

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D45/02

Profits tax – disposal of real property – the true intent of the taxpayers when the property was bought – section 68(4) of the Inland Revenue Ordinance ('IRO').

Panel: Ronny Tong Ka Wah SC (chairman), William E Mocatta and George Lo Kwan Wong.

Dates of hearing: 26 February and 21 March 2001.

Date of decision: 31 July 2002.

The taxpayers, husband and wife, purchased Property 1 in May 1996 and sold it in May 1997, barely 19 days after Property 1 was completed by the developers and assigned to the taxpayers.

The taxpayers asserted that they bought Property 1 for self-residence but when the wife became pregnant 'unexpectedly' in March 1997, they decided to immigrate to Country D and hence Property 1 was sold.

The husband's family acquired Country D's immigration status in 1994 but he had never lived in Country D. He married the wife in 1995 and in July 1996 the wife also acquired Country D's immigration status. And yet there was no decision to move to Country D at that time. The taxpayers first visited Country D in September 1997 but they stayed there for just over two weeks. The wife returned to County D in November 1997 until February 1998 when she returned to Hong Kong after the birth of the baby in December 1997. No steps were taken by the taxpayers to ship any of their furniture or belongings to County D.

The taxpayers freely admitted they lacked the necessary financial resources to purchase any family home. After Property 1 was sold, the husband admitted that for the first time, with the profit made from the sale, the taxpayers were in a position to buy a house in Country D. But they did not do that.

Held:

Having observed the taxpayers in the witness box and listened to their evidence carefully, the Board was not convinced that they were telling the truth when they said they decided to immigrate to Country D in March 1997 and that was the reason for the sale of Property 1. However, disbelieving the taxpayers on their evidence as to the reason for the sale of

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Property 1 did not prove what their intention was when Property 1 was bought. Having carefully considered the testimony of the taxpayers and the surrounding circumstances, the Board was being left with considerable doubt as to whether that was the true situation. In these circumstances, the Board was unable to say the taxpayers had properly and fully discharged their burden under section 68(4) of the IRO.

Appeal dismissed.

Leung Wing Chi for the Commissioner of Inland Revenue.

Taxpayers in person.

Decision:

Background facts

1. This is an appeal by Mr A ('the Husband') and Madam B ('the Wife') (collectively 'the Taxpayers') against the Commissioner's determination dated 28 April 2000 ('the Determination') overruling the Taxpayers' objection to their profits tax assessment for the year of assessment 1997/98.
2. The profits tax arose out of a sale of a property at Address C ('Property 1') which the Taxpayers bought on 11 May 1996. The sale took place on 24 May 1997, barely 19 days after Property 1 was completed by the developers and assigned to the Taxpayers on 5 May 1997.
3. The Taxpayers in their letter of appeal dated 26 May 2000 ('the Letter') asserted that they bought Property 1 for self-residence but when the Wife became pregnant 'unexpectedly' in March 1997, they decided to immigrate to Country D and hence Property 1 was sold as described above.
4. Both the Husband and the Wife gave evidence before us but the appeal rested largely on the evidence of the Husband.
5. What we have to consider is what the true intent of the Taxpayers was when they bought Property 1 in the light of the surrounding circumstances and their evidence.

Immigration status

6. The Husband, and implicitly, the Wife accepted all the basic facts set out in the Determination. He, however, also gave evidence to supplement his case as set out in the Letter as

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follows.

7. He is the eldest son of his family. His family acquired Country D's immigration status in 1994 but he had never lived in Country D. He had always worked for his parents' business. He worked as a manager for their publishing company until 1999.

8. He married the Wife in 1995 and in July 1996, the Wife also acquired Country D's immigration status. And yet, according to them, there was no decision to move to Country D at that time. It is to be noted that Property 1 was bought on 11 May 1996, some two months before the Wife landed in Country D although obviously by then the Taxpayers must have formed the intention, as so many people in Hong Kong did at that time, that they should eventually immigrate to Country D.

Financial resources

9. The Taxpayers at that time were living in rented accommodation provided by the parents' business. At the end of October 1996, they moved to stay with the Wife's mother and in March 1997, they moved to live with the Husband's parents.

10. The Taxpayers freely admitted they lacked the necessary financial resources to purchase any family home although in June 1993, the Husband did purchase a property at District E jointly with his mother. That was sold in February 1994 at a profit of some \$1,500,000. The Husband never explained whether he regarded himself as having a share in that profit.

11. After Property 1 was sold, the Husband admitted that for the first time, with the profit made from the sale, the Taxpayers were in a position to buy a house in Country D. But they did not do that. They did not visit Country D until 20 September 1997. Instead, another property was purchased almost immediately on 6 June 1997 ('Property 2'). Property 2, like Property 1, was purchased at a time when it was still under construction.

12. In a reply made to the Revenue's enquiry, the Taxpayers' tax representatives claimed that Property 2 was acquired with the intention 'to be solely occupied by the Taxpayers themselves'. But in evidence, the Husband admitted that he bought Property 2 for 'short-term speculation'.

13. Property 2 was purchased in the sole name of the Husband and it was sold less than a month later on 29 June 1997 with a handsome profit of some \$600,000.

14. The Taxpayers now were in an even better position to purchase a family home in Country D. But they did not do that. The profits, we were told, were 'invested' in the Husband's mother's 'portfolio' and were 'locked' there by reason of the financial turmoil at the end of 1997.

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Visits to Country D

15. The immigration records which were accepted by the Taxpayers showed that they first visited Country D on 20 September 1997, staying there for just over two weeks and returning on 7 October 1997. The Wife then returned to Country D on 3 November 1997 until 11 February 1998 when she returned to Hong Kong after the birth of the baby in December 1997.

16. The Husband visited Country D between 7 December 1997 and 31 December 1997, obviously to be present when the baby was born. Thereafter he did not return to Country D until 26 March 1999 when he visited Country D alone for some two weeks.

17. The Wife returned to Country D alone between the periods 20 May 1998 and 6 June 1998, 27 November 1998 and 18 December 1998 and 7 March 1999 and 21 May 1999, each time travelling without the Husband.

18. The Taxpayers claimed they did look for a suitable house in Country D but no specific house was found although they said their choice had 'narrowed down' to a few houses in a few districts. The Wife in fact stayed in rented accommodation during the three months of stay in Country D.

Employment

19. The Husband claimed he did give notice to his parents that he would cease working for them. But he never did. Nor did his parents employ someone to take up the position of manager in place of the Husband.

20. The Husband was to work for the parents' business in Country D but that never materialized.

21. The Wife had previously worked with a company called Company F. Originally, it was claimed that she worked there between 1 April 1996 and 15 September 1997 when she went to Country D. It is now claimed that that was in error. In fact, she only worked until September 1996. Between September 1996 and September 1997, she worked at a school, also the family business of the Husband's. After she came back in February 1998, she continued to work for the family business but on a part-time basis.

The decision to come back

22. No steps were taken by the Taxpayers to ship any of their furniture or belongings to Country D. In fact, the evidence strongly suggests their ties to Hong Kong were never severed. If there was an intention to take up their residency in Country D, their actions certainly did not

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demonstrate that.

23. The Wife, of course, did give birth in Country D but in those days, many people in Hong Kong did that simply as an insurance against what many regarded as an uncertain future of Hong Kong.

24. The Taxpayers said the decision to move back was made between January and February 1998, immediately after the baby was born. The Wife missed the Husband, it was said. Of course she did. The Husband was still working in Hong Kong all the time apart from that brief period when he was present at the birth of their son.

Our findings

25. Having observed the Taxpayers in the witness box and listened to their evidence carefully, we are not convinced that they were telling the truth when they said they decided to immigrate to Country D in March 1997 and that was the reason for the sale of Property 1. Apart from the Wife going to Country D to give birth to their son, all the evidence is consistent with the Taxpayers wishing to continue to live in Hong Kong.

26. The trip to Country D to give birth is, of course, consistent with the Taxpayers' declared intention to reside there but the circumstances strongly suggest they simply intended, like many in Hong Kong, that their son should acquire a foreign passport by birth. There was never any genuine attempt to uproot from Hong Kong.

27. However, disbelieving the Taxpayers on their evidence as to the reason for the sale of Property 1 does not prove what their intention was when Property 1 was bought. They could still have bought Property 1 with the intention to reside there as a family home.

28. Having carefully considered the testimony of the Taxpayers and the surrounding circumstances, we are being left with considerable doubt as to whether that was the true situation. The Taxpayers had no financial means to either acquire a property or to maintain it. They had been living in family accommodation at all material times. There was property speculation before and after the purchase of Property 1.

29. Furthermore, if the sale of Property 1 was not prompted by a genuine desire to immigrate abroad, what was the true reason for the sale? Why was the Husband unable to freely deploy the profits of the two sales? While we make no finding as to whether it was truly the Husband who was behind the purchases of Property 1 and Property 2 respectively, we are by no means convinced that the evidence of the Husband on this matter represents the whole truth.

30. In these circumstances, we are unable to say the Taxpayers had properly and fully discharged their burden under section 68(4) of the IRO. The appeal must be dismissed.