 July 2015 in respect of the Profits Tax Assessment for 2010/11 on her ('the Determination').
2. The Appellant chose not to give any oral evidence at the hearing. Other than those documents already submitted prior to the hearing, the Appellant did not adduce anything further.

**Facts**

3. As the Appellant raised no dispute on the facts upon which the Determination was arrived at, we find those relevant facts of this appeal:

- (a) i. By a provisional contract dated 11 October 2009, the Appellant purchased Address A ('Property 1') at a consideration of \$14,015,000. The agreement for sale and purchase was executed on 14 October 2009 and the assignment was completed on 26 August 2010.
- ii. By a provisional agreement for sale and purchase dated 30 September 2010, the Appellant sold Property 1 at a consideration of \$15,800,000. The agreement for sale and purchase was executed on 14 October 2010 and the assignment was completed on 16 November 2010.
- (b) i. By a provisional contract dated 6 March 2010, the Appellant purchased Address B ('Property 2') at a consideration of \$21,230,000. The agreement for sale and purchase was executed on 9 March 2010 and the assignment was completed on 2 June 2010.
- ii. By a provisional agreement for sale and purchase dated 8 August 2013, the Appellant sold Property 2 at a consideration of \$20,080,000. The agreement for sale and purchase was executed on 22 August 2013 and the assignment was completed on 20 November 2013.
- (c) i. The Appellant purchased Property 1 from the developer when it was under construction. The Appellant agreed to pay the purchase as follows:

<u>Payable</u>	<u>Amount (\$)</u>
Upon signing the provisional contract	700,750
<u>Payable</u>	<u>Amount (\$)</u>
On or before 2 November 2009	700,750
On or before 25 November 2009	700,750
On or before 9 January 2010	700,750
Upon completion of purchase	<u>11,212,000</u>
	<u>14,015,000</u>

- ii. To finance the purchase, the Appellant obtained a mortgage loan of \$9,810,500 from Bank C by pledging Property 1. The loan was repayable by 360 monthly instalments of \$30,884 each.

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- (d) The Appellant derived a gain of \$918,712 on sale of Property 1, which was computed as follows:

	\$
Sale proceeds	15,800,000
<u>Less: Purchase price</u>	<u>14,015,000</u>
	1,785,000
<u>Less:</u>	
Legal fee	29,628
Stamp duty	525,563
Commission to agents	158,000
Bank interest, charges and penalty	128,346
Others	<u>24,751</u>
Gain	<u>918,712</u>

- (e) In reply to a questionnaire on property transactions, the Appellant claimed that Property 1 was purchased as long-term investment and was sold for the following reasons:

‘(Property 1) was under construction at the time, so it was not possible to view the flat. I was assured that the flat was at a high enough level to provide a very good view, an asset that I consider essential for a property to maintain its value as a rental unit over a reasonable period of time. Eventually the property could be viewed and I was shocked to discover that the “very good view” was limited to the walls of the surrounding buildings, and the occasional trash-covered rooftop. I still have confidence in the development but not (Property 1). As soon as the poor view was discovered, I made plans to sell it and to replace it with another unit in the same development, but one with a good view. ... I purchase (Property 2) while (Property 1) was up for sale.’

- (f) The Assessor was of the view that the profit on sale of Property 1 should be chargeable to Profits Tax and raised on the Appellant the following 2010/11 Profits Tax Assessment:

Assessable Profits [paragraph 3(d)] \$918,712

- (g) The Appellant objected to the assessment.
- (h) The Assessor ascertained the following information from property agents:

Company D

- i. On 6 May 2010, the Appellant signed Estate Agency Agreement for Sale of Residential Properties in Hong Kong, by which the Appellant appointed Company D effective for the period from 6 May 2010 to 5 May 2011 to sell Property 1 at an asking price of \$15,600,000.
- ii. The Appellant changed the asking prices as follows:

<u>Date</u>	<u>Asking price (\$)</u>
25-06-2010	14,800,000
30-07-2010	16,500,000
10-08-2010	Range from 16,000,000 to 16,500,000
19-08-2010	16,500,000
09-09-2010	16,000,000
13-09-2010	15,800,000

- iii. Company D's computer records showed the following descriptions:

<u>Date</u>	<u>Description</u>
30-05-2010	'Urgent for sell 1.5% comm.'
28-08-2010	'Take key 3% by [Mr E]'
29-08-2010	'Key copied already can take key from admin'
13-09-2010	'Price change 15.80m... urgent'

- iv. Mr E as estate agent signed the form for and on behalf of Company D.
- v. The Appellant did not sign any Estate Agency Agreement to appoint Company D as an estate agent to let out Property 1.

Company F

- vi. On 4 September 2010, the Appellant appointed Company F to sell Property 1 at an asking price of \$16,500,000. The Appellant changed the asking price to \$15,800,000 on 12 September 2010.
- vii. The Appellant did not appoint Company F to let out Property 1.
  - (i) The Appellant put forward the following contentions:
    - i. 'A flat with a view will yield a higher rent and will experience

better capital appreciation than a flat without a view... I purchased (Property 1), sight unseen, based on assurances that it offered a fine view of Victoria Harbour. As soon as I took possession I realized that the promised view did not exist; the view was only of other building rooftops, almost all of them covered in shabby, illegal, tin-roofed structures. When I realized that I had not made a good, long term investment by buying this property, I knew that I should change it to a better quality one and this is exactly what I did. I immediately put up (Property 1) for sale and made a down payment on a unit with a good view in the same development, (Property 2), which I subsequently rented out for two years, and in which I now reside as my personal residence...’

- ii. ‘... I purchased (Property 2) before I sold (Property 1). It is mainly because I realized that I have made a mistake by buying (Property 1) due to the very poor view of the apartment... (Property 2) came along in the secondary market and after having viewed it, I further confirmed that (Property 1) is a much more inferior product and I was really determined to sell it. I bought (Property 2) because I think it is a much higher quality apartment with better long term investment potential. I took the risk of buying (Property 2) even before I can dispose (Property 1) and it shows that I was not speculating on whether I can make profit on (Property 1) or not. The decision is purely made to change the investment into a long term better quality investment.’
  - iii. ‘There is another reason why I wanted to correct my investment mistake as soon as it became apparent and that is I wanted to make the change before I retired so that I could still take out a mortgage on the property. I would face other uncertainties in the environment if I did not take timely actions... In retrospect, it has proven me right that I did take prompt action as a retiree-to-be to correct my investment mistake. Otherwise it would have been too late and I would be stuck with a substandard quality property...’
  - iv. ‘(Property 1) was sold... as it was still under constructions. What the prospective purchasers were shown were graphic representations and beautifully decorated show rooms based upon which the investors were coerced by aggressive salesman to make instantaneous purchase decision. I am a victim of this sales process...’
- (j) The Determination was so made and handed down, confirming the assessment referred to in paragraph 3(d) above. The Appellant

lodged an appeal with this Board.

### **Grounds of appeal**

4. In her grounds of appeal, the Appellant raised that the Deputy Commissioner had chosen to accept certain facts and to ignore or misinterpret others. She also challenged against the Deputy Commissioner's logic by claiming that the decision to deny her objections appeared to have been made first and that the facts and logic were incorporated in order to reach the pre-ordained conclusion.

5. Specifically, the Appellant claimed that the Deputy Commissioner had chosen to ignore that the poor view made Property 1 undesirable as a long term investment and the quick decision of the Appellant to sell it is justified, consistent with her contention to purchase a flat as a long-term investment.

6. Furthermore, the Appellant attempted to argue that to issue rental instructions would have hindered the sale of Property 1 and would have been contrary to her intention of acquiring a good long-term investment and disposing of a poor one.

7. The Appellant also sought to clarify that she discovered the poor view of Property 1 about 7 months after she contracted to purchase it, long before she took possession.

8. Lastly, the Appellant contended that the purchase of Property 2 shortly after Property 1 was put up for sale, and before the sale of Property 1 is a strong indication of her intention to acquire a property for long-term investment and not just for trade. Consequently, according to the Appellant, the purchase of Property 2 should be considered as evidence of her intention at the time of acquisition in such a way that if Property 1 had proven to have a good view as promised, she would have treated it as she did to Property 2, renting it out and perhaps even occupying it herself.

### **The law**

9. It is common ground that the following provisions of the IRO apply.

(a) Section 14 provides:

*'(1) 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.'*

(b) Section 2(1) defines 'trade' to include 'every trade and manufacture, and every adventure and concern in the nature of trade.'

- (c) Section 68(4) provides:

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

10. We also find that the following cases and the legal principles arisen therefrom apply.

- (a) Lionel Simmons Properties Limited (in liquidation) and others v Commissioners of Inland Revenue (1980) 53 TC 461;
- (b) Marson v Morton [1986] STC 463;
- (c) All Best Wishes Limited v Commissioner of Inland Revenue (1992) 3 HKTC 750;
- (d) Commissioner of Inland Revenue v Common Empire Ltd (No 2) [2007] 3 HKLRD 75; and
- (e) Lee Yee Shing v Commissioner of Inland Revenue [2008] 3 HKLRD 51.

11. According to Simmons, *‘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.’* (per Lord Wilberforce at page 491).

12. Mortimer J in All Best Wishes at page 771 stated that *‘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 realizable, 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.’* This was indeed echoed by the Court of Final Appeal decision in Lee Yee Shing where Bokhary and Chan PJJ ruled that the question whether something amounts to the carrying of a trade (or



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business) *‘is a question of fact and degree to be determined by the fact-finding body upon a consideration of all the circumstances.’*

13. Indeed, in the words of McHugh NPJ in Lee Yee Shing, the intention to trade to which Lord Wilberforce referred in Simmons is not subjective, but objective and it requires an examination of all the circumstances to see whether the ‘badges of 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?

14. McHugh NPJ also said that ‘in some cases, the source of finance for the purchase may also be a badge of trade, particularly where the asset or commodity is sold shortly after purchase’ but ‘borrowing to acquire an asset or commodity is usually a neutral factor.’

15. This list of badges coincides much with the one in Marson v Morton [1986] STC 463 in which Sir Nicolas Browne-Wilkinson V-C held that ‘a single, one-off transaction can be an adventure in the nature of trade’ and 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. 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?’ Alternatively, one may ask, ‘was the taxpayer investing the money or was he doing a deal?’

16. With regard to section 68(4), Deputy Judge To in CIR v Common Empire Ltd (No 2) stated:

*‘... The Commissioner has no burden of proving that the assessment is correct. Hence, the Board is not bound to make any finding of fact one way or the other. If the taxpayer fails to adduce any evidence to discharge his burden, or if the evidence is disbelieved, the appeal shall be resolved on the burden of proof by dismissing the appeal and upholding the assessment.’*

### **Our analysis**

17. It would have been better if we could have heard testimony directly from the Appellant herself and seen how she might react and respond to cross-examination. The Appellant explained that given her age (63 years at the date of hearing as she said in her opening submission) she might not be able to recall accurately every detail of events which took place more than 6 years ago and she did not want to be accused of saying anything which turned out to be not true. While we can understand, the concern will not materialize if a witness just says under oath whatever he or she thinks is true. This is the same if he or she just says that he or she cannot recall such and such detail.

18. As we shall elaborate further below, we would also have preferred to hear from Mr E, her estate agent, but he was not called either.

19. As a general matter, this Board does not proactively summon any witness or independently investigate the case. On the other hand, the absence of a witness for a taxpayer may prompt this Board to draw adverse inference against the taxpayer: see e.g. D14/08, (2008-09) IRBRD, vol 23, 244. On the same token, this Board may draw adverse inference against a taxpayer who is in the best position to provide such relevant information but has refused to do so in the witness box: see e.g. D45/10, (2011-12) IRBRD, vol 26, 21. In the latter circumstance, at the very least, this Board cannot attach much weight, if any, to the allegations and assertions of a taxpayer which are not tested by cross-examination. In other words, a taxpayer cannot expect this Board to act on his or her bare allegations. This is one of such cases here. On the basis of section 68(4) of the IRO and the authority of the Common Empire case, this appeal can be dismissed.

20. Further or alternatively, we now turn to apply the well-established badges of trade to the facts of this case in order to ascertain the objective intention of the Appellant.

21. The stated intention of the Appellant is not decisive and must be measured against the whole of the surrounding circumstances of the case, including things said and things done at the time, before and after.

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22. The fact that Property 1, being interest in land, can be the subject of either trading or investment is a neutral factor.

23. While the Respondent attempted to argue against the Appellant with reference to the mode of financing the purchase of Property 1, the case authorities tend to suggest that this is usually a neutral factor. The fact that the Appellant deferred bulk of the purchase price on Property 1 to the date of completion is not peculiar in the circumstances either. After all, the Appellant acquired Property 1 while it was still under construction. It is common to defer the balance of purchase price (which is more substantial in amount) to after the purchase being notified that the property is ready for occupation. In this regard, therefore, we do not hold this against the Appellant.

24. On the other hand, although there is no evidence suggesting that the Appellant has frequently engaged in similar transactions, this incident alone may still amount to an adventure in the nature of trade. As a matter of fact, shortly after acquiring Property 1, the Appellant did purchase Property 2. Had Property 2 been subject to a similar quick sale, the Appellant would probably have been in a much worse position.

25. The Appellant had held Property 1 for a short period of time. The Appellant entered into a provisional contract to purchase Property 1 while it was still under construction and Property 1 had never been rented out nor had it been for personal use before it was disposed of. Indeed, the Appellant put forward Property 1 for sale through Company D well ahead of her being notified to complete her purchase of it and no effort had ever been made to find a possible tenant. We agree with the Respondent that such a short period of ownership is a strong indicator, and the strongest factor in this case, towards trading unless the disposal can be satisfactorily explained.

26. The reason proffered by the Appellant for the quick disposal has been that Property 1 turned out to have a poor view, unexpected by the Appellant, which would not yield the investment return she had expected. However, as to the time when the so-called poor view was discovered, the Appellant had not been clear and firm.

27. The Appellant when objecting to the assessment in February 2013 contended that she realized the poor view after taking possession of Property 1. Apparently, a few photos had been taken and were sent to the Assessor in August 2013. However, those photos did not show when they were actually taken and from where. No direct oral evidence was adduced to clarify and substantiate which photo(s) was/were taken from Property 1 and when. In response to the Assessor's inquiry on the date of visit of Property 1, the Appellant wrote that she could not remember and she did not keep any copy of the document on the visit. She thought at that time it was not relevant.

28. The position was subsequently rectified and changed on her notice and grounds of appeal to this Board to the effect that the poor view was first noticed from a nearby apartment about 7 months after she had purchased Property 1 in October 2009. In her opening submission, the Appellant alleged further that she was brought to a 'neighbouring' property by Mr E, her estate agent. Mr E might have been able to assist in

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a number of ways in substantiating and establishing certain facts including the date of the visit and/or when and from where those photos referred above were taken.

29. In her reply to the Respondent's written submission that she entered into the provisional contract to purchase Property 2 (as a substitute of Property 1 as the Appellant's case is) in March 2010 rather than May 2010 (which is 7 months after October 2009), the Appellant missed the relevance and importance of the two dates and just said that she could not understand the Respondent's logic. It was until the very end of the hearing when we pressed further by asking her in which month she visited Property 1 and discovered the poor view that the Appellant said that it was during the first few days of March 2010, shortly before the purchase of Property 2. March 2010, however, is just 5 months after the purchase of Property 1, not 7 months as the Appellant had claimed so far. While it is possible that the Appellant had just miscounted the number of months between her purchase of Property 1 and the time she discovered the so-called poor view of it, we take the view that such uncertainty created by the Appellant is not necessary and could have been easily avoided. In any event, none of such information was given nor confirmed in the witness box and so this could not be admitted as evidence.

30. The burden of proving that the purchase and sale of Property 1 did not amount to an adventure in the nature of trade was on the Appellant. In light of the way that the Appellant had dealt with what would have been her strongest point, we are not convinced by the reason proffered by the Appellant for the quick disposal of Property 1.

31. As such, taking an overall view of the relevant factors and on the facts as found and inferences as drawn above, we find that the Appellant purchased Property 1 with an intention to trade. This is the case irrespective of how the Appellant had dealt with Property 2 since in deciding whether the purchase and sale of a property may constitute an adventure in the nature of trade each property has to be considered on its own facts.

### **Conclusion**

32. Accordingly, we hold against the Appellant and dismiss her appeal.