

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D47/88

Appeals – assets betterment statement – need for taxpayer to adduce proper evidence to challenge such a statement.

Assessments – assets betterment statement – disputed items.

Panel: William Turnbull (chairman), Christopher Chan Cheuk and Michael Choy Wah Ying.

Date of hearing: 21 September 1988.

Date of decision: 8 November 1988.

The taxpayer understated his profits in his returns, and was assessed on the basis of assets betterment statements. He objected to these assessments.

The taxpayer claimed (a) that his living expenses had been understated, and that (b) gambling winnings, (c) amounts owing to trade creditors and (d) proceeds from the sale of certain gold and jewellery should be deducted from the assets betterment statements.

Held:

The taxpayer had failed to discharge his burden of proof with respect to the first three items, but had succeeded in doing so with respect to the fourth item.

[Editor's note: This decision does not illustrate any major point of principle. Its interest lies in the fact that it demonstrates the evidential factors which are involved in cases where a taxpayer challenges the correctness of an assets betterment statement.]

Appeal allowed in part.

Tse Yue Keung for the Commissioner of Inland Revenue.

Taxpayer in person.

Decision:

INLAND REVENUE BOARD OF REVIEW DECISIONS

This is one more of those unfortunate cases where the assessor has had to resort to an assets betterment statement because of the Taxpayer's ignorance or inability to keep accurate accounts.

In many cases, Boards of Review and higher courts have placed on record that ignorance of accounting and of the laws of taxation is no excuse for a taxpayer failing to keep accurate accounts and filing accurate tax returns. Where a taxpayer has failed to keep accurate accounts, the assessor has no alternative but to resort to imprecise methods of trying to estimate the profits which the taxpayer has made. That is the situation in the present appeal.

The facts are as follows:

1. The Taxpayer was an employee of a decoration company and earned a salary of \$2,000 per month. The Taxpayer decided to terminate his employment and to commence business as an interior decoration contractor. He commenced his business on 1 July 1979.
2. Through the hard work and frugal life style and habits of the Taxpayer which he had learnt from his father, the Taxpayer's business was successful.
3. The Taxpayer maintained his accounts on an annual basis ending on 31 March in each year. In his business year of 1982/83, the Taxpayer went into a joint venture which was successful and resulted in his making substantially higher profits in that year than in previous years. It also led to his adopting a more lavish life style and to enquiries being made by the Inland Revenue Department into the accuracy of his business accounts.
4. The Taxpayer had maintained accounts and filed tax returns but, when the Inland Revenue Department commenced its enquiries towards the end of the calendar year 1983, it became apparent that the accounts maintained by the Taxpayer were not accurate and he had failed to include certain items of business income which should have been subject to tax.
5. The Inland Revenue Department then proceeded to prepare assets betterment statements from 1 July 1979, being the date when the Taxpayer had commenced business up to and including 31 March 1983. In due course, tax assessments were issued for the years of assessment 1979/80, 1980/81, 1981/82 and 1982/83 based on the assets betterment statements and it is from these assessments that the Taxpayer has appealed.
6. The Taxpayer disputed four specific items in the assets betterment statements which he claimed overstated the assessable profits of his business.

INLAND REVENUE BOARD OF REVIEW DECISIONS

As each of the four items was dealt with precisely and separately by the Taxpayer and the representative for the Commissioner, it is convenient for us to deal with them in the same way in this decision. All four depend entirely upon the facts of the case as we find them.

Living expenses

The first claim related to the living expenses of the Taxpayer which the assessor had included in the assets betterment statement. The assessor had included the sum of \$2,500 per month for the first period of nine months, \$3,000 per month for the year 1980/81, \$3,500 per month for the year 1981/82 and \$4,000 per month for the year 1982/83.

The Taxpayer gave evidence and was cross-examined. His evidence was to the effect that his living expenses were substantially less than those estimated by the assessor. He said that he had been earning wages of only \$2,000 per month when he started his business. He estimated that his living expenses should have been \$1,400 per month for the first period of nine months, \$1,500 per month for the year 1980/81, \$1,600 per month for the year 1981/82 and \$1,700 per month for the year 1982/83.

Though the Taxpayer gave evidence and was cross-examined with regard to his living expenses, we are unable to agree with the figures which he stated. Whilst the sum of \$1,400 may have been reasonable for the first nine months in 1979/80 when the Taxpayer first commenced his business, we cannot agree with his suggestion that his living expenses were only \$1,700 in the year 1982/83. According to his own evidence, his business was successful and he was in a profitable joint venture in the year 1982/83. He said that he frequently met with his friends socially for gambling at cards and mahjong during that year. He had four children who in the year 1980 were respectively one, two, five and six years old. It is unrealistic to think that a family of that size with children of those ages would have monthly living expenses increasing by only \$100 in each year. We have taken note of the fact that the Taxpayer owned a car which he used for his business but was no doubt also used for private purposes, and that the Taxpayer moved his residence from Shaukeiwan to Shatin. Though his move may have been after the years in question, it supports the assessor in taking the view that the Taxpayer's lifestyle and his expenses rose by more than \$100 per month.

The onus of proof in all tax appeals is upon the taxpayer and in this case the Taxpayer has not discharged that onus of proof in relation to his monthly living expenses. Accordingly, we dismiss the appeal in this regard.

Gambling winnings

The next item to be considered is a claim by the Taxpayer that he made profits during the year 1982/83 from gambling with his friends. Here again the onus of proof is on the Taxpayer and, though he gave evidence and was cross-examined, we are not satisfied that he in fact made any profits. No third parties were called to give evidence to support his claim and the only evidence which we have is his own self-serving statement that he was

INLAND REVENUE BOARD OF REVIEW DECISIONS

able to make money from cards and mahjong. He said that he gambled four nights per week and that he would lose or win \$600 to \$700 each night with the largest amount being \$1,800. It was all social gambling. He claimed that during the year in question he won about \$15,000. He said that he kept no records of his wins and losses and that he was making an estimate. We are unable to accept such a vague assertion by the Taxpayer and accordingly we dismiss his appeal with regard to his alleged gambling wins.

Amounts owing to trade creditors

The third item was a claim that, at the close of business at 31 March 1983, the Taxpayer had book debts owing by him to third parties of \$20,000. He said that this had not been deducted in the assets betterment statement. Here again we are unable to accept the Taxpayer's submission and dismiss his appeal so far as it relates to his trade creditors. Whilst it may be that he had trade creditors and the total amount might have been as high as \$20,000, he did not produce any detailed accounts and vouchers to support his figure. He said that the sum of \$20,000 represented payments appearing in his bank statements and, so he thought, related to debts arising during the previous financial year. When cross-examined, he agreed that part of his estimate comprised wages paid to employees after the year-end but he did not suggest that he was paying his employees in arrears. Wages are paid either immediately before the end of an accounting period or immediately thereafter without any delay. Such items could not have related to the preceding year.

Equally important is the fact that the Taxpayer would have appeared to have been keeping his business accounts on a cash basis using his bank accounts as the main source of information. It did not appear that he was keeping any detailed accounts of his income and expenditure. No provision was made in the assets betterment statement for moneys due to the Taxpayer from any of his customers. If trade creditors are to be included, then trade debtors should likewise be included.

As the Taxpayer kept his accounts on a cash basis, the trade creditors to whom he made reference should have been deducted from his profits for the following year. We direct that the Commissioner should, when assessing profits tax on the Taxpayer for the year of assessment 1983/84, ensure that the sums which have been disallowed from the assets betterment statement are included as expenses in the accounts for the following year.

Finally in regard to this item we note that, in the Taxpayer's own accounts, which were not accepted by the Commissioner but which were signed and approved by the Taxpayer, an item appeared under the heading of 'work in progress' in the profit and loss statement but, in the balance sheet, there was no item shown for trade creditors.

For the reasons given we dismiss the appeal with regard to the claim to deduct the alleged sums due to trade creditors.

Proceeds of sale of assets

INLAND REVENUE BOARD OF REVIEW DECISIONS

The fourth item which the Taxpayer claimed should be deducted from his assets betterment statement was the proceeds from the sale of certain gold ornaments and gold ingots. In giving evidence, the Taxpayer said that his father had given him a number of gold ingots and that his wife had a number of items of gold jewellery which she had received when they were married. In addition, his wife had purchased gold on a number of occasions. He claimed that on two occasions his wife had sold most of the gold. The first occasion was when he started his new business, and the second occasion was when he wished to pay for the flat which he was buying at Shatin. He had been able to produce receipts for some of these transactions but not for all of them. The Commissioner had accepted as deductions only those items for which the Taxpayer was able to produce receipts or other documentary evidence and had refused to accept the other items.

As in relation to the other items under appeal, the Taxpayer gave evidence on his own behalf and was cross-examined. We have dismissed this appeal so far as it relates to the three other items already dealt with in this decision, but the reason in each for our dismissal is not that we did not believe the evidence given by the Taxpayer but that he had failed in his evidence to discharge the onus of proof put upon him by the Inland Revenue Ordinance. With regard to the claim that gold ingots and jewellery had been sold on two occasions, we believe the Taxpayer and also find that he discharged the onus of proof to our satisfaction.

The Taxpayer had been able to produce a number of receipts or vouchers relating to the gold which was sold and these were accepted by the Commissioner and the assessor. Accordingly, there was no doubt whatsoever that some gold was sold and the moneys received for this gold were included in the assets betterment statement. What is in dispute is whether or not the Taxpayer is entitled to claim additional sums of money received by him in his bank account which he says related to further sales of gold.

We find as a fact that the Taxpayer and his wife did on two occasions sell gold, the first time in the year 1979/80 when the Taxpayer was establishing his new business and the second occasion in 1982/83 when he wished to finance the purchase of the apartment which he had bought.

The Taxpayer said that he and his wife did not insist upon receiving receipts for all of the gold which they sold and that it was customary for goldsmith shops not to give receipts for all such transactions. We find this explanation to be reasonable and we accept it. The Taxpayer said in his evidence that he had endeavoured to obtain supporting statements from at least one goldsmith shop with whom his wife had frequent dealings. He was unsuccessful because the goldsmith shop did not keep records of individual transactions and could not produce copies of invoices. Here again we find his evidence and explanation to be reasonable and acceptable.

This fourth item under appeal is different from the other three because it had already been accepted by the Commissioner and proved to our satisfaction that the Taxpayer and his wife did own gold which was sold in the two years in question. What we now have

INLAND REVENUE BOARD OF REVIEW DECISIONS

to decide is how much money the Taxpayer received for the gold which was sold. According to his evidence, he has identified sums of money which were paid into his bank account and which he says on affirmation and after cross-examination related to the individual gold sales. He said that he could not remember exactly all of the sales of gold and that the amount received might have been more than the amount which he claimed.

On the facts and evidence before us, we find that the Taxpayer in the year of assessment 1979/80 did sell additional gold ingots and jewellery and received the sum of \$63,000 as claimed and in the year of assessment 1982/83 did sell additional gold ingots and jewellery and received the sum of \$46,500 as claimed. As these items were disallowed by the Commissioner, we decide that the appeal of the Taxpayer is successful with regard to this fourth item and direct that the two assessments appealed against for the years of assessment 1979/80 and 1982/83 be reduced accordingly.

The assessments for the years of assessment 1980/81 and 1981/82 are confirmed and the appeal in regard to those two years is dismissed.