INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D129/00

Penalty tax – real property – whether the gains arising from the disposal of properties were liable for profits tax – section 68(4) of the Inland Revenue Ordinance (' IRO').

Panel: Anthony Ho Yiu Wah (chairman), Colin Cohen and Kenneth Ku Shu Kay.

Date of hearing: 19 January 2001.
Date of decision: 26 February 2001.

The taxpayer, a company incorporated in Hong Kong, was notified that it had been assessed to additional profits tax for the years of assessment 1994/95 to 1997/98. The additional assessable profits in question were derived from the taxpayer' s sale of certain shop units and car parking spaces in a property development.

A director of the taxpayer gave evidence and said that ' the taxpayer had a general policy or practice to build residential units and sell them all out but to retain the shopping arcade and car park facilities for rental' . The director failed to make any positive assertion as to the intention of the taxpayer in the present case. However, the director admitted in his cross-examination that ' at suitable timing, the taxpayer would make decision as to whether the property was for sale or for long term investment' . The taxpayer' s former tax representative previously stated that the taxpayer' s general policy was ' to redevelop properties for resale' .

A manager of the property department of a fellow subsidiary company of the taxpayer gave evidence and said that there were few documents outlining the plans, strategies and proposals for leasing the shops and carparks because ' leasing would normally go under a flexible and informal course' .

Held:

1. A taxpayer may indeed have different intentions in relation to different parts of the same property. But the onus in still on the taxpayer to show such different intentions. Intention can only be judged by considering all the surrounding circumstances, including things said at the time, before and after and things done at the time, before and after. The stated intention of the taxpayer at the material time cannot be decisive. But the absence of any stated intention of the taxpayer at the material time is a factor the Board need to take into consideration.

2. At the time of acquisition of the development site, the taxpayer had not formed any intention on what to do with the shops and/or the carparks. When it entered into this part of the venture, its intention obviously was to turn the development site to profitable account but it had not done any analysis to determine whether selling or letting would bring more commercial benefit to itself and had not made any decision in this regard. This does not amount to ' intention' to acquire the development site and build the shops and carparks for the purpose of investment.

Appeal dismissed.

Cases referred to:

Simmons v IRC [1980] 1 WLR 1196
All Best Wishes Ltd v CIR 3 HKTC 750
Chinachem Investment Co Ltd v CIR [1987] 2 HKTC 261
Hillems & Flowler v Murray [17TC77]

Lee Yun Hung for the Commissioner of Inland Revenue.
Neil Thomson Counsel instructed by Messrs Peter C Wong Chow & Chow for the taxpayer.

Decision:

Introduction

1. This is an appeal against the determination of the Commissioner of Inland Revenue dated 1 June 2001. In that determination, the Commissioner :

(1) confirmed the additional assessable profits for the year of assessment 1994/95 of $106,444 with tax payable thereon of $17,563;

(2) confirmed the additional assessable profits for the year of assessment 1995/96 of $7,354,460 with tax payable thereon of $1,213,486;

(3) confirmed the additional assessable profits for the year of assessment 1996/97 of $14,829,591 with tax payable thereon of $2,446,882; and

(4) confirmed the assessable profits for the year of assessment 1997/98 of $9,592,485 with tax payable thereon of $1,582,760.

2. The assessable profits or additional assessable profits in question were derived from the Taxpayer' s sale of certain shop units and car parking spaces in a property development called ' Estate A' (hereinafter called ' Estate A Shops' and ' Estate A Car Parks'). The Taxpayer' s case is that the Estate A Shops and Estate A Car Parks were its capital assets and that therefore commercial building allowances should be given to the Taxpayer in respect of the Estate A Shops and Estate A Car Parks and that profits arising from their sale were non-taxable capital gains.

The facts

3. The following statement of facts in the determination are agreed by the Taxpayer and we find them as facts.

4. The Taxpayer was incorporated as a private company in Hong Kong on 23 November 1966. Its principal activities are share investment, property investment and development.

5. At all relevant times, the ultimate holding company of the Taxpayer was a company incorporated in Hong Kong (hereinafter called ' Hold Co').

6. On 28 June 1991, the Taxpayer and five other companies acquired District B Lot by a surrender of land exchange entitlements and they jointly developed the site. The respective shares of interest of these companies in the project are as follows :

Name of companies	**Relationship**	**Percentage of interest**
Taxpayer		10.68%
Company C	Subsidiary	6.61%
Company D	Related company	1.72%
Company E	Fellow subsidiary	64.63%
Company F	Related company	15.57%
Company G	Related company	0.79%
		100.00%

7. The site at District B Lot was developed into a residential estate called ' Estate A' with a shopping arcade and carparking facilities. The total development cost was allocated to various units according to their undivided shares in the Deed of mutual covenant (' DMC') as follows :

Unit	**Undivided shares in DMC**	**Total development cost**
		$
Residential Block 1	177,548	10,352,051.92

Residential Block 2	204,158	11,903,565.33
Residential Block 3	185,507	10,816,106.61
Residential Block 4	204,158	11,903,565.33
Carparking spaces	14,807	863,331.79
Shopping arcade	87,439	5,098,187.92
Total	873,617	50,936,808.90

8. Estate A on completion has the following shop units and carparking spaces :

(a) Shops A1 to A151 on G/F;

(b) Shops B1 to B195 on 1/F;

(c) Car parking space nos AP1 to AP37 on G/F;

(d) Car parking space nos BP1 to BP7 on 1/F; and

(e) Car parking space nos CP1 to CP177 on 2/F.

9. The permit to occupy Estate A was issued on 10 June 1994.

10. (a) On 10 March 1993, the residential units in Residential Block 3 were offered for sale.

(b) On 28 June 1994, the residential units in Residential Block 4 were offered for sale.

(c) On 6 August 1994, the residential units in Residential Blocks 2 and 3 were offered for sale.

11. (a) On 3 November 1995, the Estate A Shops were offered for sale to the public.

(b) On 29 April 1997, the Estate A Car Parks were offered for sale to the public.

12. In its accounts, the Taxpayer recorded the following income and expenses :

Income	**1994/95**	**1995/96**	**1996/97**	**1997/98**
	$	$	$	$
Sale of properties	268,681,327	87,274,457	9,815,218	266,077
Less: Cost of properties sold	48,962,019	19,721,344	2,004,748	51,849
	219,719,308	67,553,113	7,810,470	214,228

Less: Selling expenses	9,100,800	3,774,330	907,091	5,517
	210,618,508	63,778,783	6,903,379	208,711
Rental income less outgoings	3,778,017	3,770,505	2,102,522	1,704,776
Dividends received from listed investments	--	1,676,000	1,247,100	3,843,750
Dividends received from subsidiary companies	45,940,000	--	--	--
Interest income	2,144,130	326,140	790,375	42,284
Profit on resale of garments	405,200	188,820	199,025	252,058
Sundry income	203,799	79,677	122,172	103,229
Profit realised from properties sold on instalments basis	10,975,837	88,220	2,683,401	--
Compensation received	15,059	--	--	--
Write back of provision for construction costs	--	--	6,043,725	--
	274,080,550	69,908,145	20,091,699	6,154,808
Less: Expenses				
Administrative and operating expenses	1,077,368	1,063,277	4,086,190	129,528
Donation	10,000,000	--	--	--
Interest expenses	4,788	--	--	--
	11,082,150	1,063,277	4,086,190	129,528
Income	**1994/95**	**1995/96**	**1996/97**	**1997/98**
	$	$	$	$
Profit before exceptional items	262,998,394	68,844,868	16,005,509	6,025,280
Exceptional item:				
- Profit on sale of long term listed investments	16,977,489	3,087,680	4,730,840	35,805,351
-				
- Profit on sale of investment properties	--	7,273,366	23,812,000	7,513,316

Profit before taxation	279,975,883	79,205,914	44,548,349	49,343,947

13. In its profits tax returns, the Taxpayer computed its assessable profits as follows :

	1994/95	**1995/96**	**1996/97**	**1997/98**
	$	$	$	$
Profit before taxation	279,975,883	79,205,914	44,548,349	49,343,947
Add: Winding-up expenses of a subsidiary	15,000	--	--	--
Balancing charge industrial building	--	--	511,519	--
	279,990,883	79,205,914	45,059,868	49,343,947
Less: Dividend	45,940,000	1,676,000	1,247,100	3,843,750
Surplus on liquidation of a subsidiary	--	--	--	58,351
Industrial building allowance	3,246	3,247	--	--
Profit on sale of long term list investments	16,977,489	3,087,680	4,730,840	35,805,351
Profit on sale of investment properties				
- Estate A	--	7,273,366	14,802,000	7,513,316
- Others (transfer to subsidiary)	--	--	9,010,000	--
Commercial building allowance				
- Estate A	106,444	81,094	27,591	16,647
- Estate H	44,010	44,010	44,010	44,010
Offshore interest	--	--	468,617	--
Assessable profits	216,919,694	67,040,517	14,729,710	2,062,522

14. The assessor raised the profits tax assessments for the years of assessment 1994/95 to 1996/97 on the Taxpayer based on the returned profits in Fact 13. The Taxpayer did not object against the profits tax assessments for the years of assessment 1994/95 to 1996/97.

15. Having examined the facts of case, the assessor came to the view that Estate A Shops and Estate A Car Parks were the trading stock of the Taxpayer. On divers dates, the assessor raised on the Taxpayer the following assessments :

(a) Year of assessment 1994/95 (additional)

	$
Commercial building allowances disallowed - Estate A	106,444
Additional assessable profits	106,444
Tax payable	17,563

(b) Year of assessment 1995/96 (additional)

	$
Profits from sale of shop units in Estate A	7,273,366
Commercial building allowances disallowed - Estate A	81,094
Additional assessable profits	7,354,460
Tax payable	1,213,486

(c) Year of assessment 1996/97 (additional)

	$
Profits from sale of shop units in Estate A	14,802,000
Commercial building allowances disallowed - Estate A	27,591
Additional assessable profits	14,829,591
Tax payable	2,446,882

(d) Year of assessment 1997/98

	$
Profits per return	2,062,522

Add: Profits from sale of shop units and car parking spaces in Estate A	7,513,316
Commercial building allowances disallowed - Estate A	16,647
Assessable profits	9,592,485
Tax payable	1,582,760

16. Company I objected, on behalf of the Taxpayer, against the additional profits tax assessments for the years of assessment 1994/95 to 1996/97. The Taxpayer also objected by itself to the profits tax assessment for the year of assessment 1997/98. The ground of objection is that the Estate A Shops and the Estate A Car Parks were capital assets. Thus, the Taxpayer claimed that commercial building allowances should be given on the unsold WOG Shop and Estate A Car Parks and the profits on their sale should be excluded from assessment.

17. Company I when corresponding with the assessor made the following assertions :

(a) ' From the very inception, the shopping arcade was planned to be a capital investment and was expected to earn rental income for the company steadily. Following the issue of occupation permit, our client appointed a leasing agent on 17 August 1994 to negotiate with and procure tenants. A copy each of the minutes authorizing the appointment of leasing agent and the letter of appointment are enclosed.'

(b) ' Our client made every effort to seek prospective tenants through the leasing agent to take up vacant shops but the market response was disappointing. As time passes, the situation did not improve. Only one arcade shop was successfully let out and this single tenant obtained also did not want to sign a long lease. Copies of offer letters to the tenant are enclosed.'

(c) ' Because of the difficulty in renting out the shops, our client after waiting for tenants for more than a year, decided to sell them rather than leaving them vacant and without generating any rental income. At the same time, our client was still looking for tenants. Attached herewith are some copy letters and internal memos. The shops were first offered for sale on 3 November 1995 and they were never offered for sale during the course of construction or after the issue of the occupation permit.'

(d) ' As no rental offer had been received by the company, the shops were sold in vacant state.'

(e) ' As at 31 March 1996, the gross floor area of the unsold arcade shops was 63,089 square feet. After the year end date, some of the shop units were successfully leased out ….'

(f) ' The original intention of the companies was to develop the property into residential units for sale and a shopping arcade for earning rental income.'

(g) ' After the issue of occupation permit on 10 June 1994, the company appointed a leasing agent in August 1994 to procure tenants for the shops.'

(h) ' The company offered the residential units for pre-sale in early 1993.'

(i) ' The company jointly with the other companies acquired the land on 28 June 1991. The land cost and the development cost were financed from interest free advances by fellow subsidiary companies, proceeds from sale of residential units and short-term bank loan.'

(j) ' The shops and the carparks were offered for lease in August 1994 but no units were let until September 1995. On 6 September 1995 one shop was leased for a short period of time.'

(k) ' The company had made every effort to procure tenants but no tenants could be found and that state of affairs continued for more than one year. The company then decided to dispose of them rather than letting them vacant without generating any income. The first sale took place on 3 November 1995.'

(l) ' The joint venture parties only orally agreed to sell the shops and carparks. No formal written document was available and no valuation was done.'

(m) ' From the very inception, the residential units were intended to be for sale and the shopping arcade and carparking spaces were to be held and retained as investment properties.'

(n) ' Upon completion of properties, that part of the development cost attributable to the residential units was transferred to the property trading account and that part attributable to the shopping arcade and carparking spaces retained was capitalised and transferred to fixed assets from Property under development. Accordingly, when the residential units were offered for sale, none of the shops and carparking spaces were included in the price list because they were to be kept as investment for rental income.'

(o) ' As there has never been any change of intention in relation to the properties, the shops and carparking spaces retained have at no time formed part of the trading stock of the company.'

The appeal

18. The Commissioner agreed with the views of the assessor and made her determination accordingly on 1 June 2000.

19. By letter dated 7 June 2000, Company I lodged a formal notice of appeal on behalf of the Taxpayer.

The evidence

20. At the hearing before the Board, the Taxpayer was represented by Counsel, Mr Neil Thomson, while the Commissioner of Inland Revenue was represented by Mr Lee Yun-hung, chief assessor. Mr J and Mr K gave evidence for the Taxpayer and were cross-examined by the Commissioner' s representative.

21. Mr J is and has been a director of the Taxpayer since December 1989. Except for that part of his testimony dealing with the intention of the Taxpayer at the time of acquisition of the property which will be set out in paragraph 23 below, the important parts of the testimony given by Mr J can be summarised as follows :

(a) He described the principal activities of the Taxpayer to include ' investments in general, property investments and property development.'

(b) Apart from Estate A at District B, the Taxpayer has engaged in development of other properties, namely, Estate H, another lot and Commercial Centre L.

(c) It has been the practice of the Taxpayer to build the residential units and sell them all out. As for the shopping arcade and car park facilities, it has been the practice of the Taxpayer to retain most of the shopping arcade units and car park facilities for long term investment for rental purposes.

(d) Upon completion of the Estate A project and issue of the certificate of compliance in August 1994, costs were allocated to the residential units, the shopping arcade and the car parks according to the undivided shares (of the land) attributed to such units. The Taxpayer then transferred the costs of the shopping arcade and car parks from the Property under development account to the Investment property account.

(e) The aforesaid allocation and transfer of costs from the Property under development account to the Investment property account was in line with the policy of the Taxpayer.

(f) The certificate of compliance was received by the Taxpayer on 5 August 1994 and on 17 August 1994. A directors' meeting was convened appointing Company E (a fellow subsidiary of the Taxpayer) as leasing agent.

(g) The Taxpayer commenced to lease out the car parks after the certificate of compliance was received and between the period from 30 September 1994 to 31 October 1994, 101 car parks were leased out. This development has a total of 221 car parks. As at today, the Taxpayer still owns and is renting out 119 car parks.

(h) The Taxpayer tried to let out the shops during the year after completion of the property but managed to lease out only one shop on short term basis.

(i) The first sale of the shop units took place on 29 September 1995. Between 29 September 1995 and 27 October 1995, a total of 25 shop units were sold.

(j) On 31 October 1995, the Taxpayer offered the shop units for public sale.

(k) On 29 April 1997, the Taxpayer put up 50 car parking spaces for sale as the price of car parking spaces soared to a very attractive level at the material time. The Taxpayer offered the car parks for sale at $500,000 each and within half a day, all 50 car parks were sold.

(l) The Taxpayer then immediately put up another 50 car parks for sale at an increased price of $600,000 each. Again, these 50 car parks were sold out within half a day.

(m) The Taxpayer then raised the price to $650,000 per car park and managed to sell out only two car parks at that price in September 1997. Further sale of car parks then stopped and the Taxpayer still owns and receives rentals from 119 car parks.

(n) During the period from 1994 to the present day, the financial position of the group of companies to which the Taxpayer belongs can be described as ' cash rich' .

22. Mr K was an assistant manager of the property department of Company E (a fellow subsidiary of the Taxpayer) between the period from February 1980 to 31 December 1991. Since 1 January 1992, he was promoted to the position of manager of Company E. The important parts of the testimony given by him can be summarised as follows :

(a) His present job description is to oversee property and property-related activities of the group of companies to which the Taxpayer belongs ('the Group') but prior to December 1998, he did not oversee matters relating to the leasing of properties of the Group.

(b) Prior to December 1998, the persons in charge of leasing matters for the Group were Mr M, Mr N and Mr O, all of whom have left the employment of the Group.

(c) A document dated 9 November 1995 containing leasing recommendation prepared by Mr N was found by him from the records of the Taxpayer. The leasing recommendation related to the proposed leasing of shop premises in Estate A and Estate H to Company P. The leasing arrangement was not reached as far as Estate A was concerned but Company P has leased Estate H from the Taxpayer.

(d) Prior to September 1995, his responsibilities in relation to Estate A were restricted to sale of residential flats only and he did not receive any instructions to sell the shopping units or the car parks. He was not quite sure of the intention of the Taxpayer in relation to the shop units and the car parks but he thought it would be mainly for rental purposes.

(e) He and his staff were from time to time approached by intended purchasers with enquiries to purchase the shop units and his response was that the Taxpayer was not prepared to sell those shopping units.

(f) In August 1995, the Taxpayer began to sell the shop units because a lot of offers to buy were received but few people indicated a wish to lease the shop units.

(g) Mr K and his staff prepared a number of memoranda in 1997 recommending the pricing and strategy for the sale of the car parks. He explained that the reason for selling the car parks was that there was at that time a lot of unused ground in the vicinity used as parking yards causing the rental for car parks to decline and there was 40% vacancy. But at the same time the sale prices for car parks spaces soared up tremendously. So he recommended to his top management to put up the car parks for sale.

(h) The first tranche of car parks, totaling 50 in number, was sold out in the morning at $500,000 each. Then, a second tranche of 50 car parks, with price increased to $600,000 each was sold out in the afternoon. Then, in around four months, he recommended that a third tranche of car parks be put up for sale at $650,000 each but only two were sold out on this occasion. The reason probably was that the price had gone up to the level which few people could afford.

(i) The document containing leasing recommendation referred to in sub-paragraph (c) above was written by Mr N on an ordinary piece of paper (instead of a standard proposal form used by all departments) because the document was only prepared by Mr N to be presented to Mr M (his immediate superior) and not to the big boss. Apart from the aforesaid document, he could not find any other documents outlining the plans, strategies and proposals for leasing the shops and car parks because ' leasing would normally go under a very flexible and informal course' .

23. (a) The main issue in dispute between the parties in the present case was the question of intention of the Taxpayer in relation to the Estate A Shops and Estate A Car Parks. In this regard, it is important to analyse the evidence adduced by the Taxpayer on this issue. Of the two witnesses called by the Taxpayer, Mr J was apparently more qualified to give evidence on the intention of the Taxpayer as he is and has been a director of the Taxpayer since 1989. Indeed, Mr K readily admitted in his testimony that he was not quite sure of the intention of the Taxpayer in relation to the shop units and the car parks but he thought it would be mainly for rental purposes.

(b) In his evidence in chief, in response to the question whether there was any discussion about the way in which the developed property would be used when the development at District B was contemplated, Mr J asserted that the Taxpayer had the usual or general policy or practice to build residential units and sell them all out but to retain the shopping arcade and car park facilities for rental and that when the development at District B was contemplated, the Taxpayer pursued the same practice. During his cross-examination when he was asked why there was no directors' minutes prepared by the companies concerned in respect of their intention towards the development of the Estate A, Mr J replied :

> ' Our traditional practice was that we did not necessarily have records to confirm our intention for development of the property. At suitable

timing, the company would make decision as to whether this property is for sale or for long term investment.'

(c) During his cross-examination, Mr J was referred to the following statement in a letter dated 26 February 1987 written by the Taxpayer's former tax representative to the Commissioner :

> ' Our client's intention is for resale after redevelopment. It has been our client's general group policy to redevelop properties for resale. Thus our client considered it unnecessary to have Directors' Meetings to support this intention.'

When asked whether the aforesaid statement is still correct, that is, whether it is still the Group's general policy to redevelop properties for resale, Mr J did not offer any explanation why the aforesaid statement made in 1987 by the Taxpayer's former tax representative differed from his own statement that it is the policy or practice of the Taxpayer to build residential units for sale and shopping arcade and car park facilities for rental.

(d) (i) Regarding accounting treatment in the accounts of the Taxpayer for the relevant period, Mr J stated that upon completion of the project and issue of the certificate of compliance (in August 1994), costs of the shopping arcade and car parks were transferred from the Property under development account to the Investment property account.

(ii) The aforesaid transfer was recorded in the audited financial statement of the Taxpayer for the year ended 31 March 1995. The audited financial statement was signed on 2 November 1995 and Counsel for the Taxpayer suggested that the accounting treatment was probably adopted several months beforehand and therefore prior to the sale of any of the shops and car parks (the sale of the first shop took place on 29 September 1995). There was no evidence before the Board as to when the preparation of the financial statement was completed and the Commissioner did not agree to the aforesaid suggestion by the Counsel for the Taxpayer.

(e) Regarding efforts made and results achieved by the Taxpayer in the leasing and sale of the Estate A Shops and Estate A Car Parks, the sequence of events can be summarised as follows :

(i) Prior to the issue of certificate of compliance, no efforts had been made to sell the Estate A Shops and Estate A Car Parks. (compared with the

residential units, the first batch of which was offered for sale on 10 March 1993 and all of which were offered for sale on 6 August 1994).

(ii) Certificate of compliance was received by the Taxpayer on 5 August 1994.

(iii) A directors' meeting of the Taxpayer was held on 17 August 1994 appointing Company E (a fellow subsidiary of the Taxpayer) as leasing agent.

(iv) The Taxpayer commenced to lease out the car parks in September 1994 and between 30 September 1994 and 31 October 1994, 101 car parks were leased out.

(v) Between September 1994 and September 1995, the Taxpayer managed to lease out only one shop on short term basis (total number of shops : 346).

(vi) On 11 August 1995, a proposal was made by the property department of the Taxpayer to its top management recommending the sale of shop units and proposing strategies to be adopted.

(vii) The first sale of the shop units took place on 29 September 1995. Between the period from 29 September 1995 and 27 October 1995, in response to ' unsolicited' offers, a total of 25 shop units were sold.

(viii) On 31 October 1995, all shop units were offered for public sale by the Taxpayer.

(ix) On 9 November 1995, a report was made by a staff member of the leasing department of the Taxpayer recording the interest of Company P to lease certain Estate A Shops and making recommendation thereon.

(x) On 18 April 1997, an advertisement was put up by the Taxpayer in a newspaper offering the remaining shop units for sale.

(xi) On 22 April 1997, a proposal was made by the property department of the Taxpayer to its management recommending the sale of the car parks and proposing strategies therefor.

(xii) On 23 April 1997, the Taxpayer issued a circular inviting owners in the development to purchase car parks.

(xiii) On 29 April 1997 in the morning, 50 car parking spaces were put up for sale at $500,000 each and were sold out within half a day.

(xiv) On 29 April 1997 in the afternoon, 50 car parking spaces were put up for sale at $600,000 each and were sold out within half a day.

(xv) The sale of car parks stopped for several months, the price was then increased to $650,000 for each car park and two car parks were sold at this price in September 1997.

24. We are unable to accept Mr J' s testimony that the Taxpayer had a general policy or practice to build residential units and sell them all out but to retain the shopping arcade and car park facilities for rental and that when the development in the present case was contemplated, the Taxpayer simply adopted the same policy or practice. In his testimony, Mr J mentioned three development projects in which the Taxpayer participated, namely, the District B project forming the subject of this appeal, the Estate H project and Commercial Centre L project. Whilst in the case of the Estate H project, the Taxpayer sold the residential units and retained the commercial units for rental, the Commercial Centre L development was treated as a trading asset of the Taxpayer and income arising therefrom was subject to profits tax. Furthermore, Mr J failed to give satisfactory explanation as to why his statement as to the general policy of the Taxpayer differed from the general policy statement previously made by the Taxpayer' s former tax representative that ' it has been our client' s general group policy to redevelop properties for resale' . The simple truth, we think, is that the Taxpayer did not have any general policy at all. It all depends on the circumstances of each project and a decision would be made after all relevant material information are available before the Taxpayer makes its decision in each case. Indeed, Mr J admitted as such in his cross-examination when he said ' our traditional practice was that we did not necessarily have records to confirm our intention for development of the property. At suitable timing, the company would make decision as to whether this property is for sale or for long term investment' .

25. Much emphasis has been placed by Mr J and Mr Thomson on the accounting treatment in the accounts of the Taxpayer for the relevant period, particularly, the transfer of the costs of the shopping arcade and car parks from the property under development account to the investment property account which was recorded in the audited financial statement of the Taxpayer for the year ended 31 March 1995. The said financial statement was signed on 2 November 1995 and Mr Thomson suggested that the accounting treatment was probably adopted a few months beforehand and before the sale of any of the Estate A Shops and Estate A Car Parks took place. Mr Lee disagreed with Mr Thomson' s suggestion and claimed that the accounting treatment could have been adopted at a date very close to 2 November 1995. There is no evidence before us to show which of Mr Thomson or Mr. Lee was correct in their respective ' speculations' but we do not think that it would make any difference at all. Even if the accounting treatment was adopted say on 2 June 1995 as suggested by Mr Thomson, it would be several months after the project had

been completed, at which time all the residential units had been offered for sale (the last batch was offered for sale on 6 August 1994) and the Taxpayer has not sold any of the Estate A Shops or Estate A Car Parks. Under such circumstances, any ordinary book-keeper would transfer (1) the costs of the residential units from the Property under development account to Properties for sale account; and (2) the costs of the Estate A Shops and Estate A Car Parks from the property under development account to investment property account. We are therefore of the view that such accounting entries are of neutral effect and would not advance the Taxpayer' s case. It certainly did not amount to contemporaneous evidence of the Taxpayer' s intention advocated by Mr Thomson.

26. Except from making certain general statements as to the general policy of the Taxpayer (see paragraph 24 above), Mr J did not actually make any positive assertion as to the intention of the Taxpayer in the present case. Nor was he able to produce any board minutes or other documentary evidence of such intention when the Taxpayer acquired the development site in 1991. Mr Thomson submitted that this gap in the evidential chain should not be a major point to be held against the Taxpayer and that what one can do and should do is to look at what happened once the certificate of compliance was obtained. In this connection, we have considered the evidence of efforts made and results achieved by the Taxpayer in the leasing and sale of the Estate A project (see paragraphs 10, 11 and 23(e) above). We find that insofar as the Estate A Shops were concerned, no efforts had been made at all for the leasing of the shops.

27. Insofar as the Estate A Car Parks were concerned, although substantial leasing did take place, the leasing was on a monthly basis and there was no evidence before us showing that the Taxpayer had done any planning for its leasing program and it appeared to be a case of passive leasing by an owner who merely entertained unsolicited offers. In a development where the ratio is one car park to seven residential flats, leasing out 100 plus car parks which was equivalent to one car park per fifteen residential flats could be easily achieved without any conscious efforts or planning by the owner. In our view, the mere fact that the Taxpayer had leased the Estate A Car Parks prior to their sale in mid-1997 was not sufficient evidence of the Taxpayer' s intention to hold the Estate A Car Parks as capital assets for investment as such leasing could equally be explained as action taken by the Taxpayer to earn rental income while it waited for an opportune time to sell the same at a substantial profit. Mr K explained that the reason for selling the car parks in 1997 was that at the material time there was a lot of unused ground in the vicinity used as parking yards thereby causing a fall in demand and an increase in vacancy rate. There was no evidence before us whether the Taxpayer attempted to find out whether the competition by the neighbouring owners was on a short-term or long-term basis. Nor was there any attempt by the Taxpayer to find out whether user as parking yards by the neighbouring owners was legal or illegal. We find it hard to believe that a developer who had the intention of holding some 200 plus car parks as long term investment property would simply change its strategy without a fight when faced with competition from some obscure neighbouring owners.

28. We also find it impossible to accept Mr K' s explanation that there were few documents outlining the plans, strategies and proposals for leasing the Estate A Shops and Estate A

Car Parks because ' leasing would normally go under a flexible and informal course' . We noted that the project had a total of 346 shops and 231 car parking spaces. With such a large portfolio of shops and car parking spaces, it is difficult to believe that an owner holding it for long term investment purposes would not have any strategic business plans for leasing, including packages for attracting anchor tenants, trade-mix for the shopping arcade, division of the car parking floors into sections for hourly parking and term parking etc. Instead, all Mr K was able to produce as evidence of the leasing efforts of the Taxpayer was a memo dated 9 November 1995 containing leasing recommendation by a staff member of the Taxpayer to his superior related to proposed leasing of certain Estate A Shops to Company P. The so-called leasing recommendation was nothing more than a purported record of expression of leasing interest by Company P. It was purportedly received by the Taxpayer on 9 November 1995 at which time 25 Estate A Shops had been sold by private sale and all the Estate A Shops had been offered for public sale. Furthermore, there was no follow-up action on this memo.

The law

29. Section 68(4) of the IRO, Chapter112, provides that *' the onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant'* .

30. Authorities cited to us included the following well known cases, namely,

Simmons v IRC [1980]1 WLR 1196
All Best Wishes Ltd v CIR 3 HKTC 750
Chinachem Investment Co Ltd v CIR [1987] 2 HKTC 261
Hillems & Fowler v Murray [17TC77]

31. In Simmons v IRC [1980] 1 WLR 1196, Lord Wilberforce said at 1199 :

- *' 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.'*

- *' intentions may be changed. What was first an investment may be put into the trading stock – and, I suppose, vice versa.'*

- *' 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.'

32. In All Best Wishes Ltd v Commissioner of Inland Revenue 3 HKTC 750, Mortimer J stated (at page771) :

' 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 common place 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 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.'

33. We also find guidance from the statements made by Asquith LJ in Cunliffe v Goodman (1950) 2 KB 237 at 253 and 254 as what amounts to ' intention' .

' An intention to my mind connotes a state of affairs which the party intending – I will call him X – does more than merely contemplate : it connotes a state of affairs which on the contrary, he decides, so far is in him lies, to bring about, and which, in point of possibility, he has a reasonable prospect of being able to bring about, by his own act of volition' .

' Not merely is the term "intention" unsatisfied if the person professing it has too many hurdles to overcome, or too little control of events, it is equally inappropriate if at the material time that person is in effect not deciding to proceed but feeling his way and reserving his decision until he shall be in possession of financial data sufficient to enable him to determine whether the project will be commercially worth while.

A purpose so qualified and suspended does not in my view amount to an "intention" or "decision" within the principle. It is mere contemplation until the materials necessary to a decision on the commercial merits are available and have resulted in such a decision.'

Conclusion

34. The authorities cited above show that the question we should ask ourselves is : what was the intention of the Taxpayer in relation to the Estate A Shops and Estate A Car Parks at the time of acquisition of the development site in 1991? At the material time did the Taxpayer intend to build the Estate A Shops and Estate A Car Parks and retain the same for long term investment for rental purposes?

35. Counsel for the Taxpayer made forceful submissions to remind us that a taxpayer may have different intentions in relation to different parts of the same property and that although the absence of board minutes of the taxpayer at the time of acquisition of the development site appeared to be a ' gap in the evidential chain' , this should not be a major point to be held against the Taxpayer. He further submitted that what one can do and what one should do is to look at what happened once the certificate of compliance was obtained.

36. We agree that a taxpayer may indeed have different intentions in relation to different parts of the same property. But the onus is still on the taxpayer to show such different intentions. We also agree intention can only be judged by considering all the surrounding circumstances, including things said at the time, before and after and things done at the time, before and after. It is correct that the stated intention of the taxpayer at the material time cannot be decisive. But the absence of any stated intention of the Taxpayer at the material time in the present case is a factor we need to take into consideration.

37. Having considered all the evidence and the facts before us, we have reached the following conclusions :

(a) We find that the Taxpayer has not discharged the onus of proving that the assessment, in so far as it was based on the premises that the Estate A Shops and Estate A Car Parks were trading assets, was incorrect or that the assessment was otherwise excessive.

(b) Indeed on the whole of the evidence and on the agreed facts, we find that at the time of acquisition of the development site, the Taxpayer had not formed any intention what to do with the Estate A Shops and/or the Estate A Car Parks. When it entered into this part of the venture in 1991, its intention obviously was to turn the development site to profitable account but it had not done any analysis to determine whether selling or letting would bring more commercial benefit to itself and had not made any decision in this regard. This does not amount to ' intention' to acquire the development site and build the Estate A Shops and Estate A Car Parks for the purpose of investment.

38. We therefore dismiss this appeal and confirm the determination of the Commissioner.