IN THE COURT OF REVIEW
AT SUVA

IN THE MATTER of an appeal to the **Income Tax Court of Review** (Appeal No: 12/2006)

BETWEEN : **TOKYU CORPORATION**

Appellant

AND : **THE COMMISSIONER OF INLAND REVENUE**

Respondent

R. Newton & P. Knight for Appellant
M. Scott for Respondent

Dates of Hearings	:	12 & 13 December 2007
Dates of Final Submissions	:	October 2008
Date of Judgment	:	1 December 2008

Judgment

This case concerns the sale of Mago Island in the Lau group of Fiji. The island has an interesting history which does not need repeating here. In 1985 Mago Island was acquired by a Japanese incorporated company, Tokyu Corporation, which is also listed in the Tokyo Stock Exchange. Tokyu Corporation resold the island in 2005. It is the imposition of tax on this resale which is the genesis of this appeal.

It is pertinent to state the grounds of appeal:

1. That the Appellant is not liable for tax under the Income Tax Act for any profit earned on the sale of Mago Island as comprised in Certificate of Title 54/5330 ("the property") because:

a) the Appellant did not acquire the property for the purpose of selling or otherwise disposing of the ownership of it; and/or

b) the Appellant did not carry out any undertaking or scheme entered into or devised for the purpose of making a profit and/or;

c) any profit earned on the sale of the property was not derived from purchase and sale which formed part of a series of transactions and which was not itself in the nature of trade or business.

2. Alternatively, section 11)a) of the Income Tax Act has no application to the said sale.

3. Alternatively, that the Appellant is not liable for the amount of tax for which it has been assessed because it did not make the alleged profit of $6,200,219.49 or any profit on the sale of the property.

4. Alternatively, the calculation of the alleged profit is incorrect.

5. Alternatively, expenses incurred during the Appellant's ownership of the property have not been properly brought to account or allowed as a deduction from the profit.

6. Alternatively, the calculation of tax payable is incorrect.

The Notice of Appeal in this case was filed on 18/10/06. The matter was first called before the Court of Review on 25 April, 2007 since there was no appointment made to the Court until February, 2007. The parties then proceeded to prepare and file an agreed set of facts, documents and attend to pre-trial matters. The case was heard on 12 and 13 December 2007. The proceeding, at the request of the parties, were recorded. However, this created more problems than envisaged. The transcripts could not be certified due to the poor quality of the recordings and consequently the transcripts.

On 25 April 2008, the Court, at the request of the parties, ordered that its handwritten notes be made available to the parties to assist in their submissions. Due to inefficiencies, and a lack of adherence to the court order, the notes were not made available to the parties until five (5) weeks later. The final submissions were received by the Court sometime in October, no date being stamped on the submissions on file. The level of support services to the Court of Review leaves much to be desired. The Court regrets the delays in the disposal of this appeal, and its judgment.

Burden of Proof

Both parties accept, in essence, that the burden of proof in appeals before the Court lies with the tax payer. Section 71 (2) of the **Income Tax Act** makes this clear: "on the hearing and determination of all objections to assessments under this Act, the onus of proof shall be on the taxpayer". The Appellant and Respondent Counsels have put a different gloss to this but the fact remains that it is the Appellant who has to prove its case on a balance of probabilities.

The essence of the Appellant's submission is that: "Tokyu has consistently asserted the sole and dominant purpose of the purchase was to implement the Shangri-la-concept" (para 3, p 2 of initial submissions). In another formulation, it asserts: "The purpose of the acquisition in 1985 was not resale. As a subset, there was no contingent purpose of resale either" (para5 (a), p2).

Learned counsel for the Appellant puts it thus: "If there is only one purpose, as in the case, it becomes irrelevant to inquire into what was the dominant purpose: Holden v Inland Revenue Commission (supra at 872). It follows that any discussion of any incidental or contingent purpose would be irrelevant" (p5 para (6).

The court would, in law, concur with its next statement: "It is of course, irrelevant that after many years Tokyu by way of fresh decision, decided to depart from its original plan and dispose of Mago Island, albeit with overarching concern for continued

preservation of the environment". The genesis of the purchase is the key issue on which the court needs to focus on.

The Court is mindful of the **Civil Evidence Act**, and has considered each witnesses evidence bearing this is mind. The court acknowledges the learned Respondent counsel's submissions on hearsay, multiple hearsay, and grades of hearsay. The Court has considered all evidence which assists it in determining the relevant facts.

The Court is aware that Mr. Gotoh whose dream of the Shangri-la led to the purchase died in 1989, some 4 years after the purchase of Mago Island. It is evident, as Counsel for the Appellant states: "that he was a dominant and charismatic leader". He was the President and Chairman of the Corporation at the time of purchase. Counsel for the Appellant states that: "The best evidence of the purpose intended by a company is necessarily the evidence of its executives and managerial employers together with its corporate records" (para13, page 4). The Appellant called 3 witnesses from Japan and a Japanese businessman resident in Fiji. They gave evidence based on statements already filed in Court. They were extensively cross examined. By consent the parties had filed 3 Volumes of "Agreed Bundle of Documents", which were heavily relied upon during the cross examination of witnesses. These will be referred as Volume 1, Volume 2 and Volume 3 in the judgment.

The Shangri-La Concept

Mr. Gotoh first presented the concept of the Shangri-La at the Sixth General Meeting of the Pacific Basic Economic Council Tourism Committee. It is not clear from the paper (pp1-7) of the Agreed Bundle of Documents **Volume 1**, when this proposal was put before PBEC. I will accept that it was in 1973, as the parties state in the cover sheet. A related document is "The Idea of Shangri-La" by Noboru Gotoh (pp8-23) which the parties date as August 1974. Another version is titled "The Idea of Shangri –

La" submitted to (not stated) authored by Noboru Gotoh, Chairman of the Shangri-La Ad Hoc Committee (pp 24-32).

The vision of Shangri- La envisaged in these papers is stated thus: "to protect the nature remaining in the Pacific Ocean from adverse impact of modern civilization and thereby contribute to the present and future prosperity of humanity" (p2). The objectives are stated as: "firstly, harmony of nature and humanity; secondly, healing through living in nature; and thirdly international exchange". In this version there are proposals for three groups of island or one island for each segment: Recreation island, Mother island and Rehabilitation island. According to this document, "The proposed International Shangri-La in the Pacific Ocean will be made up of a number of islands and the surrounding waters within a confined area in the Pacific Ocean. The area will be bounded by sides, each having a length of 100 to 300km,....." Details of the purposes of each set of island(s) are provided in the documents and need not be repeated.

A tabulated summary is provided at pp14 and 15 with the following statistics:

Islands		Users	Employees		Total	Remarks
			Employees	Families		
Recreation Island		400	100	300	800	
Rehabilitation Island		100	100	300	500	
Mother Island	Management	-	70	210	280	
	Research	-	60	180	240	
	Treatment	-	40	120	160	
	Others	-	80	240	320	Airport, hotel, etc
Total		**500**	**450**	**1,350**	**2,300**	

The mother island, "which could be described as the interface between nature and civilization" will have the airport, hotel, research institute, hospital and management office (p21). At p22 it is noted: "Incidentally, the problem is the location and money.

An island area covering 180 km^2 with one side measuring between 100km and 300km located in a vast water area, is required, with construction cost forecast to rise to Yen 50 billion".

In his August 1974 paper Mr Gotoh talks of his Utopia which he calls Shangri-La: "will commence in a location untouched by man and blessed with nature's virginal pureness. We can be thankful that there are still many stretches of land in the South Pacific that remain spoiled by man" (p25 vol. 1). Further on, in talking of the Shangri-La project he states: "The project aims at protecting a region in the South Pacific from the evils of present day civilization" (p27 vol1). He also mentions that " a hospital and institute for the study of medical science will he built in close co-operation with the International Red Cross and the World Health Organization"(p28). He also states: "Shangri La is not being designed with the idea in mind of building facilities destined for the pursuit of profits. Everybody should be involved in establishing, maintaining and sharing" (p29). He also talks about the active participation of the host country, the need for the local people to be involved since they have the "best knowledge". In calling for the other members of the Pacific Basin Economic Council (Australia, Canada, New Zealand, the USA and Japan) to please examine my proposal he concludes: "I have before me a sheet of paper which is completely blank except for the words Shangri-La written at the top" (p32 vol. 1).

It is evident from the documents tendered that the original plan envisaged a major inter-governmental proposal calling for the use of a substantial area in the Pacific region. In his submissions in reply Counsel for the Appellant states that "the Shangri – La concept had been floated by Mr. Gotoh in the early 1970's through his involvement in PBEC. His objective was to get broader PBEC involvement which ultimately did not eventuate". He further states that the comment: " a sheet of paper which is completely blank except for the words Shangri – La written at the top must be seen as rhetorical flourish and part of his wider proposal to PBEC which was never adopted". He further states: "It was written at a point 11 years prior to the acquisition of Mago Island by the Appellant. The 1974 article was followed by

extensive investigation and refinement by the Appellants own personal prior to the acquisition. The 1974 article is not contemporaneous with the acquisition and merely represents, at highest, a preliminary stage in Mr Gotoh's thinking which later underwent significant evolution".

The underlined words pose considerable problems for the Court. While much material was presented about the initial proposals to PBEC no material was tendered about PBEC's response. Why and whether the PBEC "never adopted" the proposal is not clear. Nor is there any evidence of "extensive investigation and refinement" or "significant evolution".

The evidence of Mr. Makato Watanabe who was closest to Mr. Noburu Gotoh and who had personal dealings with him leaves much to be desired as to how the concept of Shangri –La was extensively investigated and refined. It is evident from all the witnesses for the Appellant that Mr. Gotoh was held in awe by all his subordinates and no one questioned him. As Mr. Watanabe says " The Shangri – La project was a personal interest of Mr. Gotoh's outside of the mainstream of the Tokyo Corporation business "(p2). It is not clear what is meant by this.

When Mago Island was ultimately purchased Mr. Watanabe recalls as follows: "the effect of what Mr. Gotoh said was "I want you to send some property experts with Watanabe to Fiji to complete negotiations for the purchase of Mago Island as soon as possible_ _ _ _ _ _ _ _ _ . I understand Mr. Gotoh to mean he had made a decision to purchase and all that was required was a speedy implementation of that decision. I remember at that time the proposed purchase of Mago Island was seen as fairly strange and controversial amongst Tokyu staff". (emphasis added) The Court has not been informed how Japanese Corporations listed on the Tokyo Stock Exchange operate. What kind of information they are required to file, and how a "personal interest" of a powerful President and Chairman becomes part of the "mainstream business" of the corporation or otherwise.

The most important company document that was tendered was a copy of Tokyu Corporation Annual Report 1986. This includes the President's Report for the year ended March 31st, 1986. It is quite clear that the company has a diversified investment portfolio and business activities including real estate and tourism. The concluding paragraphs of the Chairman and Presidents report states: " The Group has been dedicated to " seeking to enrich mankind" since 1972, and today more than ever we are in a position to apply all our resources to attaining this goal. In addition to transportation developments, retailing and distribution, and recreations and leisure, the Tokyo Group has been vigorously expanding its cable television, consumer credit, and cultural activities in line with this goal"..."The Company and the Group as a whole have also been active overseas, particularly in the Asia – Pacific region. I have long believed that the 21st Century will mark the beginning of the Pacific Era, and the Tokyu Group has been a prime mover in making this come true and in gaining currency for this concept worldwide"(p79 vol 1).

Despite the references to "seeking to enrich mankind" a la Shangri –La and the "Pacific Era" no mention was made of the purchase of Mago island in pursuance or otherwise of this concept by Mr. Noboru Gotoh who was still the Chairman and President. It is noted in the President's report that "Under the leadership of the Tokyu Corporation, the Tokyu Group consists of 315 companies in the tertiary sector and eight educational and cultural foundations". Was Mago island part of one of those foundations? No mention of Mago Island as "philanthropic" purchase or otherwise is indicated in the 1986 Annual Report.

It is evident from the history of Mago Island, presented by Colliers International, the agents for the sale of the island by Tokyu Corporation, that it was not an island "untouched by man and blessed with nature's virginal pureness" (ref. pp 51-54, Vol 3). According to the Colliers document the island was purchased by one Rupert Ryder "...from the Somosomo chiefs after they adopted Christianity and removed the local population mid 19th century". It was then used as a plantation for a "new unique cotton" which "gained international attention for Mago Island and Fiji, after

winning gold medals..." (p.52, Vol. 3). It was at one point, "the largest cane sugar plantation in the South Pacific". It was subsequently used as a copra plantation by the Borron family which sold the island to Tokyu Corporation.

It is not clear what was rare or special about its ecosystem given its history. It may be "one of the world's singularly most spectacular private islands" but one cannot see how the visitors by invitation (or otherwise), "be able to meet with the Fijian population in their natural environment (see letter from J.N. Falvey p.65 Vol. 1). The original indigenous Fijian inhabitants were removed and the island, since its plantation days, has a significant Fiji Indian population – not an indigenous population. It is also stated in the J.N. Falvey letter that the corporation's dominant philosophy in acquiring ownership of Mago Island was of "seeking to enrich mankind". Mr. Falvey further continued: "It thus proposes to match any profit-making enterprise on Mago with the philosophical enrichment of people who may stay there from time to time" (p.65, Vol.1). How all these will benefit the local Fijian population and protect Mago from "the evils of present day civilization" remains unclear.

The Colliers advertisement also stated: "Tokyu purchased this rare island ecosystem as a retreat, with the intention of creating an ecologically sensitive resort development and a goal of long term conservation and preservation" (p.52, Vol. 3). How this will be significantly different from other so called eco-friendly or sensitive resort development is never made clear. In Mr. Gotoh's original proposals to PBEC a reference is made to Club Med in the following terms: "Club Med is a typical enterprise involving the utilization of nature by humans. However, Club Med is intended to allow its members to enjoy the benefits of modern civilization accepting and expanding it unlimitedly without questioning or examining in depth the crisis brought by modern civilization" (p.10, Vol. 1). In contrast, Mr. Gotoh's International Shangrila (sic) is based on the idea that we should just follow the way of nature by resetting all traditional ethics, morals, socially accepted values etc" (p.10, Vol. 1). One is not clear what all this about. The witnesses also suggested that may be in 20 years or sometime in future the right technology will be available to implement Mr.

Gotoh's dreams. It was never made clear what was the right technology they were seeking nor what kinds of developments envisaged.

According to the List of Agreed Facts (para. 12) on becoming aware Mago Island "was available for purchase" Tokyu Corporation formed the view ...that (it) ... "would be suitable for its purposes and proceeded quickly to purchase the island without any specific prior due diligence or feasibility studies". This does not, on the evidence before the Court, concur with para. 14 of the List of Agreed Facts that: "Tokyu Corporation formed the view that it could not carryout any development on Mago Island without adversely affecting the existing environment". What "existing environment" is alluded to, given the history of developments on the island, was never articulated in evidence. What then was the purposes of the feasibility studies (as per para. 13) in relation to para. 14 is not clear to the Court.

In considering the totality of the evidence this Court is not satisfied that the dominant or sole purpose of the taxpayer Corporation in relation to Mago Island was that which they have contended. Mr. Gotoh said in 1974: "I have before me a sheet of paper which is completely blank except for the words Shangri-La written at the top. Would you please stand here with me and let us fill the page together". The evidence presented by the appellant has not satisfied the Court that the blank sheet of paper was filled subsequently or any extensive investigation and refinement or significant evolution occurred.

Was there acquisition for disposal?

It is quite clear from the evidence that the appellant ran its case on the basis that it had only one dominant, sole purpose. What then does the Court do if the appellant does not satisfy the onus required?

The Court does not need to repeat the ratio of the authorities cited and provided by the parties, in particular, the cases of (Pascoe v FCT (1956) 6 AITR 315) and

McCormack v FCT (1979) ATR 610). Further, the Court does not see it necessary to deal with submissions on other limbs of s.11(a) of the Income Tax Act e.g. "in the nature of trade" argument. This has been adequately addressed in the Respondent's further submissions and the case of Wisdom v Chamberlain (1969) 1 AER 332). In the present case evidence is not convincing that no business purposes were never contemplated. One wonders what the purpose of getting invited world and business leaders together, even in a Shangri-La, would be.

It is pertinent to consider two Canadian cases Bayridge Estates Ltd v Minister of National Revenue [1959] Canada Tax Cases 158 and Kourdi v R [1977] 3 CTC 2691). In Bayridge the case put forward by the appellant can be stated from p.160 of the Court's judgment: "...the land ... was not purchased in the course of any business of dealing in real estate but was acquired for the sole purpose of constructing and operating a motel and service station thereon, that it was only when such purpose failed because of the appellant's inability to borrow the money's required to carry out that purpose that the appellant accepted an offer for the property and realized the profit in question, and that, in these circumstances, the profit was a capital gain and not income". In this case a director of the company gave direct evidence, parts of which are recorded in the judgment, but need not be reproduced. The appellant's case was that they did not contemplate any other purpose since they were "so sure" that their only purpose would be "successful".

In Kourdi the appellants had purchased a vacant piece of land with the intention to build a shopping centre and earn rental income. No viability study was done before the undertaking of this adventure though the appellants were aware that they were buying in a good area. After construction the occupancy rate and rental income was unsatisfactory. The appellants then sold the property to an associated company. The profits realized on the sale was reported as a capital gain but was disputed by the Minister of National Revenue. The appellant's case was that at the time of purchase the possibility of selling was not a decisive factor, and, therefore, no secondary intention required to characterize the transaction as a business

transaction. In Kourdi the Court relied upon the case of Bayridge and quoted from it in the following terms:

> "In purchasing the property, the directors relied on their own knowledge of real estate and acted without any independent appraisal of the property...I am far from satisfied that men of their ability and experience would have done this for the purpose of building a motel and service station without having arranged for the funds to finance this construction and without, at the same time, having in mind the most obvious alternative course open to them for turning the property to account for profit. Despite their optimism the possibility, if not the probability, of their not being able to obtain the necessary loan must, in my opinion, have been present in their minds...To my mind, it is not without significance that that course was the only alternative course considered and that it was decided upon as *the only thing left to do*. In my opinion, the sale of the property for profit was one of the several alternative purposes for which the property was acquired, and it was in the carrying out of that alternative purpose, when it became clear that the preferred purpose was unattainable, that the profit in question was made. It was, accordingly, a profit made in an operation of business in carrying out a scheme for profit-making and was properly assessed." (at p 2696)

In this case it is quite evident that the dream of Shangri-La was neither here nor there. It was put forward that technology to realize the Shangri-La was not available, may be it would be available in 20 years. What types of technology to do what was not made clear. It was a personal dream of the then President and Chairman of Tokyu Corporation. The purchase was seem "as fairly strange and controversial among Tokyu staff". In such circumstances why wouldn't the corporation, as a corporate entity listed on the Tokyu Stock Exchange, not consider selling it off as a means of profit making since Tokyu is a profit making corporation. Instead of the very tenuous and mostly hearsay evidence presented, better documentary evidence could have been tendered. The 1986 Annual Report, as noted, did not shed much light. If it was a "strange and controversial" purchase how was it recorded in the company accounts? The Court found no assistance from the "Ledger account print outs recording acquisition of Mago Island" (Vol. 1 pp. 101 – 127). This was mostly in Japanese.

The cases of Craddock v FCT [1969] 1 ATR 339 and Piper v FCT [1974] 4 ATR 359 are also relevant. The facts may be distinguishable but the principles are relevant. In Craddock the stated purpose of acquisition was to carry on farming as a hobby. No consideration of its farming potential was undertaken. As the Court noted: "no substantial consideration whatever to the economies of a farming enterprise on the land" was undertaken (at p. 341). The Court further noted that "two sensible businessmen were behaving quixotically" (at p. 342). As one of the businessmen stated, "we just wanted a farm. A bit of fun" was his→
description of the undertaking" (at p. 341). In this case Shangri-La was a "dream", a "hobby" of the boss who was, perhaps, quixoticall and undertook no due diligence.

In Piper the Supreme Court of NSW emphasized the correct approach to be taken in considering the evidence of a taxpayer: "evidence given by the taxpayer is ... to be scrutinized with care and to be weighed against the objective facts and the inferences to be drawn from his activities generally. Such evidence must "be considered most closely and received with greatest caution" (Pascoe v FCT (1956) 6 ATTR 315 at 316). The facts of the case in Piper are familiar to the parties and need not be repeated here. However, the decision of the Court is relevant and was stated in the following terms:

> "Having regard to the evidence as a whole, I am not satisfied that the dominant purpose of the taxpayers in relation to the premises was that which they have contended for. In so far as it is necessary to make a further finding upon the matter, the probabilities are, in my opinion, that when the premises were acquired by them, it was their dominant purpose to turn them to account so as to make a profit from them in whatever might in due course appear to be the best manner of so doing" (at p. 368).

Profit or Gain

The Court needs to deal briefly with a final matter raised in submissions by the appellant. The Court fails to understand the crux of appellant's submissions in this

regard but the gist can be gleaned from the following. In para. 29 of the appellant's submission in reply it is stated in the following terms:

> "In no part of the Income Tax Act is it specified what is meant in section 11(a) by the words "profit or gain accrued from the sale or other disposition". What those words mean, as the respondent correctly points out, is a matter of law. Hence there is no need for expert evidence."

In para. 81 of its initial submissions the appellant had put this in the following terms: "Section 11(a) in fact says nothing about accounting methodology. Absent some specific provision in taxation legislation it is a question of law what is the appropriate accounting methodology to give effect to that legislation". It becomes more confusing when the appellant states in para. 80: "Whilst section 11(a) allows certain gains to be treated as income, it does not allow the respondent to construct and deconstruct accounts to produce a more favourable result". (emphasis added)

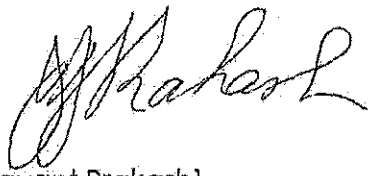
The Court is not provided the calculation of how the respondent "constructed" or "deconstructed" the accounts. A reference in footnote 91 is made to Exhibit 4. This is apparently "prepared for Robert Newton and Peter Knight – for discussion only". One assumes it was prepared by KPMG. All the Court can say is that the document makes no sense to it. The person(s) preparing the document were not called to explain what was it all about. In my view such a document with its attendant calculations did call for expert accounting evidence.

At the commencement of the case, appellant counsel stated that it was not calling any expert evidence. On this basis the respondent did not call its own accounting experts. The Court can only surmise that the appellant had no basis to argue this matter. The Court was not privy to the basis of calculations that the CIR relied upon, and which apparently generated much correspondence between the CIR and the local accountants for Tokyu Corporation – KPMG (see Vol. 3). This Court cannot second guess the CIR's calculations of tax without any expert accounting evidence nor presentation of actual figures used. The FAS 21 (Vol. 1 pp.174 – 190) without any

expert presentation is also of no assistance. All it states is that it is "Fiji Accounting Standard – the effects of changes in Foreign Exchange Rates". Para. 41 of the document notes: "Gains and losses on foreign currency transactions and exchange differences arising on the translation of the financial statements of foreign operations may have associated tax effects which are accounted for in accordance with FAS 12, Accounting for Income Tax". How this Court is to make sense of all this without proper submissions and perhaps an accountant's evidence is beyond me. The cases cited by the parties do not assist in the absence of any relation to real figures used in arriving at the income as per section 11 (a). The Court notes that section 11 of the Income Tax Act does define "total income" and the concept of profit or gain is used throughout this section. It is, therefore, not clear what the appellant contends is "a matter of law".

Orders

The appeal is dismissed. Each party is to bear its own costs.



[Jayant Prakash]

Court of Review

1 December 2008