

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D126/97

Profits tax – taxability of the profits arising from the disposal of property.

Panel: Ronny Wong Fook Hum SC (chairman), Gregory Robert Scott Crichton and Duncan A Graham.

Date of hearing: 10 December 1997.

Date of decision: 27 March 1998.

The taxpayers ('Mr and Mrs A') are husband and wife. On 8 July 1991, Mr A entered into a sub-sale agreement for the purchase of a flat in Garden I (Flat G) for \$1,625,000. Mr A completed this purchase on 15 August 1991. On the same day the flat was charged in favour of Bank J.

On 20 July, Mr and Mrs A entered into an agreement for the purchase of another flat in Garden I (Flat H) for \$1,590,000. Flat H was about the same size as Flat G. This purchase was completed two days later. On the same day the flat was charged in favour of Bank K for \$1,192,000.

On 18 November 1991, Mrs A purchased Flat L for \$1,586,000.

On 7 March 1992, Mr and Mrs A sold Flat H for \$2,365,000. They therefore held this flat for slightly over eight months.

Mr A asserted that both Flat G and Flat H were purchased for use as their family home and as the home of Mrs A's father. Further both properties were later sold because Mr A was approved to migrate to Country C on 24 September 1991 and they need to realise money from the sales in order to buy a house in Country C. Moreover, they alleged that they have had no record of trading in properties.

Held:

- (1) The Board has to ascertain the intention of Mr and Mrs A at the time when Flat H was purchased. The Board has to be satisfied that this intention is on the evidence 'genuinely held, realistic and realisable'. (All Best Wishes Limited v CIR 3 HKTC 750 applied)

INLAND REVENUE BOARD OF REVIEW DECISIONS

- (2) On the balance of probabilities Flat H was not purchased with the intention of using the same as part of the plan to house the family of Mr and Mrs A and as the home of Mrs A's father because:
- (a) It is improbable for Mr and Mrs A, who placed the welfare of their children at their fore-front, to move the whole family to District P and sever their children's educational roots. The Board further rejected their evidence of attempts to locate schools in District Q. The difficulties in securing places in those schools are notorious;
 - (b) The readiness of Mrs A in purchasing Flat L militates against an urgent financial needs for purchase in Country C; and
 - (c) The family did not really attempt to settle in Country C until 1995.

Appeal dismissed.

Case referred to:

All Best Wishes Limited v CIR 3 HKTC 750

Cheung Lai Chun for the Commissioner of Inland Revenue.
Taxpayers in person.

Decision:

The Background

1. The Taxpayers ('Mr and Mrs A') are husband and wife. They have two daughters – the elder one born on 14 September 1980 and the younger one on 24 January 1983. Mr A works as an accountant with specialisation in internal auditing.
2. By an agreement dated 10 April 1987, Mr A purchased Flat B for \$1,584,691. The occupation permit for Flat B was issued on 14 October 1987. Mr A and his family moved into that flat which was of an area of 1,533 square feet.
3. In 1989, Mr A lodged his first application for emigration to Country C. The application was unsuccessful.
4. On 1 July 1989, Mrs A and her father Mr D acquired as joint tenants of Flat E. Flat E had a floor area of 569 square feet. Mr D was then about 68 years of age.

INLAND REVENUE BOARD OF REVIEW DECISIONS

5. Mr A lodged two further applications for emigration to Country C in 1990. His second application was made before 30 July 1990. This was again unsuccessful. His third application was made on 12 December 1990.
6. By an agreement dated 16 April 1991. Mr A disposed of Flat B. The family moved to Flat F. This Flat F was rented by Mr and Mrs A for a period of two years at a monthly rent of about \$10,000 to \$12,000. Flat F had a floor area of about 1,100 square feet.
7. On 8 July 1991, Mr A entered into a sub-sale agreement for the purchase of a flat in Garden I (Flat G) for \$1,625,000. Flat G had a floor area of about 800 square feet. Mr A completed this purchase on 15 August 1991. On the same day the flat was charged in favour of Bank J.
8. On 20 July 1991, Mr and Mrs A entered into an agreement for the purchase of another flat in Garden I (Flat H) for \$1,590,000. Flat H was about the same size as Flat G. This purchase was completed two days later. On the same day the flat was charged in favour of Bank K for \$1,192,000.
9. By letter dated 23 July 1991, Mr A was informed by Country C Consulate General that his application for entry to Country C for settlement may proceed. The application was duly approved on 24 September 1991.
10. On 11 November 1991, Mr A sold Flat G for \$2,180,000. The sale was completed 10 days later on 21 November 1991. Flat G was therefore held by Mr A for slightly over four months.
11. On 18 November 1991, Mrs A purchased Flat L for \$1,586,000. At the time of her purchase, Flat L was still under construction. The purchase was completed by Mrs A on 20 June 1992.
12. Pursuant to the visa granted to the family on 24 September 1991, Mr A and his family landed in Country C on 1 February 1992. Shortly thereafter Mr and Mrs A entered into negotiations with Bank M for a foreign currency loan in Hong Kong dollar equivalent to finance their purchase of a piece of property in Country C.
13. On 7 March 1992, Mr and Mrs A sold Flat H for \$2,365,000. They therefore held this flat for slightly over eight months. They paid a total of 9 instalments of \$13,176.4 each in favour of Bank K under the charge over this property.
14. In May 1993, Mr A and his family moved from Flat F to Flat N. Flat N was a quarter provided by Mrs A's employer who took a two year tenancy for that flat. It had a floor area of 1,099 square feet.
15. On 28 July 1993, Mrs A sold Flat L for \$1,890,000. She held this flat for slightly over a year and a half.

INLAND REVENUE BOARD OF REVIEW DECISIONS

16. The couple made enquiries in December 1993 with two schools in Country C for school places for their two daughters for the year 1995. They received tentative offers from both schools. A firm offer was made by a third school in May 1994.

17. Mr D became indisposed in 1994. He was admitted into hospital in July and November 1994 suffering from cancer. He was again admitted into hospital in November 1995. Mr D passed away on 9 March 1997.

18. The issue before us relates to the taxability or otherwise of the profits arising from the disposal of Flat H.

Case of Mr and Mrs A in their correspondence exchanged with the Revenue

19. Mr A asserted in a letter dated 15 February 1994 that:

- a. 'Both (Flats G and H) were purchased for use as residence. One was intended for my wife and children, and the other for my father-in-law. The intention of such arrangement is to enable my wife to live close to her father who was in deteriorating health, and at the same time provide room to accommodate her father in a nearby flat. This was because rooms were not enough in one flat, for the use of my family and my father-in-law.'
- b. 'Both properties were later sold because I was approved to migrate to Country C on 24 September 1991 and then decided to buy a house there.'
- c. 'As the forementioned residential properties were the only properties owned by me in Hong Kong following sale of my previous residence in early 1991. That was "change of residence" and of capital nature. In addition, I had no prior record of trading in properties.'

20. Mr and Mrs A further maintained that:

- a. During the third quarter of 1991, they moved to Flat H. Flats G and H were occupied by Mr D and their family respectively until they were sold in November 1991 and March 1992 for emigration purpose. They built a house in Country C in the second half of 1992 at a cost of \$480,000 in Country C's currency.
- b. The family partly moved to Country C in the first half of 1993. Due to Mr D's medical conditions, their final departure for Country C was deferred to 1995 because Mrs A wanted to look after her father as long as possible. The family moved out of Flat N in early 1995 and moved into their residence in Country C.
- c. Between 1 February 1992 and the first half of 1995, the family stayed at all times in Hong Kong other than several visits a year to Country C.

INLAND REVENUE BOARD OF REVIEW DECISIONS

- d. Between the second half of 1995 and 12 August 1996, they did not stay in Hong Kong except for a few business visits.
- e. Since 12 August 1996, Mr A and his wife have been residing at quarters provided by Mr A's employer in Country O. They travelled weekly to Hong Kong and normally stayed in Hong Kong for less than three days a week. Their daughters travelled quarterly to Hong Kong with stays ranging from three days to two months.

Evidence before us

- 21. The evidence of Mr A:
 - a. Flats G and H were purchased at the demand of Mrs A because the medical condition of his father-in-law had deteriorated very fast and Mrs A thought it was necessary for her to move close to her father.
 - b. At that time their financial conditions were very tight. They didn't have money to pay for the deposits. They had to sell Flat B before they looked for new flat elsewhere.
 - c. Flats G and H were intended as family home. There was no plan to move to Country C at the time of purchase in view of the two failed applications.
 - d. He did not in 1991 rent a flat in District P near Flat E where Mr D was then residing because of the education of his daughters. The daughters were studying on the Island and he couldn't find school places in Kowloon for them. He did not look for places with schools in District P but concentrated with schools in District Q. It was for the same reason that he took a tenancy in Flat N in May 1993.
 - e. His family plan changed after September 1991 when his application for emigration to Country C was approved. There was no point living close to Mr D as the family may emigrate any time when 'places in school in Country C were approved'.
 - f. Flats G and H were sold 'for the purpose of buying a new home in Country C'.
 - g. His family landed in Country C just before the deadline imposed by Country C. The family continued to stay in Hong Kong until 1995 because the search for school took a longer time than expected.
 - h. His wife was financially independent. He himself did not have any record of trading in property.

INLAND REVENUE BOARD OF REVIEW DECISIONS

- i. Mrs A bought Flat L for the purpose of improving the living conditions of Mr D after their emigration. Flat L was sold because Mr D refused to move to District T.
22. The evidence of Mrs A:
- a. She worked as an executive in an advertising agency.
 - b. She was the only child of her father. Her mother passed away in 1980.
 - c. She loved her father very much but both of them had strong characters and would quarrel over little things.
 - d. Mr D used to live in District R. After her mother's death, Mr D became a loner and insisted not to live with her.
 - e. At that juncture, Mr D had a very good friend in District R by the name of Mr S. Mr S looked after Mr D for several years before Mrs A managed to convince him to move to Flat E. Mr S purchased a flat nearby.
 - f. When she submitted her application for emigration to Country C in 1989, she tried to persuade Mr D to join her. Mr D refused her invitation.
 - g. She demanded that Flat B be sold. She and her husband decided to purchase two flats in the same estate as she knew that Mr D would 'never wish to live together with me under one roof'.
 - h. She couldn't recall the extent of her contributions towards the down payment of Flat H. The subsequent instalment payments were all made by Mr A.
 - i. The arrangement envisaged was that Mr D would occupy Flat G whilst her family would occupy the other. A Filipino maid would take care of both flats. She would probably sleep in Mr D's flat in Garden I.
 - j. After she failed to convince Mr D to move to Flat H, it was used as an occasional resort house. A few relatives played mahjong there once or twice. It was never let out.
 - k. Mr D's health started to deteriorate in 1992. The delay in moving to Country C arising from search of school places for her daughters suited her personal wish to staying close to her father.
 - l. She was asked about the school applications which allegedly delayed her trip to Country C. It was pointed out to her that she applied in 1992 for places in 1994 and 1995. She explained that she had a hidden agenda in relation to Mr D. She

INLAND REVENUE BOARD OF REVIEW DECISIONS

was also told that it was very difficult to apply for a place in Country C's schools that she picked.

- m. She bought Flat L as it was still her desire to improve the conditions of her father. When she purchased Flat L, she was hoping that she could convince Mr D to move in the company of Mr S. She was however not sure at all that Mr D would accede to her wish. Her plan was frustrated by Mr S's refusal to leave his flat.
- n. Flats G and H were sold because her husband needed to realise money from the sales in order to buy a house in Country C.

The applicable principles

23. The principles are clear. We have to ascertain the intention to Mr and Mrs A at the time when Flat H was purchased. We have to be satisfied that this intention is on the evidence 'genuinely held, realistic and realisable'.

24. As pointed out by Mortimer J (as he then was) in All Best Wishes Limited v CIR 3 HKTC 750:

'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 action speak louder than words.'

Our Decision

25. We are not satisfied on a balance of probabilities that Flat H was purchased with the intention of using the same as part of the plan to house the family of Mr and Mrs A and as the home of Mr D.

26. Mr and Mrs A strike us as a couple who place the welfare of their children at their fore-front. Their decision to emigrate to Country C was prompted by the desire to cater for the future of their daughters. When Flats G and H were purchased, both daughters were being educated in school in Hong Kong. The centre of gravity of the whole family was in Hong Kong near the schools of these two daughters. In these circumstances, we do not accept that they would move the whole family to District P and sever the educational roots of their daughters in Hong Kong. We further reject their evidence of attempts to locate schools in District Q. The difficulties in securing places in those schools are notorious.

27. Mr and Mrs A contend that the move was to ensure that Mr D be properly cared for. We do not see the urgency of such need. Mr D was quite content in Flat E with Mr S. His tie with Mr S is fully reflected by his rejection of Flat L. In these circumstances it is difficult to accept that Mr and Mrs A were prepared to disturb the education of their daughters in order to fulfil the unilateral wish of Mrs A to look after her father.

INLAND REVENUE BOARD OF REVIEW DECISIONS

28. We are also not convinced that the sales of Flats G and H were prompted by the approval on 24 September 1991. The couple and their family landed in Country C at the last possible moment in February 1992. The readiness of Mrs A in purchasing Flat L militates against any urgent financial needs for purchase in Country C. There is also evidence of negotiations with Bank M for a loan in Hong Kong dollars to support the purchase of the property in Country C. The family did not really attempt to settle in Country C until 1995. Their reason for the delay arising from search of school places is inconsistent with the documentary evidence. The applications for school places were made in late 1993. They were for places in 1994 and 1995.

29. We respect the affection of Mrs A towards her father which she described in moving terms before us. She candidly admitted her clash of personality with Mr D and the very thrifty life which Mr D had chosen to live. Her plans for Mr D, whilst well-intentioned, give us the impression that the same were unsettled and loosely formulated.

30. For these reasons, we would dismiss Mr and Mrs A's appeal.