

**Case No. D1/06**

**Profits tax** – onus wholly on the appellant to show the assessment excessive or incorrect – sections 16(1), 17(1)(a) and 68(4) of the Inland Revenue Ordinance (‘IRO’).

Panel: Kenneth Kwok Hing Wai SC (chairman), Wilson Chan Ka Shun and Kenneth Leung Kai Cheong.

Date of hearing: 27 February 2006.

Date of decision: 4 April 2006.

The appellant carried on sole proprietorship business (the ‘Firm’) as an insurance agent.

For the year of assessment 2001/02, the Deputy Commissioner disallowed the expenses that the appellant claimed to have incurred and paid to her younger sister (the ‘Sister’ as sub-agents), alleged staff (the ‘Alleged Staff’ as sub-agent and secretary) and her father (the ‘Father’ as clerk), all of whom worked and resided in China mainland.

The appellant appealed.

**Held:**

1. Section 16(1) provides for deduction of all outgoings and expenses incurred in the production of profits chargeable to profits tax.
2. According to section 17(1)(a), no deduction shall be allowed for domestic or private expenses.
3. The Board was satisfied on a balance of probabilities:

3.1 The following documents were not contemporaneous:

- Written agreements between the Firm and the Sister, Alleged Staff and the Father all purportedly made on 28 December 2000 in China mainland;
- Copy of the receipt dated 27 January 2006 signed by the Sister

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acknowledging receipt of commission in the sum of RMB239,584.

- Copy of the receipt dated 30 April 2002 signed by the Alleged Staff acknowledging receipt of RMB62,480;
- Copies of the 24 receipts signed by the Alleged Staff and the Father on various dates acknowledging receipts of their respective salaries.

3.2 The appellant did not incur any of the sums she claimed to have been incurred and paid to the Sister, the Alleged Staff and the Father.

3.3 Even if any such expenses had been incurred, they were not incurred in the production of profits but were domestic or private expenses.

4. The appellant failed to discharge her onus of proving that the assessment appealed against is excessive or incorrect.

**Appeal dismissed.**

Taxpayer in person.

Wong Siu Suk Han and Ng Yuk Chun for the Commissioner of Inland Revenue.

**Decision:**

1. This is an appeal against the Determination of the Deputy Commissioner of Inland Revenue dated 25 July 2005 whereby the profits tax assessment for the year of assessment 2001/02 under charge number 3-1610435-02-2, dated 19 November 2002, showing assessable profits of \$1,500,000 with tax payable thereon of \$225,000 was reduced to assessable profits of \$998,576 with tax payable thereon of \$149,786.

2. The year of assessment is 2001/02 ('the Year of Assessment'). The basis period is 1 April 2001 – 31 March 2002 ('the Basis Period').

3. The appellant carried on business as an insurance agent in a firm name ('the Firm'). She was the sole proprietress of the Firm.

4. During the Basis Period, the appellant received \$362,835 from an insurance company and \$1,922,440 from another insurance company ('InsuranceCo'), totalling \$2,285,275. She claimed to have incurred expenses totalling \$845,802 and offered to attribute 1/3 of the

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expenses on business trip, entertainment, motor vehicle, gifts to customers and agents, and mobile phone to private use. The private use portion totalled \$137,492.

5. The Deputy Commissioner allowed deduction of all the expenses claimed except the following:

- (a) \$233,900 said to have been paid to the appellant's younger sister who resided in China mainland ('the Sister') as an alleged sub-agent;
- (b) \$61,000 said to have been paid to a resident in China mainland ('the Alleged Staff') as an alleged sub-agent;
- (c) \$42,000 said to have been paid to the Alleged Staff as a 'secretary – PRC';
- (d) \$36,000 said to have been paid to the appellant's father who resided in China mainland ('the Father') as an alleged 'Clerk – PRC'.

6. Until the hearing of the appeal on 27 February 2006, the appellant was represented by Mr A (whom we assume is Mr B) of Accounting Company C. For reasons which have not been satisfactorily explained, neither Mr A nor any other person from Accounting Company C attended the hearing and the appellant appeared in person.

7. The appellant and the Sister gave evidence on oath.

8. By letter dated 24 January 2005, the assessor wrote to Accounting Company C asking for specific information and further details on the claims for deduction. There was no response. The absence of any response was noted by the Deputy Commissioner in his Determination. By letter dated 2 February 2006, Mrs Wong Siu Suk-han wrote to Accounting Company C inviting a response to the 24 January 2005 letter and trying to agree facts. Again, there was no reply. By letter dated 20 February 2006, Mrs Wong Siu Suk-han sent a reminder to Accounting Company C.

9. By fax dated 23 February 2006, Mr A of Accounting Company C sent a brief reply and enclosed a few copy documents which included:

- (a) what purported to be an agreement made between the Firm and the Sister and signed on 28 December 2000 in City D (of China mainland);
- (b) what purported to be an agreement made between the Firm and Alleged Staff and signed on 28 December 2000 in City D; and

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- (c) what purported to be an agreement made between the Firm and the Father and signed on 28 December 2000 in City D.

10. We are not satisfied on a balance of probabilities that the alleged written agreements, copies of which Mr A of Accounting Company C sent by fax dated 23 February 2006 to the assessor were contemporaneous.

- (a) If these alleged written agreements had come into existence on 28 December 2000, there is no reason why copies had not been sent to the assessor until 23 February 2006.
- (b) There is no explanation why copies had not been sent to the assessor earlier.
- (c) The Sister was adamant in her testimony that she and the appellant signed the alleged agreement in each other's presence on 28 December 2000 in City D, even after it had been pointed to her that the appellant was in Hong Kong on 28 December 2000. Information provided by the Immigration Department showed that the appellant was in Hong Kong from 26 December 2000 to 9 January 2001.
- (d) The appellant then came up with a new version and alleged that she signed in Hong Kong and had them brought over to China for the others to sign. If the appellant had signed in Hong Kong, there was no reason for her to write down the words on all three alleged agreements that they were signed in City D.

11. At the beginning of the hearing, the appellant produced what purported to be a copy of a receipt dated 27 January 2002 signed by the Sister acknowledging receipt of commission in the sum of RMB 239,584.

12. We are not satisfied on a balance of probabilities that the alleged receipt was contemporaneous.

- (a) If the alleged receipt had come into existence on 27 January 2002, there is no reason why a copy had not produced until the beginning of the hearing.
- (b) There is no explanation why a copy had not been sent to the assessor earlier.
- (c) The Sister asserted that she had not been paid by 27 January 2002. There is no explanation how the Sister came up with the figure of RMB239,584.

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13. At the end of the hearing, the appellant produced what purported to be a copy of a receipt dated 30 April 2002 signed by the Alleged Staff acknowledging receipt of commission in the sum of RMB 62,480.

14. We are not satisfied on a balance of probabilities that the alleged receipt was contemporaneous.

(a) If the alleged receipt had come into existence on 30 April 2002, there is no reason why a copy had not been produced until the end of the hearing.

(b) There is no explanation why a copy had not been sent to the assessor earlier.

15. By letter dated 10 October 2003 to the assessor, Mr A of Accounting Company C enclosed copy documents including copies of what purported to be 24 receipts dated various dates and signed by the Alleged Staff and the Father acknowledging receipts of their respective salaries.

16. We are satisfied on a balance of probabilities that all the alleged receipts were not contemporaneous. The appellant admitted at the hearing that all 24 receipts were written out at the same time. The following summary shows that they were created after the event:

Date	No	By	Amount (RMB)	Salary for
8-4-2001	83640	Father	3,000	April
10-4-2001	83624	Alleged Staff	3,500	April 2001
8-5-2001	83625	Alleged Staff	3,000	Salary after deducting loan of 500
9-5-2001	83641	Father	3,000	May
9-6-2001	83642	Father	3,000	June
11-6-2001	83626	Alleged Staff	3,500	June 2001
8-7-2001	83627	Alleged Staff	3,500	July 2001
8-7-2001	83643	Father	3,000	July
8-8-2001	83644	Father	3,000	August
9-8-2001	83628	Alleged Staff	3,000	Salary after deducting loan of 500
8-9-2001	83629	Alleged Staff	3,500	September 2001
8-9-2001	83645	Father	3,000	September
8-10-2001	83646	Father	3,000	October
10-10-2001	83630	Alleged Staff	3,500	October
1				
9-11-2001	83647	Father	3,000	November
12-11-2001	83631	Alleged Staff	3,500	November 2001
1				

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9-12-2001	83648	Father	3,000	December 2001
10-12-200	83632	Alleged Staff	3,500	December 2001
1				
8-1-2002	83633	Alleged Staff	3,500	January 2002
8-1-2002	83649	Father	3,000	January 2002
8-2-2002	83634	Alleged Staff	3,500	February 2002
8-2-2002	83650	Father	3,000	February 2002
8-3-2002	83638	Father	3,000	<b>February 2001</b>
9-3-2002	83635	Alleged Staff	3,500	March 2002

17. Section 68(4) of the Inland Revenue Ordinance, Chapter 112, provides that the onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.

18. Section 16(1) provides for deduction of all outgoings and expenses to the extent to which they were incurred during the Basis Period by the appellant in the production of profits in respect of which she was chargeable to profits tax for any period. By virtue of section 17(1)(a), no deduction shall be allowed in respect of domestic or private expenses.

19. Whether or not the appellant did incur the alleged expenses; whether or not the alleged expenses were incurred during the Basis Period and whether or not the alleged expenses were incurred in the production of profits are questions of fact. The onus is on the appellant.

20. We are not satisfied on a balance of probabilities that the appellant had incurred any of the four sums claimed or any part thereof. Various versions which are difficult to reconcile have been put forward. No attempt had been made to explain the changes in versions. There is no contemporaneous document proving or evidencing the incurring or payment of the alleged expenses. In our view, both the appellant and the Sister were not credible witnesses.

21. According to the letter dated 10 October 2003 written by Mr A of Accounting Company C on behalf of the appellant:

- (a) the appellant agreed to pay commission to 'those sub-agents for the successfully concluded policies they introduced to our client';
- (b) the 'rate' of commission 'depended on the extent of the work they involved' ;
- (c) the payments were 'made by cash'; and
- (d) an alleged office in City D was 'mainly used by our client, her sub-agents and her PRC employees to carry on the insurance business' .

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22. However, according to the letter dated 8 October 2004 written by Mr A of Accounting Company C on behalf of the appellant:

- (a) the appellant had to pay commission to those sub-agents for introducing customers to her;
- (b) the Sister and the Father were 'domiciled' in Province E (of China mainland) 'which was quite far away from' City D and the customers in Province E 'were referred and handled by [the Sister] and [the Father]'.

23. The alleged written agreement allegedly made between the Firm and the Sister and said to be signed on 28 December 2000 provided that, upon successful introduction of a person to become an official customer, the Sister would get all the commission for the first year. On the basis of this version, there is no question of a 'rate' which 'depended on the extent of the work they involved'.

24. The Sister was evasive on where she allegedly worked and where she allegedly resided during the Basis Period.

25. The Sister claimed that her commission was credited to her bank account. She was evasive about particulars of the bank account, asserting that the account had been closed. Even if an account had been closed, there is no reason why she could not have produced the bank statements for transactions concluded before the closing of the account.

26. The appellant made no attempt to identify her source of funds and how any payment into the Sister's bank account was allegedly made. Her earlier version was that payment was by cash. She made no attempt to give any information on the date when, the place where and the amount in which she allegedly paid the Sister.

27. The Sister had no idea about insurance or the work of an insurance agent or the policies that were written allegedly upon her introduction. What she did, according to what she said in evidence, was that she gave the appellant's cards to potential customers and introduced them to the appellant who would take up the matter from there. On this version, with such a limited involvement, there is also no question of 'the extent of the work they involved'.

28. The data supplied by Mr A of Accounting Company C on behalf of the appellant in his letter dated 10 October 2003 differs from the data supplied by InsuranceCo and also differs from the data shown in the 16 copy policy information issued by InsuranceCo and produced by the appellant at the hearing. No attempt had been made to reconcile the differences. On the appellant's own data, the commission to the Sister was lower or substantially lower than the commission which she earned from InsuranceCo in five of the 12 cases. The appellant tried to wrangle out of this by asserting that the Sister would not know and would have no means of

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knowing how much she was paid by InsuranceCo. She seemed to have forgotten her emphasis earlier that everything depended on trust.

29. Even if any expense had been incurred in respect of the Sister, we are not satisfied on a balance of probabilities that such expense was incurred in the production of profits and was not a domestic or private expense.

30. One policy said to be introduced by the Alleged Staff was written after the end of the Basis Period. This person had not become a customer during the Basis Period.

31. We turn now to the sum of \$61,000.

32. No particulars had been given in respect of any of the payments said to have been paid to the Alleged Staff as alleged commission.

33. The Alleged Staff is also said to have received \$42,000 as salary.

34. One curious feature of the alleged receipts for salary which had never been explained was that salary was said to have been paid in advance well before the end of the month.

35. It would appear from the alleged written agreement allegedly made between the Firm and the Alleged Staff that the Alleged Staff was employed on about 28 December 2000 at an annual salary of RMB42,000. The amount does not reconcile with the amount of HK\$42,000 claimed by the appellant.

36. In the appellant's financial statements for the year before the Year of Assessment, the appellant claimed to have incurred \$36,000 as salary for the Alleged Staff as a secretary. If the Alleged Staff was not employed until about 28 December 2000, salary for three months, that is about RMB 10,500, should have been incurred in respect of the Alleged Staff for the year ended 31 March 2001. No explanation had been offered.

37. No particulars had been given in respect of any of the payments said to have been paid to the Alleged Staff as alleged salary.

38. The last item is \$36,000 said to be the Father's salary.

39. According to the letter dated 10 October 2003 written by Mr A of Accounting Company C, the alleged office in City D was mainly used by the appellant's 'PRC employees' and the Father was responsible for clerical works for 5½ days per week. When Mr A wrote his letter dated 8 October 2004 one year later, the Father was said to be 'domiciled' in Province E; customers in Province E were said to be 'referred and handled by [the Sister] and [the Father]';



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and the Father was paid \$36,000 ‘as a clerk to assist [the appellant’ s] business **in** [Province E] (emphasis added)’.

40. In the accounting documents sent with the Returns for the Year of Assessment, the Father was said to have been a ‘Clerk – PRC’.

41. Under the alleged written agreement allegedly made between the Firm and the Father, the Father was employed on about 28 December 2000 to be in charge of business at an annual salary of RMB36,000. The amount does not reconcile with the amount of HK\$36,000 claimed by the appellant.

42. In the appellant’ s financial statements for the year before the Year of Assessment, the appellant claimed to have incurred \$30,000 as salary for the Father as a clerk. If the Father was not employed until about 28 December 2000, salary for three months, that is about RMB 9,000, should have been incurred in respect of the Father for the year ended 31 March 2001. No explanation had been offered.

43. No particulars had been given in respect of any of the payments said to have been paid to the Father as alleged salary.

44. Even if any expense had been incurred in respect of the Father, we are not satisfied on a balance of probabilities that such expense was incurred in the production of profits and was not a domestic or private expense.

45. For reasons given above, the appellant has failed to discharge her onus of proving that the assessment appealed against is excessive or incorrect.

46. We dismiss the appeal and confirm the assessment as reduced by the Deputy Commissioner.