INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D20/98

Profits tax – sale of property – whether profits derived from the sale of the property assessable to profit tax – whether intention at the time of acquisition – genuine held, realistic and realizable"

Panel: Kenneth Kwok Hing Wai SC (chairman), Raphael Chan Cheuk Yuen and Alfred Chow Cheuk Yu.

Dates of hearing: 12 and 16 January 1998.
Date of decision: 30 April 1998.

On 27 December 1990, the taxpayer entered into a formal agreement to purchase Property B which was under construction at the time of purchase. Property B was assigned to the taxpayer by an assignment dated 6 April 1992. By a provisional agreement dated 7 April 1992, the taxpayer contracted to sell Property B and the sale was completed by an assignment dated 6 May 1992. By agreement for sale and purchase dated 18 July 1992, the taxpayer agreed to purchase Property D which was then still under construction. By an agreement for sub-sale and purchase dated 18 January 1994, the taxpayer agreed to sell Property D and the sale was completed by an assignment to the sub-purchaser dated 27 January 1994, with the taxpayer joining in as a confirmor.

The assessor was of the opinion that the respective purchases and sales of Property B and Property D amounted to adventures in the nature of trade. The taxpayer's case was that the profits in dispute were capital gains rather than trading gains and the acquisition of Property B and D were acquired for self-residence. The subsequent sale of Property B was because of the transportation problems whereas the subsequent sale of Property D was because of not enough living space.

Held: The taxpayer impressed the Board as an unreliable witness, telling lies in an attempt to explain the nil or nominal electricity consumption at Property B; and in an attempt to explain his quick sale of Property D, joining in the assignment as the confirmor. On the evidence, the Board found that the alleged intention to acquire and hold Property B as a capital asset could not have been genuinely held, realistic or realisable, even on the taxpayer's own case. The Board rejected the assertion of the taxpayer that the purchase of Property B and D were for self-residence.

Appeal dismissed.

Ngan Man Kuen for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

1. This is an appeal against the determination dated 25 June 1997 by Commissioner of Inland Revenue, rejecting the Taxpayer's objection against:

(a) the profits tax assessment for the year of assessment 1992/93 dated 14 March 1996 showing assessable profits of $670,000 with tax payable thereon of $100,500, and

(b) the profits tax assessment for the year of assessment 1993/94 dated 14 March 1996 showing assessable profits of $410,000 with tax payable thereon of $61,500.

2. The Commissioner revised:

(a) the assessment for the year of assessment 1992/93 to one showing revised assessable profits of $564,310 with tax payable thereon of $84,646, and

(b) the assessment for the year of assessment 1993/94 to one showing revised assessable profits of $291,732 with tax payable thereon of $43,759.

3. The profits for the year of assessment 1992/93 arose from the sale of a residential flat and a car parking space in District A ('the Property B') and the profits for the year of assessment 1993/94 arose from the sale of a residential flat in District C ('the Property D').

4. The Taxpayer's notice of appeal dated 24 July 1997 was received by the Clerk to the Board of Review on 28 July 1997. As the representative for CIR did not dispute the Taxpayer's statement that the Taxpayer received the determination dated 25 June 1997 on 7 July 1997, we took the view that the appeal was in time and leave to appeal out of time was not required.

The facts

5. By confirmation of instructions dated 21 December 1990, the Taxpayer agreed to purchase Property B (which was then still under construction) at the price of $958,900. The formal agreement was dated 27 December 1990. By an equitable mortgage dated 7 January 1991, the Taxpayer mortgaged Property B to Bank K to secure $800,000.

6. The occupation permit for Property B was issued on 20 November 1991 and the letter of compliance was dated 27 December 1991.

7. Property B was assigned to the Taxpayer by an assignment dated 6 April 1992. By a provisional agreement dated the following day, that is, 7 April 1992, the Taxpayer contracted to sell the Property B for $1,700,000. The sale was completed by an assignment dated 6 May 1992.

8. By agreement for sale and purchase dated 18 July 1992, the Taxpayer agreed to purchase Property D (which was then still under construction) at the price of $1,339,200. By an equitable mortgage dated 19 August 1992, the Taxpayer mortgaged Property D to the same Bank K, the consideration being all monies.

9. The occupation permit was issued on 31 December 1993.

10. By an agreement for sub-sale and purchase dated 18 January 1994, the Taxpayer agreed to sell Property D for $1,790,000. The sale to the sub-purchaser was completed by an assignment to the sub-purchaser dated 27 January 1994, with the Taxpayer joining in as a confirmor.

11. The assessor was of the opinion that the respective purchases and sales of Property B and Property D amounted to adventures in the nature of trade. On 14 March 1996, she raised on the Taxpayer profits tax assessments with estimated assessable profits of $670,000, with tax payable thereon of $100,500 for the year of assessment 1992/93 and estimated assessable profits of $410,000, with tax payable thereof of $61,500 for the year of assessment 1993/94.

12. By letter dated 12 April 1996, the Taxpayer objected to the assessments in the following term:

> *Property B*
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> *'… I worked … at District E that I have to travel from District A to Hong Kong Island everyday, and the ferry service does not help that much. I lived there for six painfully months and then sold this property and parking space, mainly due to the transportation problems. I change the residence to [Property D] that is very close to my work place.'*
>
> *Property D*
>
> *'For the sale of [Property D], I need more space as I am going to get married, and this 263 square feet saleable area which has no problem for one single resident is considered too small for two.'*

13. The Taxpayer also claimed that he had incurred various expenses including decoration expenses of $120,000 for Property B and decoration expenses of $3,773 for the Property D.

14. The assessor considered that the assessments should be revised to allow the expenses claimed by the Taxpayer in the objection, with the exceptions of the alleged decoration expenses.

15. The Commissioner agreed with the assessor; rejected the Taxpayer's objection; but revised the assessment for the year of assessment 1992/93 to one showing revised assessable profits of $564,310 with tax payable thereon of $84,646; and the assessment for the year of assessment 1993/94 to one showing revised assessment profits of $291,732 with tax payable thereon of $43,759.

The appeal

16. The Taxpayer appealed on the ground that the profits in dispute were capital gains rather than trading gains. In the course of the hearing of the appeal, the Taxpayer abandoned his appeal against the decision of the Commissioner to disallow any deduction on account of the alleged decoration expenses.

17. The Taxpayer's case was that he acquired both properties for self-residence.

18. In respect of Property B, the Taxpayer claimed in his objection that he 'lived there for six painfully months'.

19. According to China Light & Power Company Limited, only 2 units of electricity had been consumed by electric appliances at Property B during the period from 23 November 1991 to 29 June 1992, with 1 unit being consumed between 26 March 1992 and 27 April 1992, and the other unit being consumed between 27 April 1992 to 26 May 1992.

20. In his notice of appeal, the Taxpayer asserted that 'the properties concerned were used for the stay of myself'.

21. His evidence at the hearing of the appeal was that he moved in December shortly after decoration was completed; that in January and February, he was out of town and in Country F 'being interviewed for a job'; that he entered Country F on 3 January 1992 and left in about mid-February; that he only intermittently lived in Property B in February and March; that he decided to dispose of it in April, after which, he started 'to remove things out of the Property'; that there was no refrigerator at Property B; that there was no washing machine, the washings being done at his parents' home; that lights, alarm clock and radio were the electrical appliances at Property B; that he did not need the air-conditioning; and that he could not recall if he had ever stayed in Property B during day time on holiday, sick leave or otherwise. The Taxpayer said more than once that 'I haven't made up my mind whether to live there permanently'.

Our Decision

22. The Taxpayer impressed us as an unreliable witness, telling us a pack of lies in an attempt to explain the nil or nominal electricity consumption at Property B; and in an attempt to explain his quick sale of Property D, joining in the assignment as the confirmor.

Our Decision on Property B

23. We categorically reject the Taxpayer's assertions that he purchased Property B for the purpose of self-residence and that he had actually resided or stayed in Property B.

24. If the Taxpayer had resided or stayed in Property B, the electricity consumption would not have been nil except for two months when the consumption was 1 solitary unit for each of those two months. For a person who claimed to have acquired Property B to improve his living standard, and further claimed to have spent $120,000 on decoration expenses (abandoned at the hearing of the appeal), we find it incredible that he had not fitted his new residence with a refrigerator or a washing machine.

25. The 'invitation letter' that he produced in support of his assertion that he went to Country F on 3 January 1992 to attend an interview for a job is a letter dated 4 November 1991 stating that the writer company '… hereby cordially invites you to come to our company as a network computer technician specialist. We feel that you have the best qualifications for our company and we request that you please make arrangements to apply for your visa as soon as possible since we need to fill this position immediately'. On the face of this document, the Taxpayer was invited to report for work 'immediately', not to attend an 'interview' two months later. The Taxpayer did not tell us why he spent almost one and a half months in Country F.

26. Further, we find that the alleged intention to acquire and hold Property B as a capital asset could not have been genuinely held, realistic or realisable, even on the Taxpayer's own case.

27. According to the Taxpayer, the mortgage loan (the equitable mortgage being dated 7 January 1991) was $800,000, repayable by 180 instalments of $8,843.19. According to his salaries tax return for the year ended 31 March 1991, his total income (including income from his part-time job) was $141,917 (or $11,826.42 per month), and he claimed dependent parent allowance for two dependent parents. He was evasive on the amount of contributions to his parents. He maintained a car. After paying off his mortgage instalment, he would have been left with $2,983.33 per month for his own subsistence, support of his two parents and maintenance of his car.

28. His total income for the year ended 31 March 1992 was $162,776 (including part-time job income), or $13,564.67 per month, and he claimed dependent parent allowance for two dependent parents.

29. His total income for the year ended 31 March 1993 was $182,388 (including part-time job income), or $15,199 per month, and he claimed dependent parent allowance for two dependent parents.

30. His total income for the year ended 31 March 1994 was $205,680 (including part-time job income), or $17,140 per month, and he claimed dependent parent allowance for two dependent parents.

Our Decision on Property D

31. We turn now to Property D. We do not for one moment accept and we reject his assertions that he acquired Property D for self-residence and that he sold it because he needed more space as he was going to get married.

32. Property D was put forward in the objection as the residence which the Taxpayer changed to after sale of Property B – 'I change residence to [Property D] that is very close to my working place'. The truth of the matter is that the Taxpayer had never resided at Property D. He never took possession of Property D. He sold it before it was assigned to him, joining in the assignment to his sub-purchaser as confirmor.

33. The Taxpayer, an adult who had contemplated marriage with another lady (not the one whom the Taxpayer put forward as the reason for sale of Property D) before he decided to purchase Property D, gave no explanation why he decided to buy Property D which was 'too small for two', allegedly as a capital investment. He was unable to tell us anything concrete about the alleged intended marriage. He claimed that after disposing of Property D, he 'purchased' another property at District G as his intended matrimonial home. The property at District G would not and could not be completed in time for the Taxpayer's intended marriage. In the event, the Taxpayer neither got married nor acquired the property at District G. Incidentally, the reason the Taxpayer gave for selling Property B was that it was too far away from his place of work at District E, but the Taxpayer did not regard District G as being too far away from his place of work!

Assessments confirmed

34. For the reasons given above, we dismiss the appeal and confirm both assessments appealed against.