

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D143/99

Profits Tax – sale of property – whether profits derived from the sale of the property assessable to profits tax – whether intention to use as matrimonial home genuinely held, realistic and realizable.

Panel: Ronny Wong Fook Hum SC (chairman), Kenneth Chow Charn Ki and William Zao Sing Tsun.

Date of hearing: 20 December 1999.

Date of decision: 21 March 2000.

The first named taxpayer is the mother of the second named taxpayer. The Subject Property was developed jointly by a trustee organization and Company D. The husband of the first named taxpayer was a director of Company C and its various subsidiary/associate companies including Company D. The staff members of Company C were offered in a private sale of the Subject Property. By a memorandum dated 25 May 1993, the taxpayers purchased the Subject Property. At that time, the Subject Property was still under construction.

The Subject Property was assigned in favour of the taxpayers on 23 January 1995. On the following day, they entered into a provisional agreement for sale and purchase disposing the Subject Property. It was the taxpayers' case that the Subject Property was bought for own use, either by the daughter's family or themselves. The issue before the Board is whether the taxpayers are liable to profits tax in respect of the gains they made from the Subject Property.

Held :

1. The Board has to be satisfied by the two taxpayers that their intention in purchasing the Subject Property was to use the same as their residence and such intention is on the evidence 'genuinely held, realistic and realizable' (All Best Wishes Limited v CIR 3 HKTC 750 applied).
2. The Board was not satisfied that the second named taxpayer ever had the intention of using the Subject Property as her matrimonial home. The second named taxpayer did not attend the hearing and the Board has no evidence from her as to the reasons that prompted her choice of the Subject Property. The Board found that the second named taxpayer simply has not begun to discharge the onus of proof that rests squarely on her.

INLAND REVENUE BOARD OF REVIEW DECISIONS

3. Based on the evidence before the Board, the Board found that the Subject Property was totally inadequate for the needs and since the Subject Property was disposed of immediately after compliance with the conditions imposed by Company D pertaining to its alienability, the first named taxpayer was shown to be a shrewd dealer of properties. Given the first named taxpayer's husband's long association with Company C, the Board rejected the first named taxpayer's evidence that the extension of her husband's tenure was wholly unexpected. The Board therefore concluded that the first named taxpayer did not have settled intention to hold the Subject Property on a long term basis.

Appeal dismissed.

Case referred to:

All Best Wishes Limited v CIR 3 HKTC 750

Chan Tak Hong for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

Background

1. The first named Taxpayer ['Mrs A'] is the wife of Mr A. The second named Taxpayer ['Mrs B'] is one of their daughters. Mr A was a director of Company C and its various subsidiary/associate companies including Company D. Initially he was due to retire in 1995. By letter dated 30 January 1995 from Company C, his service was extended to the Chinese New Year of 1997. After 1997, Mr A became a non-executive director of Company C.
2. At all material times, Mr and Mrs A lived and still live in a house at District E ['Property 1']. Property 1 was purchased by Mr A in 1988.
3. Mrs B and her husband resided at a unit in District F ['Property 2'] since 1992. Property 2 is about 1,270 square feet. It was purchased by them on 25 June 1992. They lived there till about July 1994.
4. Building G is a residential complex developed jointly between a trustees organization ['the Trustees'] and Company D. Pursuant to the terms of an agreement dated 31 May 1993, all the car parks in the development are to be retained by the Trustees. The Trustees agree to hold

INLAND REVENUE BOARD OF REVIEW DECISIONS

124 of such car parks as 'the residents' car parks'. Those residents' car parks are let by the Trustees to residents of Building G at prevailing market rent. In the event of sale by the Trustees of the residents' car parks, they are to be offered to the residents at the prevailing market value.

5. By letter dated 12 May 1993, staff members of Company C were informed that units in Building G were being offered to them in a private sale on condition that the unit purchased 'cannot be resold until after the execution of the assignment upon completion of the building.' By an application dated 20 May 1993, Mrs A applied for the purchase of one of those units. Mrs B was designated as her co-owner. The application was successful. Mrs A was so informed on 22 May 1993. By a memorandum dated 25 May 1993, Mrs A and Mrs B purchased a unit in Building G ['the Subject Property'] at a consideration of \$6,880,000. At that time the Subject Property was still under construction.

6. On 29 October 1993, Mrs A, Mrs B and another daughter of Mrs A ['Ms A'] bought a unit and a carparking space in District F ['Property 3'] at \$4,950,000. Property 3 has an area of 1,650 square feet with four bedrooms. It was sold by the three of them on 28 March 1994 for \$8,075,000. In response to query raised by the assessor, Mrs A gave the following explanations in support of her contention that the gains arising from disposal of Property 3 were capital gains:

'[Property 3] was originally planned for purchase for [Mrs B] for residential purposes. She needed a bigger premises to house her parents-in-law, who aimed to come back to Hong Kong to live together after they obtained their citizenship in Country H. My daughter's father-in-law Mr I promised to remit funds to finance the purchase ... Accident did occur. [Mrs B's] father-in-law suddenly had a stroke. He eventually died in Country H on 14 December 1993. [Mrs B] could no longer buy the property in her own right. ... As it was not my intention to buy that property, the property had to be disposed of. That was the reason for sale ...'

7. By an agreement dated 20 July 1994, Mrs B and her husband purchased a unit in District F ['Property 4']. Property 4 is about 2,300 square feet in area. Mrs B has since been residing in Property 4 with her family. Since about 10 October 1994, one of the rooms in Property 4 was used by Mrs B's mother-in-law who returned from Country H.

8. The occupation permit in respect of the Subject Property was issued on 23 December 1994. In late January 1995, Mr A sought and obtained from a finance company a loan of \$5,538,034 for the purpose of settling the balance of the purchase price in respect of the Subject Property. The Subject Property was assigned in favour of Mrs A and Mrs B on 23 January 1995. On the following day, they entered into a provisional agreement for sale and purchase disposing the Subject Property for \$11,300,000. The issue before us is whether the two of them are liable to profits tax in respect of the gains they made from the Subject Property.

INLAND REVENUE BOARD OF REVIEW DECISIONS

Previous decision of this Board in relation to Property 3

9. Mrs A, Mrs B and Ms A challenged the profits tax assessment raised on them in respect of Property 3. Their appeal was heard by this Board in September 1998. Only Mrs A appeared at the hearing. By its decision dated 22 December 1998, this Board (differently constituted) took the view that ‘*This being a case of co-ownership by tenants-in-common, the long-term-investment intention and the ability to carry it into effect must be proved in respect of each appellant individually and in respect of all three appellants collectively.*’ The Board held that Mrs B lacked the ability to carry into effect a long-term investment intention. The Board further held that neither Mrs A nor Ms A had any intention of taking up part-ownership of the property on a long-term basis. Their contributions totalling 90% of the purchase cost were meant to be temporary loans. The Board dismissed the appeal of Mrs A, Mrs B and Ms A.

Case of Mrs A and Mrs B in relation to the Subject Property as gleaned from their correspondence with the Revenue

10. In her letter to the Revenue dated 5 June 1997, Mrs A asserted that ‘When we bought [the Subject Property], it was meant for own use, either by my daughter’s family or ourselves.’ She went on to explain that the intention to use the Subject Property as Mrs B’s residence was frustrated by the vesting of all car parks in Building G in the Trustees. Mrs B’s husband is an architect. It is essential for him to keep a car at his disposal. As far as the intention to use the Subject Property as her residence is concerned, that too was thwarted by the sudden decision of Company C in extending the directorship of Mr A. As Company C’s director, Mr A would continue to enjoy a substantial housing allowance. The Subject Property would also be too small for their social needs.

The sworn testimony of Mrs A before us

11. Mrs B did not attend this appeal. The only *viva voce* evidence came from Mrs A.

12. According to the testimony of Mrs A:

- (a) She has four children, two sons and two daughters. Her sons (born in 1968 and 1971) received their education overseas. After their graduation, they returned to Hong Kong in about the mid eighties and resided in Property 1. Property 1 is 3,000 square feet in area with five bedrooms and a garden. She is still residing in Property 1.
- (b) Mr A joined Company C in about 1958. Shipping was his major responsibility although he was also one of the directors of Company D between 1992 to 1995.

INLAND REVENUE BOARD OF REVIEW DECISIONS

- (c) The in-laws of Mrs B emigrated to Country H in about 1990. They obtained their citizenship in about 1993.
- (d) In about May 1993, Mrs B' s father-in-law repeatedly suggested that he would pay for the acquisition of a property if Mrs B and her family would live with the in-laws.
- (e) Mrs B was also an employee of Company C. Mrs A decided to submit the application in their joint names so as to improve the chance of allocation and to give Mrs B the choice. She frankly admitted that her plot was to secure payment by Mrs B' s father-in-law of the Subject Property. Mrs B would then own Property 2 and the Subject Property. She could take up the Subject Property should the same be rejected by Mrs B.
- (f) She paid the initial 20% deposit for the purchase of the Subject Property. Mrs B would only contribute should she decide to take the Subject Property. She would be prepared to make a gift of this 20% deposit to Mrs B.
- (g) When she purchased the Subject Property, she heard rumours that car parks in Building G would be available for sale. Mr A was not involved in the day-to-day running of Company D. She learned from the newspapers the vesting of all the car parks in the Trustees.
- (h) The non-availability of car parks and lack of finance led to Mrs B' s rejection of the Subject Property.
- (i) Mr A' s family has a long association with Company C. There were discussions with Company C' s overseas office several months prior to 30 January 1995 concerning the extension of Mr A' s directorship.

The applicable principles

13. As pointed out by the decision of this Board in the context of Property 3:

'The taxability or otherwise of a profit derived by a person from the sale of an asset turns on his intention at the time of its acquisition. If the intention was to dispose of it at a profit, the asset was a trading asset, and the profit is a trading profit and is taxable. If the intention was to hold it as a long-term investment, the asset was a capital asset, and the profit is a capital gain and is not taxable.'

INLAND REVENUE BOARD OF REVIEW DECISIONS

14. We have to be satisfied by Mrs A and Mrs B that their intention in purchasing the Subject Property was to use the same as their residence and such intention is on the evidence ‘genuinely held, realistic and realisable’.

15. In ascertaining the intention of Mrs A and Mrs B, we have borne in mind the oft-quoted guidance of 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 actions speak louder than words.’

Our decision

16. We are not satisfied that Mrs B ever had the intention of using the Subject Property as her matrimonial home. Mrs B did not attend the hearing before us. We have no evidence from her as to the reasons that prompted her choice (if she did in fact choose) of the Subject Property. No car park was purchased together with the Subject Property. We would expect some explanation from Mrs B as to why she was prepared to opt for the Subject Property given the importance to Mr B to have a car at his ready use. We have not heard from Mrs B as to her source of finance. She simply has not begun to discharge the onus of proof that rests squarely on her.

17. Our overall impression is that Mrs A is the master mind behind the acquisition. She is the only person who has any real interest in the pursuit of this appeal.

18. We are of the view that at no stage did Mrs A have the intention of using the Subject Property as her matrimonial home. She moves in high circles. The Subject Property was totally inadequate for the needs. She had to cater for the possibility of the return of her two sons. She had to meet the entertaining demands inherent in the position of Mr A. Given Mr A’s long association with Company C, we reject Mrs A’s evidence that the extension of Mr A’s tenure was wholly unexpected. She is still staying in Property 1. There is no suggestion of any move after cessation of Mr A’s tie with Company C. The Subject Property was disposed of immediately after compliance with the conditions imposed by Company D pertaining to its alienability. Despite her protestations, her involvement in Property 3 shows she is a shrewd dealer of properties. We have no hesitation in concluding that she did not have settled intention to hold the Subject Property on a long term basis.

19. For these reasons, we dismiss the appeal of Mrs A and Mrs B.