Case No. D51/02

Profits tax – real property – whether the gain arising from the disposition of property was liable for profits tax – sections 2, 14(1) and 68(4) of the Inland Revenue Ordinance ('IRO') – costs – frivolous and vexatious and abuse of the process – section 68(9) of the IRO.

Panel: Kenneth Kwok Hing Wai SC (chairman), Edward Chow Kam Wah and Lawrence Lai Wai Chung.

Date of hearing: 17 May 2002.
Date of decision: 9 August 2002.

The appellants Company A, Company B and Company C were private limited companies engaged in the business of 'trading in garments', 'property investment and provision of design and management services' and 'trading of textile products' respectively.

By a letter dated 3 September 1993, Company B offered to purchase a property at a consideration of $14,980,000. The formal sale and purchase agreement in respect of the property was executed on 2 October 1993. By a preliminary agreement dated 28 January 1994, Company B sub-sold the property for $23,300,000. The sale was completed on 29 April 1994 with Company B acting in the capacity of confirmor. A profit of $7,579,823 was derived from the sale.

In their respective financial accounts for the year ended 31 March 1995, Companies A, B and C reported that they derived a profit from the sale of the property from a joint venture.

In response to the assessor's enquiries, Company A, through Accountants' Firm L, asserted that the original intention in purchasing the property was for long term investment purpose. Upon the payment of initial deposits by the joint venture partners, and before the payment of the final balance, the appellants tried to arrange for a mortgage loan. However, it was unsuccessful due to the banks' new policy at that time to tighten the granting of bank loan. As the completion date was coming close, the appellants had no alternative but to dispose of the property involuntarily rather than to let the deposit be forfeited by the vendor.

The profit and loss accounts of Company B for the years ended 31 March 1993 and 1994 showed losses of $606,211 and $396,763 respectively. Its balance sheets for those two years showed shareholders' deficits of $606,211 and $396,763 respectively. Company C's profit and loss accounts for those two years showed losses of $499,346 and $755,281 respectively. Its balance sheets for those two years showed shareholders' deficits of $489,346 and $745,281

respectively. Company A's profit and loss accounts for the period from the date of incorporation on 7 May 1992 to 31 March 1994 showed a profit of $725,439. Its balance sheet as at 31 March 1994 showed shareholders' funds of $825,439.

In support of their objection and in support of their appeal, the appellants uttered and relied on copy documents purporting to be joint venture agreement and minutes of extraordinary general meetings of Companies A, B and C.

Held:

1. The stated intention was long term holding for rental income. There was no self-apparent reason why the three appellants should join together in investing in the property, if investment it was. The Board had no doubt that Company B did not have the financial ability to complete the acquisition of the property at the price of $14,980,000, not to mention holding it for an indefinite period. It was nonsensical to bring in Company C as a 'partner to share the investment because at that time … [Company B] might not be capable enough for such an investment'. While Company A was not in the red, it clearly did not have the financial means to help Company B complete the acquisition of the property or to hold it for an indefinite period. As at 31 March 1994, the aggregate shareholders' deficits of Companies B and C exceeded the shareholders' funds of Company A by $316,605. There was no evidence of any available credit line. There was no evidence on the cash flow of any of the appellants which had an aggregate net current liability. There was no evidence on the personal net worth of any of the shareholders or directors of the appellants. In the Board's decision, all the documents were not authentic and not contemporaneous. The appellants had not proved that at the time of the acquisition the intention of the appellants was to hold the property on a long term basis and that such intention was genuinely held, realistic or realisable.

2. The Board was of the opinion that the appeal was frivolous and vexatious and an abuse of the process. This was a quick confirmor sale where the appellants clearly did not have the financial means to complete the acquisition or to keep the property for an indefinite period. The Board deprecated the appellants for putting forward and relying on documents which were not authentic. Pursuant to section 68(9) of the IRO, the Board ordered the appellants to pay the sum of $5,000 as costs of the Board.

Appeal dismissed and a cost of $5,000 charged.

Cases referred to:

Simmons v IRC [1980] 1 WLR 1196
All Best Wishes Limited v CIR [1992] 3 HKTC 750
Wing On Cheong Investment Co Ltd v CIR 3 HKTC 1
D11/80, IRBRD, vol 1, 374
Hillerns and Fowler v Murray 17 TC 77
Chan Sau-kut and Another v Gray & Iron Construction & Engineering Co (a firm) [1986] HKLR 84
Marson v Morton [1986] 1 WLR 1343
D42/99, IRBRD, vol 14, 445

Cheung Mei Fan for the Commissioner of Inland Revenue.
Richard Leung Counsel instructed by Messrs Fairbairn Catley Low & Kong for the taxpayers.

Decision:

1. This is an appeal against the determination of the Commissioner of Inland Revenue dated 4 January 2002 whereby the profits tax assessment for the year of assessment 1994/95 under charge number 2-5054625-95-6, dated 25 October 2000, showing assessable profits of $7,579,822 with tax payable thereon of $1,250,670 was confirmed.

The agreed facts

2. The following facts are agreed by the parties and we find them as facts.

3. The Appellants are Company A, Company B and Company C. They have objected to the profits tax assessment for the year of assessment 1994/95 raised on them. The Appellants claimed that the profit derived by them from the sale of a property was capital in nature and should not be assessable to tax.

4. Company A is a private limited company incorporated in Hong Kong on 7 May 1992. At all relevant times, its authorised and paid up share capital was $100,000, divided into 10,000 shares of $10 each. The following persons have been its shareholders and directors:

	Number of shares held
Mr D	2,000
Mr E	2,000
Ms F	4,000
Mr G	2,000
	10,000

At all relevant times, Company A engaged in the business of 'trading in garments'.

5. Company B is a private limited company incorporated in Hong Kong on 11 July 1989. At all relevant times, its authorised and paid up share capital was $10,000, divided into 10,000 shares of $1 each. Mr D and Mr E have been its only directors and shareholders, each holding 5,000 shares in it. In its directors' report, the principal business carried on by Company B was described as 'property investment and provision of design and management services'.

6. Company C is a private limited company incorporated in Hong Kong on 7 February 1992. At all relevant times, its authorised and paid up share capital was $10,000, divided into 10,000 shares of $1 each. Mr D and Mr E have been its directors and shareholders, each holding 5,000 shares in it. In addition, a Mr H was also one of its directors. Ms I was later appointed a director of Company C on 23 June 1997. At all relevant times, the nature of the business carried on by Company C was 'trading of textile products'.

7. By a letter dated 3 September 1993, Company B through Property Agent J offered to purchase from the then owner a property at Address K ('the Property') at a consideration of $14,980,000. The letter contains, inter alia, the following terms:

(a) The purchase price was to be paid in the following manner [clause 4]:

	On or before		**Amount** $
(i)	3-9-1993	Initial deposit	500,000
(ii)	4-10-1993 or upon signing formal sale and purchase agreement, whichever is the earlier	Further deposit	2,496,000
(iii)	29-4-1994 upon completion of purchase	Balance	11,984,000
			14,980,000

(b) The vendor should, upon request by Company B after signing the formal agreement, allow a maximum of five viewing appointments of the Property by Company B [clause 11].

8. The formal sale and purchase agreement in respect of the Property was executed on 2 October 1993.

9. By a preliminary agreement dated 28 January 1994, Company B sub-sold the Property for $23,300,000. The sale was completed on 29 April 1994 with Company B acting in the capacity of confirmor. A profit of $7,579,823 was derived from the sale.

10. In their respective financial accounts for the year ended 31 March 1995, Companies A, B and C reported that they derived a profit from the sale of the Property from a joint venture.

(a) The profit reported by them was as follows:

	Share of profit
	$
Company A	2,200,000
Company B	3,179,822
Company C	2,200,000
	7,579,822

(b) The following was also stated in the explanatory note of the tax computations of Companies A and B:

'On 1/9/93, the Company signed a joint venture agreement with its related companies ... for long-term investment in [the Property] and agreed to share all income or loss arising from [the Property] among the parties.

[The Property] was held by [Company B] on behalf of the other parties. However, [Company B] could not obtain bank financing on purchases and [the Property] was then funded by the other parties. Furthermore, the parties anticipated that there would be economic depression which leads to the government's proposal to suppress property prices. The parties also anticipated that substantial decline in property value would be imminent and that bank financing would be difficult to obtain for investment properties as banks had declared that they would support the aforesaid government policy.

In order to avoid further adverse conditions as well as to release the financial burden of all parties, on receiving a favourable offer on 2/10/93 [should be 28 January 1994], the parties decided to sell [the Property].

The Company's share of the gain of ... therefore represents capital gain.'

11. In response to the assessor's enquiries, Company A, through Accountants' Firm L, put forth the following assertions in relation to the purchase and sale of the Property:

(a) 'The original intention in purchasing [the Property] was for long term investment purpose.'

(b) ' Upon the payment of initial deposits by the joint venture partners, and before the payment of the final balance, [the Appellants have] tried to arrange for a mortgage loan. However, it was unsuccessful due to the banks' new policy at that time to tighten the granting of bank loan and these were orally confirmed by [Bank M] and [Bank N] and a written reply from [Bank O] was also obtained ... As the completion date was coming close, in late January 1994 [the Appellants have] no alternative but to disposal (*sic*) [the Property] involuntarily through a property agent rather than to let the deposit forfeited by the vendor ...'

12. The assessor was of the view that Companies A, B and C had formed a partnership in the purchase and resale of the Property and that the gain on disposal of the Property should be assessable to tax. Accordingly, he raised on the Appellants the following profits tax assessment for the year of assessment 1994/95:

	$
Assessable profits	7,579,822
Tax payable thereon	1,250,670

13. Accountants' Firm L, on behalf of the Appellants, objected to the profits tax assessment for the year of assessment 1994/95 in the following terms:

' 1. [The Appellants] only operate in form of a joint venture instead of a partnership for the purpose to (*sic*) generate long-term rental income ...

2. The above mentioned joint venture was forced to be terminated and the resulting gain on disposal of [the Property] is capital nature and not taxable for the following reasons:

(a) The original intention of [the Appellants] were (*sic*) to co-operate with each others (*sic*) to generate long-term rental income under the joint venture agreement, (*sic*) the (*sic*) obtainment of bank loan is a pre-requisite for such joint venture agreement. However, the sudden change of Hong Kong economy during 1993 caused the sudden tighten (*sic*) of loan granting by banks which in turn caused such joint venture unable (*sic*) to obtain bank loan.

(b) In order to protect the long-term investment principal, [the Appellants] were forced to dispose of [the Property] in order to get the significant deposit back for other long-term investment opportunities instead of just let (*sic*) the deposit forfeited (*sic*) by the vendor.

(c) There is no past record of revenue gain on disposal of the property in (*sic*) [the Appellants] which further prove (*sic*) their intension (*sic*) of long term investment.'

14. (a) By a letter dated 27 December 2000, the assessor pointed out to Accountants' Firm L that a joint venture might amount to a partnership if the parties involved carried on a business in common with a view of profit and that having reviewed the terms of the joint venture agreement, he maintained the view that the Appellants carried on a partnership business in the purchase and sale of the Property.

(b) By a letter dated 3 March 2001, Accountants' Firm L replied that it 'accept that such joint venture is taxable provided that its profit is of revenue nature and not exempted under IRO.'

15. In reply to the assessor's enquiries, Accountants' Firm L gave the following assertions:

(a) The downpayments of the Property, amounting to 20% of the purchase price, were contributed by the Appellants as follows:

	$
Company A	1,350,000
Company B	946,000
Company C	700,000
	2,996,000

(b) The Appellants had not conducted any feasibility study as to the viability of the venture.

(c) The Property was situated in a good location which could generate a reasonable level of rental income. As the then monthly rent of a property with similar size in the vicinity was about $86,000 (that is, a rental yield of about 6.9% per annum), the Appellants considered that the investment in the Property was a good means to preserve their capitals in view of the then low bank interest deposits rate which was around 3.5% per annum.

(d) As the Appellants had not yet completed the purchase when the preliminary agreement for sale was signed, they did not have the right to offer the Property for letting.

(e) The Appellants originally planned to apply for a mortgage loan of $10,486,000 (that is, 70% of the purchase price of the Property) which would have been repayable by 180 monthly instalments of $101,808 each. They should have no difficulty in meeting the shortfall of $15,808, being the difference between the monthly loan instalment and the expected monthly rent.

(f) The Appellants had obtained their bankers' oral consent in granting a mortgage loan before Company B entered into the formal sale and purchase agreement. The bankers, however, subsequently rejected their loan application due to the sudden tightening of bank policy which was directly affected by the abrupt change of property market conditions in late 1993. Documentary evidence in relation to the Appellants' initial oral enquiries to bankers and the bankers' initial oral consent were not available.

(g) In order to avoid the forfeiture of the deposits, the appellants on 8 January 1994 resolved to sell the Property. On 10 January 1994, they appointed Property Agent J as their estate agent which eventually solicited a buyer on 27 January 1994. As the Appellants were then still unable to obtain a bank loan to finance the balance of the purchase price, they had no alternative but to sell the Property on 28 January 1994.

(h) In recognition of the efforts spent by Company B in arranging the acquisition of the Property, soliciting bankers for mortgage loan and arranging the disposal of the Property, Companies A and C agreed to increase Company B's share of profit in the venture by surrendering part of their profits amounting to $326,607 each to Company B.

16. The assessor has since obtained the following information:

(a) During the four years ended 31 March 1991 to 1994, Companies A, B and C returned the following assessable profits or (adjusted loss):

Year ended 31 March	**Company A**	**Company B**	**Company C**
	$	$	$
1991	-	(615,480)	-
1992	-	(433,314)	-
1993	220,236	227,323	(489,494)
1994	689,967	86,377	(252,765)

(b) The auditors' report of Company C for the two years ended March 31 1993 and 1994 contained the following statements made by the auditor:

'The balance sheet has been prepared on a going concern basis. In view of the significant accumulated deficits and net liabilities at March 31, (1993/1994) continuance in business as a going concern is dependent upon the company attaining future profitable operations and the financial support of its bankers and directors.'

(c) According to the Hong Kong Property Review 1994, the property market in the year 1993 was described as follows:

'For the Hong Kong Property market, 1993 has been a year characterised by increases in price and rental levels in all sectors, apparently undisturbed by the various uncertainties and other political problems such as the controversy over the construction of the new airport.

Emerging from a period of stabilization early in the year, activity in the domestic section increased substantially after the end of the first quarter and this continued until July/August when major banks imposed further restrictions on mortgages. The 70% mortgage ceiling was lowered to 60% and below for properties over five million dollars. There was some reduction in speculative activity at the lower end of the market but luxury domestic sales and the leasing market have continued to remain very strong. This was brought about by limited supply coupled with strong demand from local professionals returning from overseas and expatriates newly arriving in the Territory. Sparked off by the optimism shown by developers at the mid December Government land auction for a residential site in Lung Ping Road, Kowloon activity gathered momentum again with price and rental levels reaching new record highs by the end by the year.'

17. In response to the assessor's request to comment on paragraphs 3 to 16 above, Accountants' Firm L put forward the following further assertions:

(a) 'It is common practice for a sale and purchase agreement to include a clause of viewing appointments ... The purpose of the insertion of the clause for five viewing appointments was to enable [the Appellants] to arrange for potential tenants to examine [the Property] even before the completion date, so [the Property] would be let out immediately after the completion of the acquisition.'

(b) 'Although [the Appellants] did not engage any independent third party to perform a formal feasibility study on the viability of the long term investment, [the Appellants] had performed an informal feasibility study themselves as follows:

(1) [The Appellants] have estimated the rental value of [the Property] ... was around HK$86,000 per month which gave rise to an expected rate of return of about 6.9% per annum while bank interest rate was only 3.5% at that time.

(2) [The Appellants] had reviewed property market and noted that the property market was blooming (*sic*) in August 1993 and they anticipated the rental price would increase.

(3) [The Appellants] had also considered the financial capability to finance such investment by each of the joint venturers. Each joint venturers intended to finance such investment by their profits/fund from their own operations. In case if there was shortage of funds, the shareholders of each joint venturers had agreed to provide financial support in the form of either shareholders' loans or share capital. As the shareholders are wealthy persons, they are able to provide the required funds if needed.'

(c) '... [the Appellants] originally planned to obtain a bank loan of 70% of purchase consideration of [the Property] even though a mortgage loan of 60% of purchase consideration may be sufficient ... Such balance of the purchase consideration could be financed by the shareholders of [the Appellants] as the shareholders of [the Appellants] are wealthy persons.'

(d) The financial position of Company C

'(1) As per the auditors' report of [Company C] for the year ended March 31, 1994, such sentence was only an emphasis of matter and did not constitute a qualified audit opinion.

(2) The shareholders had provided all the necessary financial support to [Company C] throughout all the years and [Company C] is still in operation now. Therefore, [Company C] has no going concern problem at all. A letter of financial support was also obtained for the year ended March 31, 1994.

(3) The shareholders of [Company C], who are all wealthy persons, had resolved that they would provide the required funds for this long term investment if needed.'

The appeal hearing

18. The objection was unsuccessful and the Appellants, through their solicitors, Messrs Fairbairn Catley Low & Kong, gave notice of appeal by letter dated 24 January 2002, on the ground that:

> ' in the Determination the Commissioner of Inland Revenue had failed to give due weight to the evidence which showed that the property was acquired by [the Appellants] with an intention for long term investment and thereby erred in holding that the profit arising from the disposal of the property is revenue in nature and is therefore subject to profits tax'.

19. At the hearing of the appeal, the Appellants were represented by counsel, Mr Richard Leung, and the Respondent was represented by Ms Cheung Mei-fan, assessor.

20. Mr Richard Leung called four persons, namely Mr D, Mr E, Ms P and Mr Q, to give oral evidence. No witness was called by Ms Cheung Mei-fan.

21. Mr Richard Leung cited:

(a) Simmons v IRC [1980] 1 WLR 1196

(b) All Best Wishes Limited v CIR [1992] 3 HKTC 750

(c) Wing On Cheong Investment Co Ltd v CIR 3 HKTC 1

22. Ms Cheung Mei-fan cited:

(a) D11/80, IRBRD, vol 1, 374

(b) Hillerns and Fowler v Murray 17 TC 77

(c) Chan Sau-kut and Another v Gray & Iron Construction & Engineering Co (a firm) [1986] HKLR 84

(d) Sections 2, 14, 22 and 68 of the IRO

23. Just before Ms Cheung Mei-fan began her oral submission, Mr Richard Leung applied for permission to amend the ground of appeal by adding the following ground:

> ' Even if the Board were to find that the Property was acquired by [the Appellants] without an intention for long term investment, in any event, the profits tax assessed should be levied separately on each of the taxpayer companies in accordance with

> the profits that it shared, with [Company C] being able to bring forward its tax loss to set off its shared profits in the transaction.'

Ms Cheung Mei-fan said in the course of her submission on this proposed ground that the proper course was for the Appellants to apply for set-off under section 19C(4) of the IRO and that the set-off would be applied if the Appellants were to apply on the working day after the hearing of the appeal. Mr Richard Leung withdrew his application to amend.

Our decision

24. Section 68(4) of the IRO provides that the onus of proving that the assessment appealed against is excessive or incorrect is on the Appellants. Section 2 defines 'trade' as including 'every trade and manufacture, and every adventure and concern in the nature of trade'. Section 14(1) excludes profits arising from the sale of capital assets.

25. We remind ourselves of what Sir Nicholas Browne-Wilkinson VC said in Marson v Morton [1986] 1 WLR 1343 at pages 1347 to 1349 and [1986] STC 463 at pages 470 to 471; what Lord Wilberforce authoritatively stated in Simmons v IRC [1980] 1 WLR 1196 at page 1199 and (1980) 53 Tax Cases 461 at pages 491 to 492; and the statement of the law by Orr LJ at pages 488 and 489 of the report in Tax Cases, which was approved by Lord Wilberforce as a generally correct statement (WLR at page 1202 and Tax Cases at page 495).

26. We also remind ourselves of what Mortimer J, as he then was, said in All Best Wishes Limited v CIR [1992] 3 HKTC 750 at page 771:

> ' *The Taxpayer submits that this intention, once established, is determinative of the issue. That there has been no finding of a change of intention, so a finding that the intention at the time of the acquisition of the land that it was for development is conclusive. I am unable to accept that submission quite in its entirety.*
>
> *I am, of course, bound by the Decision in the Simmons case, but it does not go quite as far as is submitted. This is a decision of fact and the fact to be decided is defined by the Statute – was this an adventure and concern in the nature of trade? 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 commonplace 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 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. Having said that, I do not intend in any way to minimize the difficulties which sometimes arise in drawing the line in cases such as this, between trading and investment.' (at page 771)

27. The citation of the Wing On Cheong Investment case reminded us of what Mortimer J said in All Best Wishes:

> '*Reference to cases where analogous facts are decided, is of limited value unless the principle behind those analogous facts can be clearly identified.'* (at page 770)

28. The stated intention was long term holding for rental income.

29. There is no self-apparent reason why the three Appellants should join together in investing in the Property, if investment it was. Mr D asserted that:

> 'Well, [Company B] at that time were looking for a partner to share the investment because at that time we think [Company B] might not be capable enough for such an investment.'

30. We have no doubt that Company B did not have the financial ability to complete the acquisition of the Property at the price of $14,980,000, not to mention holding it for an indefinite period. Its profit and loss accounts for the years ended 31 March 1993 and 31 March 1994 showed losses of $606,211 and $396,763 respectively. Its balance sheets for those two years showed shareholders' deficits of $606,211 and $396,763 respectively. The net current liabilities of $823,208 and $12,330,090 were made up as follows:

	1994	**1993**
	$	$
Current assets		
Cash at bank	735,112	614,587
Deposits and prepayments	4,254,209	2,304,768
Accounts receivable	871,222	58,161
Amount due from a related company	10,000	340,000
	5,870,543	3,317,516
Less: Current liabilities		
Bank overdrafts (secured)	231,723	-

Amounts due to directors	3,462,845	3,012,525
Amounts due to related companies	2,783,600	30,000
Current portion of long-term loans (secured)	1,242,436	284,845
Accrued charges	9,732	719,354
Deposits received	8,400,900	94,000
Accounts payable	2,069,397	-
	18,200,633	4,140,724
	(12,330,090)	(823,208)

31. Company C's shareholders' deficits were comparable to the shareholders' deficits of Company B. It is nonsensical to bring in Company C as a 'partner to share the investment because at that time ... [Company B] might not be capable enough for such an investment'. Accountants' Firm L, Company C's auditors, said this in their report to members of Company C for the year ended 31 March 1994:

> ' We have not been invited to attend the stock taking ...
>
> We have not been able to obtain sufficient information to satisfy ourselves as to the existence of these deposits [$776,063].
>
> The balance sheet has been prepared on a going concern basis. In view of the significant accumulated deficits and net liabilities at March 31, 1994 continuance in business as a going concern is dependent upon the company attaining future profitable operations and the financial support of its bankers and directors.
>
> Should the Company be unable to continue in business as a going concern, adjustments would have to be made to reduce the value of assets to their recoverable amount, to provide for any further liabilities which might arise, and to reclassify fixed assets as current assets.
>
> Subject to the foregoings ...'

Company C's profit and loss accounts for the years ended 31 March 1993 and 31 March 1994 showed losses of $499,346 and $755,281 respectively. Its balance sheets for those two years showed shareholders' deficits of $489,346 and $745,281 respectively. The net current liabilities of $522,083 and $777,456 were made up as follows:

	1994	**1993**
	$	$
Current assets		
Cash on hand	492	24

Accounts receivable	4,952,362	3,194,738
Deposits and prepaym (*sic*)	793,805	495,013
Amount due from a di (*sic*)	4,470,494	4.043,340
Inventories	441,000	580,413
	10,658,153	8,313,528
Less: Current liabilit (*sic*)		
Bank loans and overd (*sic*)	1,887,478	2,506,916
Accounts payable	800,545	1,704,756
Bills payable	8,649,033	4,577,942
Accrued expenses	98,553	45,997
	11,435,609	8,835,611
	(777,456)	(522,083)

32. While Company A was not in the red, it clearly did not have the financial means to help Company B complete the acquisition of the Property or to hold it for an indefinite period. Its profit and loss accounts for the period from the date of incorporation on 7 May 1992 to 31 March 1994 showed a profit of 725,439. Its balance sheet as at 31 March 1994 showed shareholders' funds of $825,439. The net current assets of $759,079 (with $594,607 due from a related company and thus dependent on the ability of the related company to pay its debts as and when due) were made up as follows:

	1994
	$
Current assets	
Cash at bank	141,260
Accounts receivable	3,987,252
Prepayments	125,000
Amount due from a related company	594,607
	4,848,119
Less: Current liabilities	
Bank overdraft	527,924
Accounts payable	3,377,543
Accrued charges	24,288
Profits tax payable	159,285
	4,089,040
	759,079

33. As at 31 March 1994, the aggregate shareholders' deficits of Companies B and C exceeded the shareholders' funds of Company A by $316,605 ($396,763 + $745,281 - $825,439).

34. As 20% of the price had been paid, the Appellants would have needed 10% to 20% of the price of $14,980,000, depending on whether the bank financing was 70% or 60% of the price, were they to complete the acquisition. Mr D asserted in his testimony that the Appellants would source it from:

> '... cash in bank or the available credit line or cash flow they have ... and the directors'.

35. The Appellants' cash on hand or in bank as at 31 March 1993 and 31 March 1994 totalled less than $1,498,000 (see paragraphs 30 to 32 above). In any event, since the Appellants' aggregate current liabilities exceeded the aggregate current assets, the Appellants simply did not have $1,498,000 (let alone $2,996,000) to fund the completion of the acquisition.

36. There is no evidence of any available credit line. In any event, borrowing had to be repaid with interest.

37. There is no evidence on the cash flow of any of the Appellants which had an aggregate net current liability.

38. There is no evidence on the personal net worth as at September 1993 or April 1994 of any of the shareholders or directors of the Appellants. There is no evidence on the cash flow of any of them. What we do have is the admission by Mr D that he was the director shown in the audited accounts of Company C to be indebted to Company C in excess of $4,000,000. In this context we note that Company B, a company with shareholders' deficits, was indebted to directors and related companies. What we also have is the admission by Mr E that it was 'probably correct' that he had difficulty servicing the bank loan of $1,600,000 in respect of a property jointly acquired by him and his wife on 15 October 1991 and sold on 5 September 1992.

39. Even if the Appellants should somehow manage to complete the acquisition, there is still no evidence of their financial ability to hold the Property for an indefinite period. None of the Appellants' witnesses pointed to the actual rental of any or any comparable property. Whilst on rental, we see no commercial sense in borrowing at least 70% (depending on the extent of utilisation of 'available credit line') of the price at 8.25% interest for an alleged 6.9% rental return (assuming that we accept the assertion of 6.9% rental return which we do not).

40. In support of their objection and in support of their appeal, the Appellants uttered and relied on copy documents purporting to be:

(a) joint venture agreement dated 1 September 1993 made by the Appellants;

(b) minutes of an extraordinary general meeting of Company C held at Address R on 1 September 1993 at 10:00 a.m.;

(c) minutes of an extraordinary general meeting of Company A held at Address S on 1 September 1993 at 10:30 a.m.;

(d) minutes of an extraordinary general meeting of Company B held at Address R on 1 September 1993 at 11:30 a.m.;

(e) minutes of a board meeting of Company C held at Address R on 27 January 1994 at 10:00 a.m.;

(f) minutes of a board meeting of Company A held at Address S on 27 January 1994 at 10:30 a.m.; and

(g) minutes of a board meeting of Company B held at Address R on 27 January 1994 at 11:30 a.m.

41. (a) was referred to in the explanatory note of the tax computations of Companies A and B [see paragraph 10(b) above] and a copy was sent to the Respondent under cover of the letter dated 5 November 1996 from Accountants' Firm L.

42. Copies of (b) to (d) and (e) to (g) were sent under cover of the letter dated 19 September 2001 by Accountants' Firm L [see paragraph 17 above].

43. In our decision, all the documents, (a) to (g), were not authentic and not contemporaneous. (a) was made up at or about the time when the tax computations of Companies A and B were prepared. (b) to (d) and (e) to (g) were made up at about the time of the letter of Accountants' Firm L dated 19 September 2001.

44. (a) purported to be a joint venture agreement dated 1 September 1993 by which the Appellants agreed to invest in the Property in equal shares. As (b) to (d) all referred to the joint venture agreement having been entered, the joint venture agreement must have been signed before 10:00 a.m. when the first of the three meetings was said to be held. The Appellants would have us believe that on 1 September 1993:

(a) Mr E signed the joint venture agreement on behalf of Company B sometime before 10:00 a.m.;

(b) Mr D signed the joint venture agreement on behalf of Company C sometime before 10:00 a.m.;

(c) Ms F signed the joint venture agreement on behalf of Company A sometime before 10:00 a.m.;

(d) Mr D and Mr E then attended an extraordinary general meeting of Company C at 10:00 a.m. at Address R;

(e) Mr D, Mr E, Ms F and Mr G then attended an extraordinary general meeting of Company A at 10:30 a.m. at Address S;

(f) Mr D and Mr E then returned to Address R to attend an extraordinary general meeting of Company B at 11:30 a.m.

45. If the joint venture agreement had in fact come into existence on 1 September 1993, there is no reason why there was no mention whatever of any co-investors in the audited financial statements of Company B for the year ended 31 March 1994 which were prepared on the basis that Company B was entering the transaction alone. There is also no reason why the 'co-investment' was not mentioned and not reflected in the audited financial statements of Company A or Company C for the year or period ended 31 March 1994. In our decision, (a) was made up at or about the time when the tax computations of Companies A and B were prepared.

46. Mr D asserted that he attended all three meetings on 1 September 1993 and alleged that the Company A meeting was held at Address R, and not Address S. If the meetings had in fact been held, and if (b) to (d) were authentic and contemporaneous, there is no reason why the Company A minutes should not have correctly recorded the place where it was in fact held. There was no or no plausible explanation. The following resolution was passed at all meetings:

> 'It was noted that an Joint Venture Agreement has been entered among [names of the other two Appellants] and the Company on 1 September 1993 for purchasing a property at [Address K] at the price of HK$14,980,000.00 in equal shares.
>
> It was resolved that the subject purchase be ratified and approved and that the shareholders hereby unconditionally agree to provide financial supports to the Company for the above investment in the form of either shareholders' loans or share capital when required.'

What was noted was the entering of 'an Joint Venture Agreement ... on 1 September 1993 ... at the price of HK$14,980,000.00'. 1 September 1993 was the very day of the meetings. More importantly, no price was mentioned in the joint venture agreement. The resolution was that 'the subject purchase be ratified and approved'. As no purchase had in fact been made by 1 September 1993, there was no purchase to ratify or approve. Last but not least, Mr G left Hong Kong on 29 August 1993 and did not return until 13 September 1993. He could not possibly have

attended the Company A meeting on 1 September 1993. In our decision, (b) to (d) were made up at about the time of the letter of Accountants' Firm L dated 19 September 2001.

47. We turn now to (e) to (g). The Appellants would have us believe that on 27 January 1994, the following board meetings were in fact held:

(a) Mr D, Mr E, Mr H and Ms I attended the board meeting of Company C at 10:00 a.m. at Address R;

(b) Mr D, Mr E, Ms F and Mr G then attended an extraordinary general meeting of Company A at 10:30 a.m. at Address S;

(c) Mr D and Mr E then returned to Address R to attend the board meeting of Company B at 11:30 a.m. with Mr D also representing Company C and Ms F representing Company A.

Mr D asserted that he attended all three meetings and alleged that the Company A meeting was held at Address R, and not Address S. If the meetings had in fact been held, and if (e) to (g) were authentic and contemporaneous, there is no reason why the Company A minutes should not have correctly recorded the place where it was in fact held. That (e) to (g) were made up afterwards is evidenced by the fact that Ms I did not become a director of Company C until many years after 27 January 1994 (see paragraph 6 above). In our decision, (e) to (g) were made up at about the time of the letter of Accountants' Firm L dated 19 September 2001.

48. The oral evidence is just as bad. In our assessment, Mr D, Mr E and Mr Q were **not** truthful witnesses. What Mr Q said in evidence was not consistent with the letter dated 1 June 2001 from Bank O which was initialled by him before it was sent:

> 'The handling officer recalled that the property market was volatile and speculative at that time, so our bank showed no interest to commit the said mortgage and therefore reject the loan application.'

49. For the reasons we have given, the Appellants have not proved any of the following and their case of capital asset fails:

(a) that at the time of the acquisition, the intention of the Appellants was to hold the Property on a long term basis;

(b) that such intention was genuinely held, realistic or realisable;

(c) their financial ability, whether alone or collectively, with or without their shareholders, to complete the acquisition of the Property;

(d) their financial ability, whether alone or collectively, with or without their shareholders, to keep the Property for an indefinite period.

Disposition

50. We dismiss the appeal and confirm the assessment as confirmed by the Commissioner.

Costs order

51. We are of the opinion that this appeal is frivolous and vexatious and an abuse of the process. This was a quick confirmor sale where the Appellants clearly did not have the financial means to complete the acquisition or to keep the Property for an indefinite period. We deprecate the Appellants for putting forward and relying on documents which are not authentic, see D42/99, IRBRD, vol 14, 445. Pursuant to section 68(9) of the IRO, we order the Appellants to pay the sum of $5,000 as costs of the Board, which $5,000 shall be added to the tax charged and recovered therewith.