FACV No. 11 of 2018
[2019] HKCFA 25

IN THE COURT OF FINAL APPEAL OF THE HONG KONG SPECIAL ADMINISTRATIVE REGION

FINAL APPEAL NO. 11 OF 2018 (CIVIL)
(ON APPEAL FROM CACV NO. 115 OF 2017)

BETWEEN

PERFEKTA ENTERPRISES LIMITED **Appellant**

and

COMMISSIONER OF INLAND REVENUE **Respondent**

Before:	Chief Justice Ma, Mr Justice Ribeiro PJ, Mr Justice Fok PJ, Mr Justice Cheung PJ and Mr Justice Gummow NPJ
Date of Hearing:	18 June 2019
Date of Judgment:	12 July 2019

J U D G M E N T

Chief Justice Ma:

1. I agree with the judgment of Mr Justice Fok PJ.

Mr Justice Ribeiro PJ:

2. I agree with the judgment of Mr Justice Fok PJ.

Mr Justice Fok PJ:

3. This appeal concerns a charge to profits tax in relation to a payment received by the appellant upon the disposal of a property that had been owned by it as a long-term capital asset. The correctness of that charge depended on the question of whether the appellant changed its intention concerning its ownership of the property so that, when disposing of it, it was carrying on a trade or business.

A. Introduction

A.1 Background facts

4. The background facts were substantially agreed between the parties and the following summary, taken from the recitation of those agreed facts in the judgment of the Court of Appeal,[1] will suffice for present purposes.

5. The appellant, Perfekta Enterprises Limited, was incorporated in Hong Kong in 1965 and carried on the business of toy manufacturing. In 1969, it acquired most of a building in Kwun Tong, called Vanda Industrial Building, which it used as its manufacturing base in Hong Kong. In 1977, it acquired the remainder of the building and continued to manufacture toys there. This building will be referred to in this judgment as "the Property" and the site on which it was situated as "the Lot".

6. The appellant's manufacturing base shifted from Hong Kong to the Mainland from the late 1970s. In 1978, the appellant established a toy factory in Guangzhou, which relocated to Shenzhen in 1985. In 1987, the appellant ceased its manufacturing operations at a factory it owned in Tsuen Wan in Hong Kong and disposed of that factory.

7. From 1991, a series of applications was made in relation to the Lot to enhance its value. In 1991, an application was made to the Town Planning Board for permission to develop a composite industrial and office building on the Lot. This was rejected. A second application to the Town Planning Board, in June 1992, of the same nature was approved. In October 1992, an application was made to the District Lands Office, Kowloon East, for modification of the lease conditions for the redevelopment of the Lot by the construction of a composite industrial and office building. In 1993, a third application to the Town Planning Board in respect of a revised design of the proposed composite building was approved. General building plans for such a building submitted to the Buildings Department in 1993 were initially disapproved but, on re-submission, were approved. In 1994, the District Lands Office indicated a preparedness to recommend a modification of the lease to allow the development of the Lot by way of surrender and re-grant, subject to the payment of a premium of HK$61,420,000.

8. On 21 April 1994, at a meeting of the board of directors of the appellant, a proposal from Cheung Kong (Holdings) Limited ("Cheung Kong") for the redevelopment

[1] CACV 115/2017, [2018] HKCA 301, Judgment dated 1 June 2018 ("CA Judgment"), at [2].

of the Property was discussed. The material paragraph of the minutes ("the Minutes") recorded as follows:

> "Re: 25 Chong Yip Street, Kwun Tong, Redevelopment plan
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> The Chairman reported that discussions had taken place with representatives of Cheung Kong (Holdings) Limited who had approached [the appellant] with a suggestion of a joint development of the Company's industrial premises at 25 Chong Yip Street, Kwun Tong. As the premises were acquired 24 years ago (since May 1969) and were in need of upgrading it was recommended that the duscussions [sic] with Cheung Kong proceed. Consideration would have to be given to the leasing of alternative premises for the Company's manufacturing operation during the period of development if such were to proceed. The proposal from Cheung Kong (Holdings) Limited envisaged the sale to third parties of the newly developed industrial & office building as the manufacturing business of [the appellant] was seen to be a 'sunset industry' in Hong Kong and with more production being carried out in PRC, the redevelopment of the site and subsequent sale would be an appropriate method for [the appellant] to realise its long term asset. It was agreed that any joint development program would have to provide for [the appellant] to have an entitlement to take up sufficient space for its own manufacturing requirements in the future. It was decided that for internal purposes any such joint development should be carried out in an entity separate from [the appellant] and that consideration be given to a sale of the property to a wholly owned subsidiary which would subsequently enter into a development venture with Cheung Kong."

9. On 23 April 1994, the Lot was valued at HK$418,000,000, reflecting its development potential, but without taking into account any premium payable.

10. In May 1994, Cheung Kong proposed to the appellant a joint venture arrangement for the redevelopment of the Property. This led to the execution, by the appellant, Cheung Kong and Great Poka Limited (a subsidiary of Cheung Kong) ("Great Poka") of a Redevelopment Agreement relating to the Property dated 30 July 1994 ("the Redevelopment Agreement"). The material terms of that Redevelopment Agreement are set out below in Section A.2. Pursuant to clause 3.02 of the Redevelopment Agreement (see below), Great Poka paid a sum of HK$165,104,100, described as an "Initial Payment", to the appellant as consideration for the right to redevelop the Lot in accordance with its terms. As will presently be seen, under this agreement, the actual joint venture parties were to be Cheung Kong, Great Poka and the appellant's wholly-owned subsidiary company (then as yet not formed, so it was known simply as "Newco").

11. In August 1994, the appellant and the Government entered into an Agreement and Conditions of Exchange in respect of the Lot.

12. By an Assignment dated 14 November 1994, the appellant assigned the Lot to its wholly owned subsidiary, Prodes Company Limited ("Prodes") for a consideration of HK$314,315,900. On 24 November 1994, Prodes, Great Poka and Cheung Kong entered into the New Agreement ("the New Agreement") (a draft of which had been annexed to the Redevelopment Agreement) for the carrying out of the redevelopment joint venture. The profits of the joint venture, after deduction of expenses, were to be shared equally between Prodes, on the one hand, and Great Poka, on the other. In December 1994, vacant possession of the Lot was given to Great Poka and, in the same month, the appellant's manufacturing operations at the Property ceased.

13. On 10 February 1999, Prodes, Great Poka and Winrise Limited ("Winrise") (another subsidiary of Cheung Kong) entered into an Agreement for Sale and Purchase of the Lot, whereby Prodes sold the Lot to Winrise for a consideration of HK$332,661,000. On the same date, those parties also entered into an Agreement relating to the Manner of Payment of the Purchase Price whereby it was agreed that, of the purchase consideration, HK$315,210,899.27 would be paid to Great Poka by way of reimbursement to it of the land premium paid and construction costs incurred in the redevelopment of the Lot.

14. On 11 February 1999, the board of directors of the appellant ratified and approved an Assignment between the appellant and Prodes whereby Prodes assigned its rights under the New Agreement to the appellant and the appellant released and discharged Prodes from its liabilities owing to the appellant.

15. In August 2007, following the redevelopment of the Lot and the sale of the units in the redeveloped building, the appellant received 50% of the balance of the net proceeds in the sum of HK$386,223.21.

A.2 The Redevelopment Agreement

16. Material terms of the Redevelopment Agreement included the following:

(1) Recital (6):

> "Subsequent to surrender and regrant of the Lot but prior to redevelopment, [the appellant] intends to transfer the registered and beneficial ownership of the Lot to its wholly owned subsidiary ('Newco')."
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> Prodes became the subsidiary known as Newco.

(2) Clause 3.02:

> "[Great Poka] shall pay to [the appellant] as consideration for [the appellant] granting to [Great Poka] the right to redevelop the Lot in accordance with the terms of this Agreement an Initial Payment totalling HK$165,104,100 …".

(3) Clause 5.01:

> "Within four (4) months after the date of issue of the Conditions [the appellant] shall at its sole cost and expense transfer the registered and beneficial ownership of the Lot to Newco subject to Newco executing the New Agreement referred to in Clause 5.02 below."

(4) Clause 5.02:

> "[The appellant] hereby agrees and undertakes with [Great Poka] to procure that Newco shall simultaneous [sic] with but immediately after the execution of an assignment of the Lot in its favour enter into a new agreement ('the New Agreement') with [Great Poka] and [Cheung Kong] in the form as set out in Appendix II. [Great Poka] and [Cheung Kong] agree and undertake with [the appellant] that they shall enter into the New Agreement with Newco. Should Newco fail to execute the New Agreement as contemplated in this Clause, the assignment of the Lot to it shall not take effect and shall become null and void and [the appellant] shall be deemed to have replaced Newco in its position and continue as the registered and beneficial owner of the Lot under the New Agreement which shall be deemed to have been executed and shall come into operation immediately upon Newco's failure to execute the New Agreement. …".
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> The New Agreement referred to in this clause was the agreement that was eventually executed by Prodes, Great Poka and Cheung Kong on 24 November 1994 (referred to earlier at [12] above).

(5) Clause 6.01:

> "This Agreement shall be terminated in the event that:-
>
> (i) Newco refuses or fails for whatever reason to execute the New Agreement; …"

(6) Clause 6.02:

> "Where this Agreement is terminated by reason of sub-clause (i) above [the appellant] shall forthwith refund to [Great Poka] (a) all moneys paid to [the appellant] by [Great Poka] as Initial Payment, …".

(7) Clause 8.01:

> "This Agreement is in the nature of a joint venture and sale and purchase of interest in property. Nothing herein contained shall be deemed to constitute a partnership between [the appellant] on the one part and [Great Poka] and [Cheung Kong] on the other part. …".

B. Procedural history

B.1 Determination

17. By a Determination dated 19 May 2011, the Deputy Commissioner of Inland Revenue agreed with the assessor's view that the Initial Payment to the appellant of HK$165,104,100 should be assessable to profits tax and accordingly increased the appellant's Additional Profits Tax Assessment for the year of assessment 1994/95 by the net sum of HK$162,624,798 (being the amount of the Initial Payment less professional and legal fees and agreed adjustments), on which the additional tax payable was assessed at HK$26,833,092.

B.2 Board of Review

18. The appellant appealed to the Board of Review[2] contending that the Initial Payment was a capital receipt on which profits tax was not chargeable. By a majority, the Board of Review allowed the appellant's appeal, but on an unusual basis not contended for by either party before it. The Board majority[3] found that, although there was a change of intention on the part of the appellant, there was no relevant change of intention to one of trading and remitted the assessment to the respondent for revision or annulment. The basis of this decision, however, was based on a "reinvestment theory" that posited that the appellant sold the Property and used part of the proceeds to invest in a joint venture to be carried out by Prodes. The Board minority[4] found that there was a change of intention on the part of the appellant to trade as at the date of the Redevelopment Agreement.[5]

B.3 Case Stated Appeal to Court of First Instance

19. The respondent appealed by way of Case Stated and questions arising from the decision of the Board of Review submitted by it and also by the appellant were put to the Court of First Instance for determination.[6] By his judgment dated 27 April 2017 ("the CFI Judgment"), Chung J held that the Board majority decision to remit the assessment to the respondent should be set aside, as there was no evidential basis for the "reinvestment

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2 In Board of Review Case No. D18/15, under reference B/R 18/11, Decision dated 20 October 2015 ("BOR Decision")

3 Mr Miu Liong, Nelson, Barrister-at-Law, and Mr Mark Richard Charlton Sutherland, Barrister-at-Law, FCIArb.

4 The Chairman, Mr Kenneth Kwok Hing Wai, SBS, BBS, SC, JP.

5 BOR Decision at [123].

6 HCIA 1/2016, before Chung J.

theory".[7] He rejected the appellant's argument that the appellant did not change its intention to trade since it was Prodes, its subsidiary, that participated in the joint venture and therefore carried out the redevelopment project.

B.4 Court of Appeal

20. The appellant appealed to the Court of Appeal,[8] materially contending that Chung J was wrong in holding that the Board minority did not err in finding that it had changed its intention to trade in respect of the Lot. By a majority,[9] the Court of Appeal rejected the appellant's ground of appeal in relation to there being no change of intention on its part to trade in relation to the Lot. Godfrey Lam J, dissenting in relation to this ground of appeal, held that there was no change of intention on the part of the appellant to trade and would therefore have allowed the appeal and annulled the assessment. In the event, by reason of the Court of Appeal's unanimity in respect of a separate ground of appeal advanced by the appellant,[10] the appeal was allowed to the extent that the appellant was permitted to amend its ground of appeal against the assessment and the question of the valuation of the Lot for the purpose of assessing the taxable profit and the amount of tax thereon was remitted to the Board for determination.

B.5 Leave to appeal to this Court

21. The parties' respective applications for leave to appeal to this Court were dismissed by the Court of Appeal by its Decision dated 21 August 2018.[11] Their renewed applications to this Court for leave to appeal were heard by the Appeal Committee on 13 November 2018.[12] Leave to appeal was only granted to the appellant on the "question of law" basis and also on the "or otherwise" basis under the Court's statute.[13]

22. The question of law for which leave to appeal was granted arose because of a dispute between the parties as to the status of the Board minority's decision in the light of the successful appeal against the Board majority's decision and was in the following terms:

> "In the event of a successful case stated/appeal vitiating a majority decision of a board of review/tribunal ('the Majority Decision'), can the Court substitute the finding in the minority decision ('the Minority Decision') for that of the board of review/tribunal, with the consequence that any challenge to the Minority Decision is a challenge to a conclusion from primary facts which can only succeed if it is demonstrated to be unreasonable, illogical or plainly wrong? Or should the matter be remitted

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7 Neither party had sought to persuade the judge to uphold this.

8 CACV 115/2017, [2018] HKCA 301, Judgment dated 1 June 2018 ("CA Judgment").

9 Cheung & McWalters JJA.

10 Concerning the appellant's right, on the assumption the Lot was part of its trading stock, to have the value of the land disposed of taken into account in calculating its profit.

11 CACV 115/2017, [2018] HKCA 544.

12 FAMV 56 & 57/2018, [2018] HKCFA 55 (Ribeiro, Fok & Cheung PJJ).

13 Hong Kong Court of Final Appeal Ordinance (Cap.484), s.22(1)(b).

> to the board of review/tribunal with the opinion of the court for proper findings to be made free from the legal errors identified, unless it can be shown that the conclusion of the Minority Decision is the true and only reasonable conclusion?"[14]

23. Leave to appeal on the "or otherwise" basis was granted to the appellant to contend that "the majority of the Court of Appeal erred in concluding that the Taxpayer changed its intention as to the basis on which it held its property at Chong Yip Street, Kwun Tong, so that it disposed of the said property as a trading asset in the nature of a trade rather than selling the same as a capital asset."[15]

C. The ambit of this appeal

C.1 The relevant tax principles

24. It was not in dispute that profits tax would not be chargeable on the Initial Payment if it was a profit arising from the sale of a capital asset and would only be chargeable if it was derived by the appellant from its carrying on of "a trade, profession or business" in Hong Kong: Inland Revenue Ordinance (Cap.112) ("the IRO"), s.14(1). The term "trade" includes every trade and manufacture, and every adventure and concern in the nature of trade: *ibid.* s.2(1).

25. Since it was common ground that the Property had been held by the appellant as a long-term capital asset prior to its disposal, in order for the Initial Payment to be taxable under s.14(1), it would be necessary to find that there was a change of intention on the part of the appellant such that its intention was to dispose of the Property as part of a trade or business: *Church Body of Hong Kong Sheng Kung Hui v Commissioner of Inland Revenue*.[16]

26. Disposal of land at an enhanced value would not necessarily indicate an intention to trade by its owner, nor would the expenditure of money on the property in order to enhance its sale price necessarily lead to the conclusion that the landowner was engaging in an adventure in the nature of trade.[17]

27. The question of whether there is an intention to trade is a question of fact and:

> "… in determining whether an activity amounts to trading, the fact-finding tribunal must consider all the circumstances involved in the activity. It will then have to make a 'value judgment' as to whether this constitutes trading and whether the requisite intention to trade can be inferred. Regardless of what is claimed to be the intention subjectively, the question falls to be

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14 FAMV 56 & 57/2018, [2018] HKCFA 55, Determination dated 13 November 2018 at [2].
15 *Ibid.* at [1].
16 (2016) 19 HKCFAR 54 at [23], [44]-[47], [73].
17 *Ibid.* at [23], [48]-[49], [73].

> determined objectively having regard to all the surrounding circumstances."[18]

As that passage shows, in determining an intention to trade, it is important to identify the activity that is said to amount to trading and, in practical terms, to ask the question: "What trading or business venture has the taxpayer embarked upon?"

C.2 The approach of an appellate court

28. There was no dispute between the parties that the approach of an appellate court on an appeal on a point of law only is limited by the three propositions identified in *Kwong Mile Services Ltd v Commissioner of Inland Revenue*.[19]

29. In his judgment in that case, at [37], Bokhary PJ stated:

> "In an appeal on law only the appellate court must bear in mind what scope the circumstances provide for reasonable minds to differ as to the conclusion to be drawn from the primary facts found. If the fact-finding tribunal's conclusion is a reasonable one, the appellate court cannot disturb that conclusion even if its own preference is for a contrary conclusion. But if the appellate court regards the contrary conclusion as the true and only reasonable one, the appellate court is duty-bound to substitute the contrary conclusion for the one reached by the fact-finding tribunal. The correct approach for the appellate court is composed essentially of the foregoing three propositions. These propositions complement each other, although the understandable tendency is for those attacking the fact-finding tribunal's conclusion to stress the third one while those defending that conclusion stress the first two."

30. It follows that, even if the Board of Review's decision was vitiated by an error of law, it was not open to Chung J or the Court of Appeal (nor indeed is it open to this Court) to substitute a different conclusion to that drawn by the Board on the primary facts found unless the contrary conclusion is the true and only reasonable conclusion on those primary facts. Instead, the proper course would be to remit the matter to the Board of Review with the court's opinion for it to make findings on the relevant question (here, the question of whether there was a change of intention on the part of the appellant in respect of the Lot). Both parties recognised this proposition in making their respective submissions on this appeal and, as will be seen, each advocated that their conclusion on the primary facts was the true and only reasonable conclusion that could be drawn.

C.3 The parties' respective contentions

31. The appellant's case on appeal is straightforward. It being common ground that the Lot was held by the appellant as a long-term capital asset, it was for the

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[18] *Ibid.* at [50].
[19] (2004) 7 HKCFAR 275.

respondent to show that there was a change of intention on its part to trade the Lot. The appellant maintains that it had no intention to trade the Lot and that any intention to trade was that of Prodes, a separate legal entity to the appellant. This, it was contended, is embodied in the Minutes, the Redevelopment Agreement and the New Agreement. Since there was no change of intention to trade on the part of the appellant, the Initial Payment received by it was not chargeable to profits tax.

32. For the respondent's part, it was contended that the true and only reasonable conclusion on the facts was that the appellant did change its intention from capital holding to trading via its subsidiary, Prodes, as held by the Board minority. The contention was that the appellant was embarking on a venture in the nature of a trade in respect of the Lot as a property developer. As will be discussed in further detail later in this judgment (at Section D.3), at the hearing of this appeal it became apparent that the respondent was advancing an alternative argument, not dealt with by the courts below, concerning the nature of the trading venture on which the appellant embarked.

D. Did the appellant change its intention in respect of the Lot?

D.1 The conclusions in the courts below

33. The Board minority's finding – consistent with what Chung J and the majority of the Court of Appeal considered to be the correct conclusion – was that the appellant changed its intention to one of trading the Lot "on 30 July 1994 when the appellant entered into the Redevelopment Agreement".[20] The crux of the Board minority's reasoning leading to that finding was as follows:

> "121. The nature of a joint venture involves a commercial, business or trade purpose. Cheung Kong, Great Poka and the appellant entered into the Redevelopment Agreement to engage in trade with a view to making a profit. I do not accept that Cheung Kong and Great Poka joined hands with the appellant to merely enhance the old property for the benefit of the appellant.
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> 122. In my Decision, by the time the appellant had entered into the Redevelopment Agreement, the activities had gone beyond mere enhancement for the purpose of realising the old property for its maximum profit. The Redevelopment Agreement was in express terms binding on the appellant. The appellant was then engaged in trade."[21]

34. To the argument that it was Prodes, a separate legal entity to the appellant, that engaged in the nature of a trade in respect of the Lot, the Board minority held that the facts showed that Prodes "was the appellant's alter ego".[22]

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20 BOR Decision at [123].
21 *Ibid.* at [121]-[122].
22 *Ibid.* at [127].

35. In the Court of First Instance, Chung J rejected the appellant's argument that it did not change its intention and that the redevelopment was carried out by its subsidiary Prodes for three reasons.[23] First, he held that "the use of another legal entity to carry out the redevelopment was meant to be an 'internal' arrangement (hence the phrase 'for internal purposes')",[24] referring to the Minutes. Secondly, he held that the appellant's obligations under the Redevelopment Agreement did not end with the transfer of the Lot to Prodes because, in the event Prodes failed to enter into the New Agreement, clause 5.02 of the Redevelopment Agreement would deem the appellant to have replaced Prodes and, at Great Poka's request, the appellant would be obliged to execute the New Agreement. Thirdly, he held that clause 8.01 of the Redevelopment Agreement made it clear that the joint venture was between, on the one part, the appellant and, on the other, Great Poka and Cheung Kong.

36. In the Court of Appeal, Cheung JA (with whom McWalters JA agreed) rejected the appellant's first ground of appeal, which was that Chung J was wrong in holding that the Board minority did not err in finding that the appellant had changed its intention to trade in respect of the Lot.[25] His reasoning was similar to that of Chung J in the Court of First Instance. Thus, he held that:

> "By the terms of the Redevelopment Agreement together with the receipt of the initial payment, the Board cannot be faulted from forming the view that the only true and reasonable inference is that taxpayer had engaged in trade."[26]

Cheung JA also rejected the appellant's argument based on the separate legal personality of Prodes. He held that "the use of Prodes was only a method or mechanics of implementing the [appellant's] intention to trade."[27]

D.2 The intention to trade was that of Prodes, not the appellant

37. For the following reasons, I respectfully disagree with the conclusion reached by the courts below insofar as they held that the appellant changed its intention from disposing of the Lot as a capital asset to one of trading the same.

38. As already noted, it was common ground that the Lot was held by the appellant as a long-term capital asset. The steps taken by it, from 1991 onwards to enhance the value of the Lot by obtaining planning permission, government consent for a variation of the lease and approval of the building plans, are steps that are entirely consistent with the

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23 CFI Judgment at [52].
24 *Ibid*. at [46].
25 CA Judgment at [5.2] and [6.1] to [6.23].
26 *Ibid*. at [6.16].
27 *Ibid*. at [6.22].

appellant disposing of the Lot as a capital asset for the best price obtainable and do not necessarily evidence its intention to enter into a venture in the nature of a trade.[28]

39. The Minutes show clearly that, on 21 April 1994, the appellant decided to dispose of the Lot by way of a joint venture with Cheung Kong. However, the Minutes also show clearly that an entity "separate" to the appellant was to be used for this purpose and that it was the appellant's intention to sell the Lot to a subsidiary, which would then enter into the development venture with Cheung Kong. On their face, the Minutes support the appellant's contention that it did not change its intention with regard to the Lot but rather that it was going to dispose of the Lot by way of transfer to a subsidiary, which would then trade the Lot by redeveloping it with the assistance of Cheung Kong.

40. The fact that a subsidiary of the appellant was to be used for the purpose of the redevelopment of the Lot is important. The appellant and Prodes were two separate legal entities and "the court is not free to disregard the principle of *Salomon v. A. Salomon & Co. Ltd.* [1897] A.C. 22",[29] save in limited circumstances.[30] In the present context, one such circumstance might have been where the respondent was able to rely on section 61 or section 61A of the IRO,[31] which deal respectively with "artificial or fictitious" transactions and transactions designed to avoid liability for tax, but there is no suggestion in the present case that those provisions apply and the respondent has not sought to invoke them. Otherwise, as Lord Millett NPJ held in *ING Baring Securities (Hong Kong) Ltd v Commissioner of Inland Revenue*:[32]

> "… for tax purposes in this jurisdiction a business which is carried on in Hong Kong is the business of the company which carries it on and not of the group of which it is a member; the profits which are potentially chargeable to tax are the profits of the business of the company which carries it on; and the source of those profits must be attributed to the operations of the company which produced them and not to the operations of other members of the group."

41. In the circumstances, and with respect, the Board minority erred in holding that Prodes was the "alter ego" of the appellant. Chung J's reference to the phrase "for internal purposes" in the Minutes cannot change the fact that, absent some reason to ignore the separate corporate personality of Prodes, the operations of the appellant's subsidiary were not those of the appellant itself. Similarly, Cheung JA's conclusion that Prodes was "only a method or mechanics of implementing the [appellant's] intention to trade" [33] wrongly treats the appellant's subsidiary as a mere nominee or alter ego of the appellant. In my view, the courts below wrongly overlooked the fact that, interposed as it was into the

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28 *Church Body of Hong Kong Sheng Kung Hui v Commissioner of Inland Revenue* (*supra.*) at [23], [44], [48]-[49].

29 *Adams v Cape Industries plc* [1990] Ch 433 at 536 per Slade LJ.

30 *Prest v Petrodel Resources Ltd* [2013] 2 AC 415 at [35] per Lord Sumption JSC.

31 As was the case, for example, in *Commissioner of Inland Revenue v Tai Hing Cotton Mill (Development) Ltd* (2007) 10 HKCFAR 704.

32 (2007) 10 HKCFAR 417 at [134].

33 CA Judgment at [6.22].

redevelopment, Prodes was a separate legal entity embarking on its own account on a trading venture to redevelop the Lot and that, since it was doing so, it would be redundant for the appellant to engage in that venture.

42. That it was the appellant's intention that any redevelopment of the Lot be undertaken by its subsidiary, rather than by itself, was underscored by the terms of the Redevelopment Agreement entered into on 30 July 1994 (set out in Section A.2 above):

(1) That agreement recited that, subsequent to the surrender and re-grant of the Lot but "prior to redevelopment", the appellant "intends" to transfer ownership of the Lot "to its wholly owned subsidiary", defined as "Newco".

(2) By clause 3.02, the appellant granted the right to redevelop the Lot to Great Poka in consideration of the Initial Payment.

(3) Within four months of the grant of the new lease, the appellant was to transfer the registered and beneficial ownership of the Lot to Newco (clause 5.01).

(4) By clause 5.02, the appellant undertook to procure Newco to enter into the New Agreement with Great Poka and Cheung Kong. That New Agreement set out the terms on which the Lot was to be redeveloped. It was the appellant's subsidiary that was to embark on that venture, not the appellant. Although clause 5.02 also provided that, in the event Newco did not enter into the New Agreement, the appellant would do so, this was clearly a provision for the benefit and protection of Great Poka, since that company was granted a power of attorney to execute the New Agreement on behalf of the appellant.

(5) The Redevelopment Agreement would be terminated in the event that Newco did not execute the New Agreement (clause 6.01) and, in that case, the appellant would be obliged to refund the Initial Payment (clause 6.02).

43. The provisions of the Redevelopment Agreement referred to demonstrate that the appellant's intention, as reflected in the Minutes, was carried into effect by way of the joint venture to redevelop the Lot. Prodes was incorporated to fulfil the role of Newco. The appellant duly assigned the Lot to Prodes on 14 November 1994 and, on 24 November 1994, Prodes duly entered into the New Agreement with Great Poka and Cheung Kong. Significantly, the appellant was not a party to the New Agreement and the provisions of clause 5.02 by which the appellant might have become a party to it were never triggered so that the intention must have remained that Prodes would carry out the redevelopment rather than the appellant. The profits of the joint venture envisaged by the New Agreement were to be shared equally between Prodes, on the one hand, and Great Poka and Cheung Kong, on the other.

44. In these circumstances, the submission of Mr Paul Shieh SC,[34] that on a proper reading of the Redevelopment Agreement, it is clear that irrespective of whether Prodes had any intention to trade the appellant itself had the requisite intention to trade, cannot be accepted.[35] It emerged in the course of the hearing that there were two variants of this argument being advanced on behalf of the respondent. The first, more straightforward argument, is that the appellant was embarking on a venture in the nature of a trade by itself participating in the joint venture. The second alternative (which will be addressed in Section D.3 below) is that the appellant was engaged in a trade in the nature of procuring its subsidiary to enter into the joint venture agreement.

45. As regards the respondent's first line of argument, the whole structure of the contractual arrangements was for Prodes to carry out the property redevelopment and for the appellant to drop out of the picture. That this is what in fact happened supports the inference that this remained the appellant's intention throughout. Mr Shieh's reliance on the fact that the Redevelopment Agreement did not provide for the sale of the Lot by the appellant to Cheung Kong or Great Poka, or to Prodes,[36] does not alter the fact that the arrangement was for the appellant to assign the Lot to Prodes for it to carry out the joint venture. Nor does it matter that Prodes was incorporated after the execution of the Redevelopment Agreement,[37] since the critical question is one of the intention of the appellant in relation to the Lot and that intention is to be gleaned not only from the terms of the agreement but also the events subsequent to its execution.

46. There is nothing in these facts to suggest that the appellant's intention to dispose of the Lot to its subsidiary and to use that subsidiary as the vehicle to carry out the redevelopment joint venture of the Lot ever changed. As Mr Clifford Smith SC[38] submitted, the power of procuring its subsidiary to enter into the New Agreement lay entirely within the hands of the appellant, so that, even after the Redevelopment Agreement was executed, it would only be in the event that the appellant positively changed its intention from one of disposing of the Lot as a capital asset to one of trading the Lot itself that it might, by reason of clause 5.02, become a party to the New Agreement. As we have seen, it never did.

47. It is also material to note that the consideration received by the appellant for its grant of the redevelopment right to Great Poka (i.e. the Initial Payment of HK$165,104,100) and on its disposal of the Lot to Prodes (the sum of HK$314,315,900) amounted to a total of HK$479,420,000 being the amount at which the Lot was valued on 23 April 1994, taking into account the land premium paid (HK$61,420,000). In other words, it was intended that the appellant would receive no more than if it had sold the Lot, having paid the land premium, in the open market to a third party to redevelop.

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34 Appearing with Mr Mike Lui for the respondent.
35 Case of the Respondent at [22].
36 *Ibid.* at [22.2]-[22.3].
37 *Ibid.* at [22.4].
38 Appearing with Mr Justin Lam for the appellant.

D.3 The respondent's alternative trading argument

48. In the course of the hearing, Mr Shieh sought to advance an alternative argument as to the nature of the venture on which the appellant was engaged. The argument is found in the following submission in the Case of the Respondent:

> "The case is ***not*** one whereby [the appellant] had realised the capital value of the Lot and then left it completely to the independent judgment or discretion of Prodes to decide whether to redevelop the Lot. The whole deal was *preordained* by the terms of the Redevelopment Agreement (to which only [the appellant], Great Poka and Cheung Kong were parties) before Prodes had come into the picture. [The appellant] either (i) procured Newco to sign the New Agreement or (ii) took up the role of a joint venture partner with Cheung Kong carrying out the redevelopment/trade itself. Either way, [the appellant] was in a business venture as a trader."[39]

49. The point at (ii) in the passage quoted is the respondent's first line of argument, addressed in Section D.2 above. The respondent's alternative argument, at (i) in the passage quoted, is that the appellant was engaged in a trade or business of procurement, whereby it procured a subsidiary to enter into the property redevelopment joint venture and undertook various positive obligations under the Redevelopment Agreement. The profit arising on the venture was said to be the Initial Payment and Mr Shieh identified its source as the appellant's ability to grant contractual rights and undertake obligations.

50. This argument is different to the basis on which the Court of Appeal majority, Chung J or the Board minority decided in favour of the respondent and Mr Shieh candidly acknowledged that the alternative point he was advancing in this Court had not been raised in this form either before the Court of First Instance or the Court of Appeal.

51. Leaving aside the question of whether it was open to the respondent to advance a wholly new point on appeal to this Court, the alternative trading argument is, with respect, untenable. In advancing the argument, Mr Shieh invited us to look at the transaction commercially and as a matter of economics. However, doing so, the appellant's alternative argument lacks reality. It is to be remembered that one is asking the question, "What trading or business venture has the taxpayer embarked upon?" Here, the appellant was a toy manufacturer. It had been holding long-term a capital asset in the form of the Property. The substance of the transaction was that the appellant was disposing of that capital asset. It had enhanced the value of the asset prior to disposal by way of assignment to a subsidiary, who was intended to be a participant in a joint venture with Great Poka and Cheung Kong to redevelop the Lot, taking advantage of its enhanced value. The appellant was not intended to be a participant in that joint venture unless, by actions within its own control, it decided that its subsidiary would not participate. It was no part of the appellant's business to act as a procurer of joint venture participants for property developers. The rights it granted and the obligations it undertook were designed to enable the appellant to dispose of the Lot to

[39] Case of the Respondent at [22.4(d)] (emphasis in original).

its subsidiary and then to drop out of the joint venture project to redevelop the Lot. None of those rights or obligations supports a conclusion that the appellant was intending to embark on a venture in the nature of a trade in respect of the Lot.

D.4 The true and only reasonable conclusion on the facts

52. For these reasons, in my view, the true and only reasonable conclusion on the undisputed evidence and primary facts is that the appellant did not change its intention in relation to the Lot and did not enter into a venture in the nature of a trade in disposing of it. In this regard, I respectfully agree with the conclusion of Lam J, dissenting, in the Court of Appeal.[40]

E. Not necessary to address the question of law for which leave granted

53. In light of the conclusion reached in Section D.4 above, I would substitute the contrary conclusion that the appellant did not engage in a trade in disposing of the Lot in place of that reached by the Board of Review and the courts below. It is therefore unnecessary to address the question of law for which leave to appeal was granted.

F. Conclusion and disposition

54. For the above reasons, I would therefore allow the appellant's appeal and annul the assessment.

55. I would direct any submissions as to costs be filed in writing within 14 days of the date of the handing down of this judgment, to be dealt with on the papers.

Mr Justice Cheung PJ:

56. I agree with the judgment of Mr Justice Fok PJ.

Mr Justice Gummow NPJ:

57. I agree with the judgment of Mr Justice Fok PJ.

(Geoffrey Ma)	(R A V Ribeiro)	(Joseph Fok)
Chief Justice	Permanent Judge	Permanent Judge

[40] CA Judgment at [30].

(Andrew Cheung)
Permanent Judge

(William Gummow)
Non-Permanent Judge

Mr Clifford Smith SC and Mr Justin Lam, instructed by Pang & Associates, for the Appellant

Mr Paul Shieh SC and Mr Mike Lui, instructed by the Department of Justice, for the Respondent