

# INLAND REVENUE BOARD OF REVIEW DECISIONS

## Case No. D67/96

**Profits tax** – asset betterment – large unexplained transactions – taxpayer failed to discharge onus.

Panel: Audrey Eu Yuet Mee QC (chairman), Gerald To Hin Tsun and William Tsui Hing Chuen.

Dates of hearing: 10 and 29 October 1996.

Date of decision: 18 November 1996.

### **Appeal dismissed.**

Case referred to:

D28/88, IRBRD, vol 3, 312

Chor Hon Chung for the Commissioner of Inland Revenue.

Yuen Kim Hung Michael of Messrs Poon Mak & Wan for the taxpayer.

### **Decision:**

1. The Taxpayer appeals against the Commissioner's determination in respect of the revised profits tax assessments on him for the years of assessment 1984/85 to 1990/91.

#### **A. BACKGROUND**

A.1 The Taxpayer was a fixed pitch hawker in District A. He said he was told by friends that, as a hawker, he did not have to pay tax as his income would have been low. He did not keep books and did not file profits or salaries tax returns.

A.2 In November 1990, the Inland Revenue commenced investigation into the Taxpayer's tax affairs. The Taxpayer was first interviewed by the Revenue on 14 November 1990. A detailed note was taken of the interview and sent to the Taxpayer by a cover letter dated 30 November 1990 inviting the Taxpayer to check the accuracy of the interview note and to make corrections where necessary. The letter and the interview note were in both English and Chinese. On 7 January 1991, the Taxpayer's then tax adviser returned to the Revenue a copy of the interview note as signed by the Taxpayer and with certain supplements and amendments at the back thereof.

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A.3 According to the interview note, the Taxpayer told the Revenue that he had four sources of income:

(a) Employment

He was a part time employee of Company B working 2 – 3 hours a day, usually in the afternoon. He was paid \$2,000 per month with an extra month's salary in January as bonus.

(b) Jade Hawker Pitch

He operated a fixed pitch hawker stall in District A. He estimated that his stock on hand on the day of the interview was \$100,000 to \$300,000. Daily turnover ranged from a few thousand dollars to ten thousand dollars.

(c) Jade Consignment

He would sell jade for others on consignment basis and earn a commission at the discretion of the consignors.

(d) Purchase of Motor Vehicle Parts

He would earn commission from making purchases of motor vehicle parts in Hong Kong on behalf of organisations in Country C. The commission was fixed by the Country C agencies.

A.4 At the interview, the Taxpayer showed the Revenue documents relating to 31 savings and current accounts in his name or in the joint names of himself and his wife. Some of these were for multi-currencies or foreign currencies such as Australian, Canadian, Japanese, New Zealand or United States currency.

A.5 Subsequent to the interview, the Taxpayer mentioned another 8 other bank accounts plus two overseas accounts in Country D in the names of himself and his wife.

A.6 As a result of the investigation, the Taxpayer later filed salaries and profits tax returns. However no contemporaneous books or records were produced. The Taxpayer's many accounts showed very substantial dealings. Based on the information supplied, the Inland Revenue prepared two asset betterment statements in respect of the Taxpayer.

### **B. THE ASSETS BETTERMENT STATEMENTS**

B.1 The Revenue worked out the Taxpayer's assets for each year ending 31 March for the relevant years of assessment from 1984/85 to 1990/91. The major part of the assets was bank balances and time deposits as at the relevant dates. These do not include anything in the two overseas bank accounts referred to earlier. The Taxpayer claimed that the monies in the two overseas accounts do not belong to him or his wife and he refused to disclose the bank statements or balances.

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B.2 During the relevant years, the Taxpayer had made substantial payments or remittances to his sons and daughters-in-law. There were also a number of unidentified cash withdrawals ranging from \$1,000,000 to \$2,000,000 on each occasion. The Revenue included these payments, remittances or unidentified cash withdrawals as assets of the Taxpayer. The total assets betterment during the relevant years came to \$24,470,229.

B.3 The Taxpayer objected to the assets betterment statement. He said that the balances in the bank accounts of him and his wife were partly sale proceeds of jade consigned or entrusted to him and partly monies he held on behalf of organizations in Country C.

B.4 Subsequent to his objection, the assets betterment statement was revised such that the unidentified withdrawals in the years ending 31 March 1990 and 1991 were taken out of the assets and the betterment was reduced from \$24,470,229 in the earlier statement to \$13,665,365 in the revised statement.

B.5 The Commissioner's determination was based on the revised assets betterment statement. The Taxpayer objected to this as being excessive and appeals to this Board.

### C. THE LAW

C.1 Section 68(4) of the Inland Revenue Ordinance places on the Taxpayer the onus of proving that the assessment appealed against is excessive or incorrect.

C.2 This is particularly important in a case involving assets betterment statements which, by their very nature, do not pretend to be accurate or precise in estimating the taxable position. We refer to the test laid down in D28/88, IRBRD, vol 3, 312 at page 317:

*'An assets betterment statement in its final or revised form is nothing more than an account of how the assessor has arrived at estimating the taxable profit of a taxpayer. It is not and does not pretend to be accurate or precise. It is merely a calculation of a taxpayer's income on a 'net assets basis' in default of any other available information. If a taxpayer is aggrieved by an assessment founded on such a statement, it is for him to show how and to what extent it is incorrect or excessive. If he fails to do that, the assessment will be confirmed. It is for the taxpayer to displace the assessment. The taxpayer can blame no one except himself for such a state of affairs having arisen and can blame no one except himself if he finds it difficult to discharge the burden and prove that the betterment profit revealed by the assets betterment statement is wrong. The onus is not discharged by the taxpayer simply appearing before the Board and saying that the assets betterment statement is wrong. The onus is not discharged by the taxpayer if he leaves the Board in a state of conjecture by his failure to give evidence on matters peculiarly within his knowledge. If he elects to remain silent or is unable to give detailed and acceptable evidence or is unable to obtain independent acceptable documentary evidence and to call*

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*witnesses to substantiate the truth of what he says, then he leaves the Board with no alternative but to uphold the assessments based on the assets betterment statement because, like the Commissioner before it, the Board has no better means of ascertaining the true profits of the taxpayer.*

*The assets betterment statement method of estimating the income of a taxpayer provides the taxpayer with the opportunity, if he is aggrieved by the assessment raised on that basis, of satisfying the Board that the increase in his wealth did not arise from his business activities. If at the end of the Board hearing there is no acceptable evidence or insufficient evidence to warrant a conclusion that the assessments are excessive, then the same must stand.'*

We would go further, even when the Board suspects that the assessments may be excessive, if the Taxpayer has not given credible evidence as to how excessive, the Board cannot help, by way of speculation or conjecture, as to how the assessments can be reduced.

C.3 We turn to see what the Taxpayer says about the asset betterment statements.

### **D. THE EVIDENCE**

D.1 The Taxpayer is represented by Mr Yuen, his tax representative. Mr Yuen informed us that the total assets in the statements are agreed. What is disputed is that part of the cash in the accounts belonged to third parties. The unidentified cash withdrawals were repayments to these third parties.

D.2 The Taxpayer was the only witness. He and his wife live in a flat in District E purchased in 1987 for \$325,000. According to the interview note, his monthly living expenses was in the region of \$2,000 to \$3,000. They have three sons, Mr F, the eldest in Country D, and Mr G and Mr H who were at the material time construction workers residing in Hong Kong.

D.3 His evidence mainly dealt with money from two sources:

- (a) deposits for Country C organizations;
- (b) sale proceeds of jade on consignment basis.

#### **Deposits for Country C organizations**

D.4 Association I is an association in Country C receiving donations from Hong Kong and one other city. Its function is to liaise with Chinese overseas. It is said to be country controlled.

D.5 Company J is a country owned commercial enterprise which imports cars or motor spare parts into Country C.

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D.6 Mr K, a civil servant of the Country C Government, was the man behind both Association I and Company J. He was the classmate of the Taxpayer's son and had known the Taxpayer and his family for some twenty years. There has been various changes of personnel. Mr K might now have been posted elsewhere as there had been little contact with him in the last three years. There had also been changes in other officers such as managers or salesmen over the years.

D.7 Although it was apparently their business to receive donations, for reasons unexplained, neither Association I nor Company J had any bank account in their names in Hong Kong. Instead money was to be paid into one of the many accounts of the Taxpayer, his wife or one of his sons, mixed with their own personal funds. From time to time, someone would ring up the Taxpayer informing him that a deposit had been made and the Taxpayer would bring the passbooks to the bank for stamping. Such amounts might be a few thousand each time, but usually tens of thousands and sometimes hundreds of thousands. The person who telephoned might be a collector who had gathered and grouped together the donations. Some of the deposits might be donations for building a school. Sometimes the deposits were for Company J, they might be from individuals or companies. It was not clear who these individuals or companies were. It was not clear why donations would be made to Company J, a commercial enterprise. The Taxpayer explained that both Company J and Association I were country owned, commercial secrets were country secret and there were often internal transfer between them.

D.8 The Taxpayer never gave any receipt for these deposits. He was unable to estimate the total amount of the deposits received over the years. Nor could he remember the names of the persons who called him to inform him of the deposits.

D.9 The money so deposited was remitted to the Taxpayer's eldest son Mr F in Country D. He was supposed to buy second hand cars for import to Country C. But the Taxpayer was rather coy and repeatedly qualified his answer by saying he had no personal knowledge of this and merely relied on what his son said he had done with the money.

D.10 According to the Taxpayer, about \$5,600,000 had been remitted out for the purchase of cars or spare parts. As the Revenue had pressed him for documentary proof, he had gone to Association I and Company J and obtained various statements from these two organizations. According to one such statement dated 19 May 1993 from Association I, the Taxpayer had remitted out about \$3,000,000. According to another dated 20 May 1993 from Company J, the Taxpayer had remitted out about \$2,600,000. The Taxpayer explained that the two organizations would do internal transfers such that the total remittance of \$5,600,000 was apportioned between the two. After the purchases, there was still some surplus left over in his accounts which he had handed back to Company J and Association I.

D.11 The Taxpayer's two sons in Hong Kong, Mr G and Mr H assisted in the transactions by remitting money overseas, placing orders for the cars or spare parts, dealing with the paper work, liaising with various parties, etc. None of them, whether the Taxpayer or his two sons in Hong Kong, was paid in any way for the work and for the use of their

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accounts. They had the benefit of the interest and made some exchange gain although there was exchange loss at times.

D.12 The Taxpayer was reminded that in the interview note for 14 November 1990, which he had signed as accurate, it was recorded that he earned a commission for this type of transaction, which commission was determined by the Country C agencies. He agreed that his tax representative had gone over the interview note with him. He said he knew there were minor mistakes or discrepancies in the interview note but he did not bother to correct them.

D.13 Other than the various statements from Company J or Association I, the Taxpayer was unable to produce any documentary evidence. He explained that he did keep scraps of paper where the outstanding balances were written down but once the balances were checked and said to be accurate he would throw away the scraps of paper. Needless to say, he could not identify the deposits or remittances in his bank accounts.

### **Sale proceeds of jade on a consignment basis**

D.14 His eldest son's father-in-law was Mr L. Mr L lived abroad. He had asked various persons to bring packets of jade to the Taxpayer for sale in Hong Kong. According to one of the letters produced, Mr L died in 1984.

D.15 The Taxpayer could not remember details such as when Mr L died, how many times the Taxpayer received jade, when was the last time he sold the jade, etc. He could only say that the total proceeds of sale were just over \$2,200,000. Mr L had died many years ago and the proceeds were left with the Taxpayer. At some stage, the Taxpayer could not remember when, he remitted the proceeds to his son in Country D who was supposed to return the money to the widow Mrs L. The Taxpayer could not identify these remittances from his bank accounts. Instead of remitting the whole amount in one go, he did so in various amounts over a period of time. At first he said this was to avoid loss of the money, when pressed, he said he wanted to hang on to the money longer for the interest.

D.16 This was supported by a letter obviously written by his son confirming that \$2,200,000 were proceeds from the sale of jade. The letter bore the name of Mrs L, but the Taxpayer is unable to confirm if it was signed by her.

D.17 Apart from the letter, there is no record of jade from Mr L. No receipt was ever given. After the proceeds were remitted, the packets on which were written the records of the sales were thrown away.

D.18 The Taxpayer was not paid any commission for jade from Mr L. However it was agreed that he could keep the interest on the proceeds and the small balance over \$2,200,000.

D.19 In a letter dated 28 February 1991 from the then tax adviser to the Revenue, the Taxpayer named three other persons in Country M who had consigned jade to him for sale.

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He confirmed the names and addresses of these persons in his evidence. It started in 1984. At first the quantities were small, about a few ten thousands. It peaked in 1989. Sometimes he received articles to the amount of \$3-4 million, \$5-6 million or even \$7-8 million. It averaged \$2-3 million per consignor. He did not have to give any security or any receipt for the jade or the proceeds of sale. The annual sale was over \$10 million to even \$20 million. He only received a commission of 0.1 – 0.2% depending on the consignor. Sometimes if there was a loss, no commission was payable.

D.20 The consignors would come to Hong Kong around 3 – 6 months' intervals or sometimes even longer when the Taxpayer would pay them the proceeds and tell them which packets had been sold and which packets remained.

D.21 The Taxpayer said he did record the dealings on paper but the papers were thrown away once the amounts were settled. Two of the three consignors had now passed away. He could not identify the amounts in his bank accounts which represented repayments of the sale proceeds to the consignors.

### **Other Suppliers**

D.22 The Taxpayer claimed in one of his letters to the Revenue dated 15 June 1993 that part of the money in his accounts represented outstanding payment due to his suppliers for purchases he had made. He was asked to name some of his suppliers referred to. He said he could not remember as it was so long ago.

### **Overseas bank accounts**

D.23 He was asked about the two overseas accounts. These accounts were operated by Mr F by means of a power of attorney. The money did not belong to Mr F. It was used to separate his personal funds from funds remitted to him for the purchase of cars or spare parts.

D.24 On one occasion, when the Taxpayer and his wife were travelling abroad, he was short of money and borrowed some money from one of these overseas accounts. Later when he returned to Hong Kong, he repaid the money by remitting to the account. According to Schedule 8 of the assets betterment statement, the Taxpayer remitted a sum of \$148,447 on 12 December 1989 to his overseas account. The Taxpayer said this was the repayment. Yet according to a letter dated 28 February 1991 from his tax representative, the Taxpayer claimed that he and his wife only spent \$16,000 during the trip in November 1989. When this was pointed out to him, the Taxpayer said the \$148,447 was to repay his gambling losses. He was reminded that in the interview note of 14 November 1990, which he signed, he claimed to have no significant winning or loss in gambling. He could not really explain the discrepancy.

## **E. REASONS FOR DECISION**

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E.1 The Taxpayer appeared to be a man of modest circumstances. He and his wife lived in a modest flat. The monthly expenses was only \$2,000 to \$3,000. He operated a fixed pitch hawker stall and did part time work which paid \$2,000 a month.

E.2 Yet he operated an unusually large number of bank accounts. The amount of cash in banks and time deposits (excluding the overseas accounts) rose from \$174,528 as at 31 March 1984 to \$13,750,604 as at 31 March 1989. We have to consider the Taxpayer's explanation for this increase.

E.3 The Taxpayer's account of the deposits (D.4 to D.7) is truly amazing and totally incredible. Clearly the deposits could not be 'donations' to Association I or Company J. No genuine donors or collectors of donations would agree to pay donations into different personal accounts without even a receipt. If they were 'donations', they were clearly not used for the purpose intended. Money intended to build a school was used to buy cars and spare parts instead.

E.4 Although the bulk of the money was said to be used to buy cars or spare parts, money was not remitted directly to the suppliers. According to Schedule 8 of the assets betterment statement, substantial sums were remitted to the overseas accounts of the Taxpayer, his wife, his two sons Mr F and Mr H. The total came to \$6,765,724 in the years ending 31 March 1990 and 31 March 1991. According to Schedule 9, amounts totalling \$2,118,700 were paid into the accounts of his other son Mr G in the year ending 31 March 1991. There is no credible explanation as to why the remittances had to be made to these accounts if they were meant for the purchase of cars or spare parts. When asked, the Taxpayer explained that he was not free to send the remittances, the bank would not let his son send the remittances unless the money was first transferred to his son's account. If the Taxpayer was able to transfer the money into the accounts of his sons in Hong Kong he would be able to remit them to his son in Country D. There was also no reason why any money should be sent to the overseas account of Mr H. Thus the pattern of remittances does not support the Taxpayer's evidence as to what the money was used for. Other than unidentified cash withdrawals, the substantial payments and remittances were all to members of the Taxpayer's family.

E.5 Still on the remittances, we do not accept the Taxpayer's evidence that he remitted \$148,447 to his overseas account to repay his gambling losses while travelling abroad. This was wholly inconsistent with the information he had earlier supplied to the Revenue through his tax representative (see D.24 above). A gambling loss of \$148,447 was extremely unlikely and very significant in the light of his \$2,000 to \$3,000 living expenses every month and his \$16,000 travelling expenses claimed. He would hardly have forgotten to mention it when specifically asked about his gambling habits.

E.6 We also have regard to the interview note of 14 November 1990 where it was clearly stated that the Taxpayer earned commission from making purchases of motor vehicle parts and that the commission he received was set by the Country C agencies. Yet when he gave evidence, he denied receiving any commission in respect of these transactions, despite the work he and his sons in Hong Kong did. He had ample time to



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consider the interview note, he was specifically invited to make corrections and he did make some corrections. It was not his case that he was unaware of any mistake. He said he knew there were minor discrepancies but did not bother to make the corrections. We find an inconsistency on such crucial point impossible to accept. The Taxpayer was being investigated by the Revenue for failure to report his income. A mistake as to whether commission was payable could not be said to be minor nor could it have gone undetected. We do not accept that he received no benefit from these transactions other than interest or exchange gains as he claimed.

E.7 Although Association I and Company J featured significantly in the Taxpayer's evidence, there was no specific mention of these two organizations in the interview note. Furthermore in paragraph (1) of the interview note, the Taxpayer only mentioned remittances for the sale of Mr L's jade. He said apart from this, he did not remit any sum out of Hong Kong. Yet Schedule 8 to the assets betterment statement shows substantial remittances out of Hong Kong to accounts of the family members. The statements from Association I and Company J purported to certify remittances out of \$3,000,000 and \$2,600,000. It was totally unclear how these \$3,000,000 or \$2,600,000 were remitted for Association I or Company J. In the circumstances, we do not attach any weight to the statements.

E.8 We also reject the Taxpayer's evidence on the jade consignment. We do not accept his evidence that Mr L left jade or sale proceeds of \$2,200,000 with the Taxpayer for years without any receipt or record. He was clearly making up excuses in the course of his evidence when asked why he did not repay the \$2,200,000 sale proceeds in one lump sum (see D.15 above).

E.9 Similarly we do not accept that the gentlemen from Country M left substantial amounts of jade of millions of dollars with the Taxpayer without any receipt or security. According to the interview note, the jade stock he had in November 1990 was some \$100,000 to \$300,000 and his daily turnover was modest. This was in stark contrast to his evidence that turnover came to some \$10 million or \$20 million a year with the consignments.

E.10 The Taxpayer was vague and evasive. His evidence was punctuated by repeated excuses (which did not always come out in the interpretation) that his memory was poor especially after he had fainted on a few occasions. The vagueness was partly due to the lack of records. It was only too convenient an excuse that the records were thrown away or that events took place a long time ago. We believe that the Taxpayer deliberately tried to cover his tracks by not having any records, by opening numerous bank accounts, by mixing the money and by making large cash withdrawals which cannot be traced.

E.11 We do not accept that the Taxpayer has told us the full story. It might well be that much of money in the Taxpayer's accounts belonged to third parties. However the Taxpayer is unable to give a credible account of how much or which portion of it belonged to whom. In the circumstances we cannot help him by speculation or conjecture.

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E.12           Accordingly for reasons given, we find that the Taxpayer has not discharged the onus and the appeal is accordingly dismissed.