

HCIA 2/2009

**IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
COURT OF FIRST INSTANCE**

INLAND REVENUE APPEAL NO. 2 OF 2009

Between

CHURCH BODY OF THE HONG KONG
SHENG KUNG HUI

Appellant

and

COMMISSIONER OF INLAND REVENUE

Respondent

AND

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**IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
COURT OF FIRST INSTANCE**

INLAND REVENUE APPEAL NO. 3 OF 2009

Between

HONG KONG SHENG KUNG HUI
FOUNDATION

Appellant

and

COMMISSIONER OF INLAND REVENUE

Respondent

(Heard together)

Before: Hon Reyes J in Court
Date of Hearing: 20 January 2010
Date of Judgment: 27 January 2010

J U D G M E N T

I. INTRODUCTION

1. The Church Body is the incorporation of the Anglican Church in Hong Kong. I shall refer here to the Church Body as the Church. The Foundation is the incorporation of the Anglican Bishop of Hong Kong. Both the Church and the Foundation are charitable bodies.

2. The Church and the Foundation appeal by way of Case Stated against 2 Decisions of the Board of Review dated 17 June 2008. By the Decisions, the Board upheld 2 Determinations by the Commissioner dated 6 November 2006 assessing the Church and Foundation to profits tax for the years 1998/99 to 2004/05. The Decision in relation to the Foundation simply incorporates that in relation to the Church, the relevant facts being the same in both cases. In this Judgment, therefore, references to the Board's Decision should be taken as references to the Decision in relation to the Church.

3. The Board certified 2 questions for this Court to answer:-

- (1) Whether, on the facts found by the Board, and on the true construction of the Inland Revenue Ordinance (Cap.112) (IRO), the true and only reasonable conclusion is that there was no change of intention from capital holding to trading/business, whether by September 1989 or December 1990 or at all.

- (2) If the Answer to Question (1) is in the negative, whether, on the facts found by the Board, and on the true construction of the IRO, it was open to the Board to conclude that the proviso to IRO s.88 does not apply.

II. BACKGROUND

4. The Church and the Foundation owned certain land (the Old Lots) in Tai Po. Part of the Old Lots was occupied by an orphanage (the Home). The Old Lots had belonged to the Church and the Foundation since the 1930s. The Church and the Foundation had planned since the 1970s to develop the Old Lots.

5. Although there had been discussions in the 1970s to use the land adjacent to the Home as a retirement village for the clergy, that plan was put on hold in the 1980s and never revived.

6. In the 1980s there had also been talk about refurbishing the Home. But the Home was so old that renovation was unlikely to prolong its life for more than 5 years. Eventually, from September 1989 at the latest, the re-provisioning the Home was treated as a separate project from the development of the Old Lots. In September 1989, the proposal being seriously considered in relation to the Home was to re-locate the children's section of the Home to an adjacent site, the babies' section to Yuen Long, and the rest of the Home to another Tai Po lot owned by the Foundation.

7. In the early 1990s, architects commissioned by the Church and the Foundation submitted various plans to the Government for the purpose of obtaining town planning permission for a substantial residential development in the Old Lots. A set of plans were approved by the Town Planning Board in July 1990.

8. In December 1990 architects applied on behalf of the Church and the Foundation to the Districts Land Office Tai Po for a land exchange of the Old Lots to permit the building of the residential development as approved.

9. In May 1993 a premium of some \$704 million was agreed between Government on the one hand and the Church and the Foundation on the other.

10. In July 1993 the Church and the Foundation invited various developers to submit tender offers for 2 Options. Option A was for the outright purchase of the Old Lots at a consideration inclusive of the \$704 million premium. Option B entailed the establishment of a joint venture with the Church and Foundation for the redevelopment of the Old Lots.

11. In August 1993 the Church and the Foundation accepted Cheung Kong's tender for Option B.

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12. In November 1993 the Church and the Foundation surrendered the Old Lots to the Government in exchange for the grant of a New Lot in Tai Po. The Church and the Foundation owned the New Lot as tenants-in-common in the ratio of 44:56.

13. In December 1993 the Church and the Foundation entered into a Joint Venture Agreement with Cheung Kong and Montaco (collectively, the Developers) for the development of the New Lot as a private residential area. Montaco is a Cheung Kong subsidiary.

14. In March 1998 the Church, the Foundation and the Developers agreed that 129 residential units and 94 car parking spaces in the development would be allocated to the Church and the Foundation.

15. In August 1998 Government issued an occupation permit for the development (which had been named “Deerhill Bay”). Deerhill Bay comprised 22 houses, 5 blocks of low-rise buildings and 5 blocks of high-rise buildings. It had 381 residential units in all.

16. Between 1998 and 2006, the Church and the Foundation sold their residential units and car-parking spaces at Deerhill Bay. From the sales, the Church derived a profit of some \$452 million, while the Foundation made a profit of some \$667 million.

17. In its Decision, the Board summarised the actions of the Church and the Foundation thus:-

“70. It is clear from the evidence of Mr Li [Fook Hing] that he approached the matter on commercial principles, with the laudable object of raising as much income as possible for [the Church] and its charitable activities. [The Church and the Foundation] actively marketed the disposal of the Old Lots by approaching leading developers in Hong Kong for offers and tenders. They sought and subsequently obtained town planning permission. [They] have performed activities in relation to the Old Lots in an organised and coherent way with a view to maximising the income from their development. They sought and subsequently obtained a new grant by surrendering the Old Lots, thereby substituting the Olds Lots by the new Lot. They have chosen to carry on a separate adventure or enterprise of a lucrative commercial and trade character, different and distinct from their charitable work.”

18. The Board held that, although the Church and Foundation had initially acquired the Old Lots as a capital asset, their initial intention changed to one of using the Old Lots (or parts thereof) for the purpose of trading or business. According to the Board, that change of intention had occurred by September 1989 or, alternatively, December 1990 at the latest.

III. DISCUSSION

A. Question (1): Change of intention

19. Mr Anthony Neoh SC (appearing for the Church and the Foundation) submits that the Board's approach was too narrow. The Board (Mr. Neoh says) failed to have regard to the charitable status of the Church and the Foundation. As charities, neither entity (Mr Neoh says) was empowered to venture its trust property (including the Old Lots) in any sort of trade or business. On the contrary, the trustees of the Church and the Foundation are under a fiduciary duty to preserve the assets of the 2 entities and not to expose the same to the risk of loss in a trade or business.

20. Mr Neoh suggests that the redevelopment of the Old Lots by way of a substitution for the New Lot and the building of Deerhill Bay was no more than a means of preserving the value of the Old Lots. The redevelopment was merely a means of enabling the Old Lots to be sold at the best possible price in accordance with the duties of the trustees and the objects of the Church and the Foundation. The whole undertaking was a "one-time event, with no more objective than the derivation of the best capital sum".

21. In support of his contentions, Mr Neoh refers me to the *Constitutions and Canons of the Chung Hua Sheng Kung Hui* (made pursuant to s.5 of the Hong Kong Sheng Kung Hui Ordinance (Cap.1157) (HKSKHO)). The *Constitutions* regulate the organisation of the Anglican Church in Hong Kong and Macau. In its Preamble, Mr Neoh points out that the *Constitutions* (at least in the version promulgated in 2000) speak of a "desire" by the Anglican Church "to be a community to exemplify in the world the good news of Jesus Christ, born out of God's love, and heralded in the power of the Holy Spirit".

22. Mr Neoh also draws my attention to the Regulations of the Foundation (made pursuant to s.13 of the Hong Kong Sheng Kung Hui Foundation Ordinance (Cap.1159) (HKSKHFO)). Those provide in Reg. 3.1 that "the Foundation shall provide financial support to the Church" and Reg. 3.2 that "assets of the Foundation shall only be applied or used as grants solely for the Church by the instruction of the House of Bishops".

23. Mr Neoh invites me to infer from the foregoing documents that (as charities promoting the Christian ethic) the Church and the Foundation have objects which prevent them from entering into trade or business, in contrast to limited companies which are primarily formed to enter into business for the profit of shareholders.

24. I am not persuaded by Mr Neoh's submissions on Question (1).

25. First, Mr Neoh's contention that the Old Lots were trust property was not ventilated before the Board by counsel then representing the Church and the Foundation. This Court must consequently be wary of entertaining the argument on an appeal by way of case stated since the argument is fact-sensitive.

26. Mr Neoh asserts that the Old Lots constituted property held by the Church and the Foundation under a charitable trust. No evidence was adduced in support of that assertion before the Board as the point was not taken before the Board.

27. The Commissioner does not accept that, merely because property is owned by a charity, that property is without more subject to a charitable trust. Evidence needs to be adduced to explain why it is said that the property is subject to a trust, let alone a charitable one. Mr Peter Ng SC (appearing for the Commissioner) rightly complains that, if Mr Neoh's argument were now permitted, the Commissioner would be deprived of the opportunity to adduce evidence rebutting the assertion that the Old Lots were subject to a charitable trust.

28. Second, in any event, purely as a matter of logic, from the documents cited by Mr Neoh, I cannot deduce much (if anything) as to what may or may not have been the intention of the Church and the Foundation relative to the Old Lots in September 1989 or December 1990.

29. This is because the HKSKHO and HKSKHFO on which Mr Neoh specifically predicates his argument were both enacted in February 1999. Accordingly, the *Constitutions* and the Regulations promulgated thereunder, all post-date the critical times determined by the Board. One cannot safely infer the existence of a past intention from the subsequent enactment of a limitation.

30. It is possible that ordinances analogous to the HKSKHO and the HKSKHFO governed the situation before February 1999. For instance, there were the Chinese Anglican Church Body Incorporation Ordinance (No.18 of 1902) and the Bishop of Victoria Incorporation Ordinance (originally enacted as No.4 of 1925). But these appear to have imbued the Church and the Bishop with powers. Nothing is said about the purposes (charitable or otherwise) for which such powers may be legitimately used. I have not been referred to subsidiary legislation promulgated under the latter 2 statutes expressly stating that the powers of the Church or the Foundation can only be used for specific charitable purposes.

31. I note that pre-2000 versions of the *Constitutions* do not appear to contain the wording which Mr Neoh stresses. Even if they did, I do not see how the expression of a "desire" to exemplify the teachings of Christ necessarily means that the Church is curtailed from engaging in a trade or business. There is no self-evident contradiction between a Christian life and engagement in a trade.

32. At best, the pre-2000 *Constitutions* declare that the Church "accept[s] the Scriptures of the Old and New Testament and believe[s] them to contain all things necessary to salvation, and to be the ultimate standard of faith". This is far too vague. Different people understand different things from the Old and New Testament. I am unable to construe the Preamble of the *Constitutions* (whether in their pre- or post-2000 version) as a statement that the exercise of the Church's powers are limited to the narrow purposes which the law regards as charitable.

33. The reality (I think) is that, if one wishes to work out the precise limitations on the powers the Church and the Foundation to deal with the Old Lots in the period up to

September 1989 or December 1990, one has to conduct an investigation into fact. The appropriate time for doing that was the hearing before the Board. Before this Court, appeals can only proceed by way of case stated on questions of law.

34. Third, in any event, assume that it can be established that the Church and Foundation have relevant limitations in their constitutions relating to the disposition of property. Assume further that such limitations forbid both entities from using assets for non-charitable purposes. Even then, I do not think that it follows from the existence of a prohibition in an entity's constitution that, as a matter of fact, the entity did not engage in a trade or business or did not have an intention of so doing.

35. The fact that A is prohibited from doing X by a regulation does not logically imply that A has not in fact done X. One cannot infer what is or is not, from a prescriptive statement about what one should or should not do. The existence of a prohibition in regulations governing the Church and the Foundation could not by itself preclude an investigation into fact or falsify the Board's conclusion. As Mr Ng points out, the law reports are replete with instances of charities (with acknowledged charitable objects) found by the Courts to have engaged in trades or businesses chargeable to tax. See, for example, *Coman v. Governors of the Rotunda Hospital, Dublin* [1921] AC 1; *Royal Agricultural Society of England v. Wilson* (1924) 9 TC 62; *Brighton College v. Marriott* (1925) 10 TC 213; *British Legion, Peterhead Branch, Remembrance and Welcome Home Fund v. CIR* (1953) 35 TC 509. Note also paragraph 64 of the Board's Decision citing the latter cases.

36. Fourth, in my view, it was open to the Board to decide as it did. It was a reasonable conclusion on the facts that the Church and the Foundation experienced a change of intention.

37. At the end of the day, Mr Neoh was constrained to arguing essentially that September 1989 or December 1990 were the wrong dates for a change of intention, simply because the Church and the Foundation were not irrevocably bound to develop the Old Lots at that point in time. It was not (Mr Neoh suggested) until 1993 when the 2 bodies entered into a Joint Venture with Cheung Kong that the die was irrevocably cast and the Rubicon crossed. After the deal with Cheung Kong was struck, the Church and the Foundation were contractually bound to go through with the development of the Old Lots. But before then, the Church and the Foundation could have put a stop to any development plans. Everything before 1993 was thus (Mr Neoh stressed) merely exploratory and tentative. Nothing became fixed as a matter of intention until 1993.

38. Mr Neoh's suggestion may be one way to read the facts. But it is by no means the only reasonable reading. The Board's interpretation of the facts in relation to the intentions of the Church and the Foundation is equally plausible. One does not necessarily change one's intention only when one is irrevocably bound. One can change one's intention long before that point in time. The Board so found on the facts. I cannot say on the material before me that there was anything perverse or unreasonable in that conclusion.

39. I would answer "No" to Question (1).

B. Question (2): Application of IRO s.88

40. Section 88 provides:-

“Notwithstanding anything to the contrary in this Ordinance contained there shall be exempt and there shall be deemed always to have been exempt from tax any charitable institution or trust of a public character;

Provided that where a trade or business is carried on by any such institution or trust the profits derived from such trade or business shall be exempt and shall be deemed to have been exempt from tax only if such profits are applied solely for charitable purposes and are not expended substantially outside Hong Kong and either:-

- (a) the trade or business is exercised in the course of the actual carrying out of the expressed objects of such institution or trust; or
- (b) the work in connection with the trade or business is mainly carried on by persons for whose benefit such institution or trust is established.”

41. On s.88, the Board noted that the Church and the Foundation essentially adduced no evidence on how their share of the proceeds from the Deerhill Bay development were actually applied. The Board stated in its Decision:-

“81. The appellants [the Church and the Foundation] have adduced no evidence on the application of the profits. The onus of proof under section 68(4) is on the appellants and they fail to prove that the proviso to section 88 applies. We decline to draw any inference in favour of the appellants. If the profits have in fact been applied solely for charitable purposes, the appellants may reasonably be expected to have material evidence on it. If any inference is to be drawn, it is one adverse to the appellants.

82. The appellants have adduced no evidence on the profits not being expended substantially outside Hong Kong. The onus of proof under section 68(4) is on the appellants and they fail to prove that the proviso to section 88 applies. We decline to draw any inference in favour of the appellants. If the profits have in fact not been expended substantially outside Hong Kong, the appellants may reasonably be expected to have material evidence on it. If any inference is to be drawn, it is one adverse to the appellants.

83. The appellants have not been able to identify any expressed object of the Foundation or the Church Body. We reject the appellants’ contention that the proviso is also applicable to implied objects. The

statutory requirement is ‘expressed’ objects or ‘明文規定’ in Chinese. The onus of proof under section 68(4) is on the appellants and they fail to prove that the proviso to section 88 applies. We decline to draw any inference in favour of the appellants. Indeed, if any inference is to be drawn, it is one adverse to the appellants.

Further and in any event, property development is not alleged to be an object of the Foundation or the Church Body. Thus, the trade or business in this case could not be said to be, and was not, exercised in the course of the actual carrying out of the objects or alleged objects of the Foundation or the Church Body.

84. The work in connection with the trade or business was not carried on by persons for whose benefit the appellants were established. Requirement [(b)] in [IRO s.88] is not satisfied and the proviso to section 88 does not apply.
85. The appellants fail on each and every one of the requirements and the proviso to section 88 does not apply.”

42. Mr Neoh has attempted to fit the present circumstances into the wording of the proviso in a variety of ways.

43. Mr Neoh first argues that the Board found in paragraph 70 of its Decision (quoted above) that the Church and the Foundation used the entire of the profits from the Deerhill Bay development in charitable activities.

44. But, in light of paragraphs 81 to 85 of the Decision quoted above, Mr Neoh’s submission is surprising. I do not think that it can be right. Read in context, all that the Board was saying in paragraph 70 is that the Church and the Foundation had the laudable motive of using as much of the income generated from the Old Lots as possible in their charitable activities. That does not mean that, at the end of the day, all of the income generated was expended on charitable activities. Nor does paragraph 70 say anything about how much of the income generated was actually used in charitable activities.

45. Second, Mr Neoh suggests that there was “unchallenged evidence” before the Board to the following effect: “Funds received by the Church Body and Foundation is expended in furtherance of spreading the Gospel and for charitable purposes in Hong Kong.” The latter quotation comes from the Witness Statement of Bishop Louis Tsui which was adduced before the Board. Bishop Tsui also gave oral evidence at the hearing before the Board.

46. My difficulty is that the Board were plainly unimpressed by Bishop Tong’s Statement as a whole. At paragraph 42 of its Decision, the Board observed, for instance, that Bishop Tong had failed in his evidence to define what he meant by “the charitable activities of the Church”. It is far from clear that when referring to “charitable purposes” or

“charitable activities” generally, Bishop Tong had in mind what the law regards as “charitable”. The quoted sentence was challenged by the Commissioner’s lawyers in submissions before the Board. The Commissioner through counsel asked to see relevant accounts showing just how and where (in Hong Kong or elsewhere) profit monies were expended. No such accounts were provided. Thus, Bishop Tong having unfortunately given no further written or oral particulars, the Board plainly could not and did not attach much (if any) weight to his evidence.

47. Third, Mr Neoh refers to the Foundation’s Regulations 3.1 and 3.2 as evidence that the Foundation could not use its monies otherwise than for charitable purposes. But, as already discussed, this argument conflates a statement of principle with a statement of fact. The latter cannot be inferred from the former.

48. Further, the Regulations do not establish that the relevant monies were substantially expended for charitable activities in Hong Kong (as opposed to elsewhere). To fall within the proviso to s.88, it is necessary to show that monies have not been substantially expended outside of Hong Kong.

49. Fourth, Mr Neoh refers to the *Constitutions* as evidence that the Church must have used its monies solely for charitable purposes. This argument is problematic for the reasons already identified.

50. Further, I do not think that the Preamble to the *Constitutions* (whether pre- or post-2000) can constitute “expressed objects” of the Church and the Foundation within the terms of s.88. The Preamble is too vague to serve such purpose.

51. Fifth, Mr Neoh asserts that the development of the Old Lots was “undertaken by committees of the Church ... who are therefore persons for whose benefit the Church was established”. But there is simply no evidence of this and the Board made no such finding of fact as Mr Neoh asserts.

52. Mr Neoh submitted that, as the committee members are part of mankind (or the Anglican communion) and the Anglican Church was started centuries ago to benefit mankind (or the Anglican communion), the requirements of sub-paragraph (b) of the proviso to s.88 are met.

53. But I doubt that it can be said in any meaningful sense that the Church and the Foundation were established for the benefit (among others) of the committee members which undertook the development of Deerhill Bay. Committee members may have been Anglicans (although it is unclear to me from the Decision and the Agreed Facts whether this was actually the case). But it would be an odd usage of English to say that the Anglican Church was established “for their benefit” as members of mankind (or of the Anglican communion). It seems to me that s.88 envisages something much narrower, namely, that the particular persons who carried out a business or trade are the specific persons for whose benefit a charity was formed or, at least, are persons belonging to a specific class (as distinct

from mankind or the Anglican communion in general) for whose benefit a charity was established.

54. In light of the foregoing, I would answer “Yes” to Question (2).

IV. CONCLUSION

55. The Board’s Decisions are upheld. The Church and the Foundation fail in their appeals. The appeals are dismissed. There will be an Order *Nisi* that the Church and the Foundation pay the Commissioner’s costs, such costs to be taxed if not agreed. There will be certificate for two counsel.

(A. T. Reyes)
Judge of the Court of First Instance
High Court

Mr Anthony Neoh, SC and Mr Denis Yu, instructed by Messrs P C Woo & Co, for the Appellants in both actions

Mr Peter Ng, SC and Mr Eugene Fung, instructed by the Department of Justice, for the Respondent in both actions