CACV 196/1998

IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION

COURT OF APPEAL

CIVIL APPEAL NO. 196 OF 1998

(On appeal from Inland Revenue Appeal No. 2 of 1997)

BETWEEN

THE COMMISSIONER OF INLAND REVENUE	Appellant
and	
EMERSON RADIO CORPORATION	Respondent

Court : Hon. Mortimer, V.P., Godfrey & Rogers, JJ.A. in court

Hearing : 21 & 22 October 1998

Judgment : 12 February 1999

J U D G M E N T

Godfrey, J.A. :

Introduction

If you carry on business in Hong Kong, you are liable to profits tax on your assessable profits *arising in or derived from Hong Kong* : see s.14(1) of the Inland Revenue Ordinance, Cap. 112 ("the Ordinance"). The source of the profits is of fundamental importance. If the profits do not arise in or are not derived from Hong Kong from a business carried on in Hong Kong, they are not, generally speaking, subject to profits tax. However, s.15 of the Ordinance brings in to the charge to profits tax certain receipts which would otherwise escape.

In the present case, we are concerned with s.15(1)(b), under which sums (not otherwise assessable to profits tax) received by a person "for the use of or right to use in Hong Kong" various types of intellectual property (including a trademark) are to be *deemed* to be receipts of the recipient arising in or derived from Hong Kong from a business carried on in Hong Kong.

Here, the Commissioner of Inland Revenue ("the appellant") contends that certain sums received under a series of Royalty Agreements made between Emerson Radio Corporation ("the respondent"), which is incorporated in New Jersey, USA and does not carry on business in Hong Kong, and its wholly owned Hong Kong subsidiary ("the HK subsidiary"), were received by the respondent for the use of, or the right to use, *in* Hong Kong, the trademark to which the Royalty Agreements relate. The respondent contends that the sums in question were received by the respondent for the use of (*not* for the right to use) the trademark *outside* Hong Kong.

As we shall see, under the Royalty Agreements, the royalties to be received by the respondent from its HK subsidiary are calculated by reference to the sales made by the HK subsidiary *to its US customers*. That being so, the only relevant "use" of the trademark, says the respondent, is its use offshore; for only that use generates the receipts which the appellant seeks to assess to profits tax. On the contrary, says the appellant, the HK subsidiary did "use" the trademark (and in any case had been granted "the right to use" it) by applying it, in Hong Kong, to the goods in the course of their manufacture; and the locality of the sales is irrelevant.

The Board of Review rejected the respondent's contention. On appeal by the respondent, the judge (Mr. Robert Ribeiro, S.C., sitting as a Recorder of the Court of First Instance) held that only those receipts representing royalties paid to the respondent in relation to the sale of goods manufactured in Hong Kong rather than elsewhere were caught by s.15(1)(b). Before us, the appellant and the respondent maintain, in the case of the appellant, that *all* the receipts, and in the case of the respondent, that *none* of the receipts, are assessable to profits tax; but, failing this, each is content to accept the view of the judge, with his consequential direction of the necessary apportionment.

We have to decide who is right; the appellant; the respondent; or the judge.

The facts

The facts may, for present purposes, be shortly stated.

The original Royalty Agreement (made on 1 April 1984) between the respondent and its Hong Kong subsidiary, after reciting (in Clause 1) that the respondent (described as "Emerson") held the rights for the use of the trademark "Emerson" for electronic home entertainment products sold in the US, and that its HK subsidiary wished to continue to sell "Emerson" brand products to customers with locations in the US, provided (in clause 2) as follows :

> "2. Compensation
>
> Emerson HK agrees to pay Emerson for the use of the 'Emerson' trademark on products it sells to its US customers. The fee to be paid will be 1.8 percent of the sales price of the products sold to the US customers of Emerson HK. If during any fiscal year ending March 31 sales by Emerson HK to US customers exceed $50,000,000, the fee on the excess sales will be 1 percent of the sales price of products sold in excess of $50,000,000. Payment of the royalty fees will be due within thirty days after the end of each month."

(In 1987, and again in 1991, the rates of royalty were revised upwards; nothing turns on this.)

Goods bearing the respondent's trademark "Emerson" were duly manufactured by its HK subsidiary, both in Hong Kong and elsewhere, and duly sold by the HK subsidiary to its US customers. But the HK subsidiary did not sell any goods to customers in Hong Kong; and it did not conduct any selling activities in Hong Kong in relation to sales outside Hong Kong. Its activities in Hong Kong were limited to handling paperwork; receiving purchase orders from the respondent; issuing purchase orders to manufacturers; arranging and handling letters of credit facilities; co-ordinating shipments of goods; and liasing with manufacturers concerning production of goods.

The issues

The questions in issue are questions of law; more precisely, questions as to the true construction of the words "for the use of" where the same appear in s.15(1)(b) and in Clause 2 of the Royalty Agreements.

The questions of construction

It is first to be observed that the sums caught by s.15(1)(b) are sums received either "for the use" or "for the right to use" the trademark, etc. In my opinion, the distinction here drawn is a distinction between a sum paid and received for the *actual* use of the mark, and a sum paid and received for *the right* to use the mark even if no actual use of the mark is made at all. So the character of the sums paid and received must be ascertained by reference to the terms of the contract between the payer and the payee.

Under Clause 2 of the Royalty Agreements here, the payments provided for are to be made, as it seems to me, not for *the right* to use the mark, but "for" its *actual* use.

On this footing, the appellant says the application of the mark to the goods in Hong Kong, and all the activities in Hong Kong ancillary or preparatory to sale of the goods, constitute "use" of the mark in Hong Kong. The respondent, on the other hand, says that payments for the use of the mark under Clause 2 of the Royalty Agreements are payments in respect of sales of the goods *outside* Hong Kong and so are not payment for the use of the mark *in* Hong Kong.

I do not think this difference can be resolved by reference merely to the ordinary meaning of the words "for the use of" in s.15(1)(b), which are much too general to admit of such an approach. Of course, in a sense "use" of a trademark takes place whenever it is applied to the goods; indeed, it is a "use" of a trademark simply to reproduce it on an invoice for the goods : see *Cheetah Trade Mark* [1993] FSR 263. But we are not looking for any general meaning; we are looking for the meaning of the words "for the use of" where they appear in their context; i.e., in s.15(1)(b). What are the payments made "for"?

The payments made under the Royalty Agreements here are not made, as I consider, for the privilege of applying the mark to the goods; they are payments made for the right to sell the goods bearing the mark, and thereby to generate the receipts in respect of which the royalties are to be paid. Here there were no such sales in Hong Kong; nor were any such sales contemplated. For the purposes of s.15(1)(b), there was no relevant "use of" the mark in Hong Kong.

Conclusion

In these circumstances, I find myself unable to agree with the judge or with the appellant. I would hold, that on the facts found by the Board, the Board should have held that for the purposes of s.15(1)(b) the HK subsidiary did not use the respondent's trademark in Hong Kong but only outside Hong Kong. That conclusion is sufficient (save as to costs) to dispose of this appeal.

Rogers, J.A. :

The questions in this appeal arise primarily from the questions posed in the Case Stated :-

> “1. Whether the true and only reasonable conclusion that can be drawn from the primary facts found and evidence accepted by the Board is that the Hong Kong Company did not use the trademark in Hong Kong?
>
> 2. Whether, if the trademark was used in Hong Kong, the true and only reasonable conclusion that can be drawn from the primary facts found and evidence accepted by the Board is that the royalty payments were not made for the use in Hong Kong of the trademark?
>
> 3. Whether, on the facts found by the Board, the Board erred in law in a holding that :
>
> (i) the Hong Kong Company used the trademarks in Hong Kong for the purposes of section 15(1)(b) of the Inland Revenue Ordinance; and/or
>
> (ii) all of the royalty payments made in respect of the use of the trademarks were royalty payments made in respect of the use of the trademarks in Hong Kong for the purposes of section 15(1)(b) of the Inland Revenue Ordinance?
>
> 4. In the alternative, whether, on the facts found by the Board, the Board erred in law in refusing to apportion the royalty payments between payments for use of the trademark in Hong Kong and payments for the use of the trademark outside Hong Kong as the Board held that the royalty payment was one indivisible sum?”

There is a supplemental question which turns on whether the royalty payments were for the use of the trademark or the right to use the trademark in Hong Kong.

The Board in coming to its decision remarked that whether or not the royalties were taxable under section 15(1)(b) is not a matter of different people forming different views, there could only be one correct answer and that is a question of law and fact. That truism belies the fact that this case has already demonstrated that there is broad scope for divergence as to what that correct answers are.

The facts found by the Board

I would draw attention to the following facts which were found by the Board. In setting them out, I have, for convenience, used the numbering which appears at page 5 of the Case Stated and I refer to those parts of the facts which I consider important to this judgment :-

"(ii) Products were manufactured ….. inside Hong Kong.

(vii) The Hong Kong Company's activities in Hong Kong were limited to handling paperwork; ….. issuing purchase orders to manufacturers; arranging and handling letter of credit facilities; co-ordinating shipments of goods; and liasing with manufacturers concerning production of goods.

(ix) The 'Emerson' trademark existed in many countries, including the countries where the goods were manufactured (Taiwan, Japan, Malaysia, Thailand, Hong Kong) and in ….. (USA).

(x) The 'Emerson' trademark was physically applied to the products by the manufacturers."

The Royalty Agreement

The receipts which are the subject of the present appeal arose by reason of the Royalty Agreements. The Agreements were all essentially in identical form and varied only as to the percentage payable as royalty and other matters which do not affect this case. The material wording is in Clause 2 of the first 2 Agreements which reads :

"Emerson HK agrees to pay Emerson *(i.e. the Taxpayer)* for the use of the 'Emerson' trademark on products it sells to its US customers. The fee to be paid will be ___ percent of the sales price of the products sold to the US customers of Emerson HK."

Clearly, on this wording, the royalty payment was a payment in arrears for each use of the mark. If there were no use, there would be no royalty payment. Hence, in my view, this Royalty Agreement was clearly an agreement to pay for use of the mark rather than the right to use the mark.

The question then arises as to whether the payment is a payment for the use of the United States mark alone or whether it is a payment for use of the Emerson trademark in each country relevant to the specific transaction in respect of which the royalty for the sale is being paid. Although the words in Clause 2 of the Royalty Agreement "use of the 'Emerson' trademark on products ….." could mean a use of the Hong Kong (or for that matter Taiwanese, Japanese, Malaysian, Thai or any other) Emerson trademark, in the context in which it is used in the Royalty Agreement, I consider that the words of Clause 2 are specifically referable to the US trademark since it is to that which reference is made in Clause 1 of the Agreement. Nevertheless, as Mr. Barlow, on behalf of the Taxpayer, conceded in argument, there must be an implied licence from the Taxpayer to Emerson HK to use the trademark in Hong Kong insofar as is necessary. In the circumstances of this case, it does not seem to me to be of consequence that the licence is an implied licence as opposed to an explicit licence. The implication of the licence springs from the Royalty Agreement itself and thus the licence to use in the countries other than the United States is comprehended within the Agreement. Hence, the payment under the Royalty Agreement is a payment not merely for use of the trademark in the United States but for use of the Emerson trademark in such other countries as it has been used for the purpose of accomplishing the relevant sale in the US.

The Appellant's argument

The thrust of the Appellant's argument is that there has been no use of the Emerson trademark in Hong Kong.

Section 14(1) provides that whether there has been use of the trademark in Hong Kong is fundamental because of the wording of the Inland Revenue Ordinance "profits tax shall be charged ….. in respect of (the Taxpayer's) assessable profits arising in or derived from Hong Kong …..".

Section 15(1) is a deeming provision. It provides that :

> "For the purpose of this Ordinance, the sums described in the following paragraphs shall be deemed to be receipts arising in or derived from Hong Kong from a trade, profession or business carried on in Hong Kong ….
>
> (b) sums, not otherwise chargeable to tax under this Part, received by or accrued to a person for the use of or right to use in Hong Kong a …... trademark ….."

The use of the words "not otherwise chargeable to tax" would indicate that one or more of the conditions necessary for charging tax in accordance with section 14(1) might not have been complied with.

In essence, the argument is that a trademark is a mark used in the course of sale of an article for the purpose of denoting origin. Since the sales of the articles took place in the United States, there was no use of the trademark in Hong Kong.

Whatever historical or theoretical basis there might be for that proposition, in common understanding, the application of a trademark to goods by a manufacturer constitutes use of that mark. Furthermore, the statutory trademark law since the introduction of legislation relating to trademarks in the last century has treated the application of a mark to goods by a manufacturer as use both for the purposes of infringement and for the purposes of use necessary for the existence of a mark and maintenance of registration. Moreover, the law relating to merchandise marks and more lately trade descriptions, again treats use by a manufacturer as use of the mark no matter who sells the goods or where the goods are sold. The first question in the Case Stated must therefore be answered in the negative.

Once, therefore, it is established that royalty payments are made, at least in part, for the use of the trademark in Hong Kong, the Appellant's argument falls away and the second question also has to be answered in the negative.

The Commissioner of Inland Revenue's arguments

Mr. Kotewall, S.C. sought to put the basis upon which the Commissioner claimed the Taxpayer's liability to tax on four bases.

1. Use by the US parent in licensing

It was argued that the taxpayer had used the Emerson trademark in Hong Kong by licensing the Hong Kong Company to use its trademark. I entirely agree with the views expressed by the Recorder below that this argument is based upon a misconstruction of section 15(1)(b). In my view, the wording of that sub-section requires a payment to the Taxpayer by another person on account of that other person's use or the permission granted to that other person to use the trademark. The sub-section does not relate to sums which the Taxpayer receives or accrues by reason of his own use of the trademark. Furthermore, in my view, to construe the word "use" in relation to a trademark to cover mere licensing and no more would be to stretch the meaning of that word beyond what is legitimate.

2. The Hong Kong Company's royalty payments were in respect of rights to use the mark

There are two matters which arise in this context. The first is as to whether this argument can be raised at all and the second is as to whether, if it is raised, the argument is sound.

A. Can this question be raised

The Recorder below allowed the question to be raised. In my view, it was open for him to do so but as I have indicated and will seek to expand below the issue of law sought to be raised, in my view, fails.

The procedure for appeal by way of Case Stated from the Board to the High Court is governed by section 69 of the Inland Revenue Ordinance. Section 69(1) reads :

> "The decision of the Board shall be final :
>
> Provided that either the appellant or the Commissioner may make an application requiring the Board to state a case on a question of law for the opinion of the ….. court."

It might be supposed on the basis of that wording that the Case Stated must contain the only question of law which may be raised. But section 69(5) reads :-

> "Any judge of the High Court shall hear and determine any question of law arising on the stated case and may in accordance with the decision of the court upon such question confirm, reduce, increase or annul the assessment determined by the Board, or may remit the case to the Board with the opinion of the court thereon. Where a case is so remitted, the Board shall revise the assessment as the court may require."

The Recorder below considered that on its own, the wording of section 69 would preclude the High Court from considering any question of law were it not contained in the Case Stated. I consider however that the words of section 69(5) should be given a more liberal interpretation and that the Court would be empowered to determine a question of law which it considered arose from the Case Stated.

On the basis of authority however, the Recorder held that it was open to the Court to determine a question of law if it arose out of the Case Stated. For my part, I would also agree with this and I do not consider it necessary to go through those authorities or to comment further thereon other than to say that if the matter be a new point not argued before the Board, there may be problems caused by the fact that sufficient facts have not been found by the Board which would preclude a Court from hearing and determining a question or would dictate that the case be remitted for further consideration. Be that as it may, in my view, the point raised fails.

B. <u>The right to use</u>

The argument on behalf of the Commissioner on this footing is based upon the premise that the US parent company gave permission to the Hong Kong Company to use the trademark in any country which it chose. The country of manufacture was a matter of choice for the Hong Kong Company. Hence, in making royalty payments under the Royalty Agreement, the Hong Kong Company was paying in part for a right to use the trademark in Hong Kong even though for a particular transaction, it was not so used.

That argument would have validity if there were a blanket licence or if there were a single licence fee payable irrespective of the quantities manufactured. But that is not this case. In this case, a royalty was payable in respect of each item sold based upon the selling price of that item and each item was subject to a royalty payment severally. Since, of course, that assessment of the royalty payment would be one made upon the sale and hence after manufacture, the royalty payment was a payment in respect of use which had in fact been made. There was therefore in respect of, for example, a product manufactured in Taiwan, no question of any right to use the trademark in Hong Kong since the royalty payment was made after the relevant events in respect of use which had been made of specific trademarks. That did not include in respect of the Taiwan manufactured goods any use of the Hong Kong trademark.

3. Use by ordering goods to be manufactured

The third argument of the Commissioner is based upon the fact that the royalties paid were part of the Hong Kong Company's business expense to earn Hong Kong sourced profits. The Commissioner submits that the trademark was used in the Hong Kong Company's profit generating activities, in particular, it was argued that the Hong Kong Company used the mark by causing goods to be made by third parties not only in Hong Kong but in China, Malaysia, Thailand, Taiwan, Japan and South Korea bearing the name of the Taxpayer. Reliance was placed upon the instructions given for the manufacturer of those products by the Hong Kong Company and by the purchase by the Hong Kong Company of those goods which were then sold to customers in the United States. It is not clear that use of the trademark "Emerson" was made on, for example, invoices, order forms and other material but for the purposes of this judgment, it is assumed that it was.

For a mark to constitute a trademark in relation to goods, not only must there be a mark but there must be goods in relation to which the mark is used. Although therefore use of a mark on an invoice can be use of a trademark, that cannot be use of that trademark within the jurisdiction if the goods never came within the jurisdiction. We have been referred to 3 cases *Hermes Trade Mark* [1982] RPC 425, *Cheetah Trade Mark* [1993] FSR 263 and *Stichting Greenpeace Council v. Income Team Limited* [1996] 1 HKLR 269 in which use on an invoice has been held to be use of a trademark. In each case, however, the relevant goods were goods within the jurisdiction.

It is unnecessary for the purposes of this judgment to question the full extent of the truth of the statement in paragraph 11(ix) of the Case Stated where it is said :-

"Without the licence from its parent the Hong Kong Company could not have carried on its business in Hong Kong."

It can be said, however, that it would not be an infringement of a trademark in Hong Kong for one person to order goods marked legitimately with the mark in one country and have them transported directly and sold in another country where the use of that mark in relation to those goods is likewise legitimate, if despite that, the goods marked with that mark were subject of third party rights in Hong Kong.

The putting of a trademark on an invoice is, in my view, therefore not a use of the trademark in Hong Kong if the goods to which that trademark refers never came within Hong Kong at any stage.

The broader aspect of this part of the argument on behalf of the Commissioner namely that the royalty payments constituted a business expense in relation to the Hong Kong Company which paid profits tax on the basis that its profits were generated from a trade or business and were sourced in Hong Kong fails, in my view, to address the correct question. The correct question is not whether the royalty payment in question is derived from a business carried on in Hong Kong but whether the royalty payment in the terms of section 15(1)(b) was for use of a trademark in Hong Kong. This aspect of the argument therefore avoids the real question.

4. <u>Royalty payments were single indivisible sum</u>

In some respects, the fourth argument on behalf of the Commissioner was similar to the third in that it sought to rely upon the aspect that the royalty payments were derived from profits on sale by the Hong Kong Company. It was argued that the licence was necessary for the Hong Kong Company to carry on its trade. On the basis that goods bearing the mark were manufactured under instructions in Hong Kong, it was argued, in my view, correctly that there had been use of the trademark in Hong Kong.

It was said however that the royalty payment was a single indivisible sum. I find myself unable to agree with this proposition. The Royalty Agreement appears to me to be clear. It is that the fee will be paid as a percentage on the sales price of the products sold to the US customers. In that regard, the percentage possibly was, for matters of convenience, worked out on the basis of the global sales figures of the Hong Kong Company but in reality it related to each individual item which was sold. The payment calculated in respect of an item, for example, manufactured in Taiwan and shipped directly to the United States would have been no different in principle than would have been a payment in respect of use of a trademark in Taiwan for goods which were wholly manufactured and sold in Taiwan.

True it is that it might be said that the licence was a global licence to the extent that it appears to have been offered and accepted on an all or nothing basis in the sense that the licence to sell in the United States and the implied licence for the use in Hong Kong was dependent on the agreement to pay royalties in respect of all products sold in the United States no matter where they had been manufactured but, on my analysis, that argument must fail because it does not make the royalty payments indivisible. If a hypothetical product were manufactured in Hong Kong and sold in the United States in the first half of the year and royalty payments had been made in respect thereof, it could not be said that any subsequent royalty payments for goods manufactured in another country and sold in the United States in the second half of the year in any way validated or licensed the use of the trademark in Hong Kong in the first half. To explore that analysis further, if it were alleged that the manufacture and exportation of the goods in Hong Kong in the first half of the year were either an infringement or an offence because of non payment of royalties based on the manufacture in the third country and sale in the United States somewhat later, that argument would be bound to fail because the use in Hong Kong was clearly a licensed use : payment of royalties would have been made in respect of the goods which had been manufactured in Hong Kong, the failure to pay in respect of the goods which had been manufactured elsewhere would not operate retrospectively to invalidate the licence.

Whilst it must be acknowledged that there is scope for argument in this matter and I differ from the conclusion reached by the experienced Board after much deliberation, I have come to the clear view that the judgment of the Recorder that the payments were, in principle, divisible must be correct.

In my view, therefore, this appeal should be dismissed.

Mortimer V-P :

The respondent, Emerson Radio Corporation (Emerson), is the owner of the trademark “Emerson” for electrical goods sold in the United States of America. It does no business in Hong Kong but Emerson Radio (Hong Kong) Ltd (the subsidiary) is its wholly owned subsidiary doing business in Hong Kong. Emerson and the subsidiary have a royalty agreement whereby the subsidiary “agrees to pay Emerson for the use of ‘Emerson’ trademark on products it sells to its US customers”. These royalty fees are due within 30 days after the end of each month.

These payments received by Emerson were assessed as chargeable to profits tax under s.15(1)(b) of the Inland Revenue Ordinance as payments received for the use of a trademark in Hong Kong. The Board of Review upheld the assessments and the taxpayer appealed. On 30 June 1998 Mr Recorder Ribeiro SC allowed the appeal in part holding that only royalty payment received in respect of goods sold in the US but manufactured and trademarked in Hong Kong were chargeable to tax. He ordered an apportionment of the amounts paid.

Both the Commissioner of Inland Revenue (the Commissioner) and Emerson appealed. The Commissioner contends that all the payments are chargeable to tax. Emerson contends that none are chargeable to tax.

The facts

Although the subsidiary carries on business in Hong Kong, the goods upon which it pay royalty fees under the agreement were manufactured and trademarked in various parts of the world. Some had the trademark affixed in Hong Kong. In respect of all the goods the purchase orders were received in Hong Kong and all the arrangements for manufacturing, trademarking, shipping, payment and credit were made in Hong Kong. The details are in the case stated.

The royalty agreement limits the payment of royalty fees for using the trademark on goods sold by the subsidiary to customers in the US. But this agreement does not reflect the full legal relationship between Emerson and the subsidiary on the trademark. It is conceded that the sums payable must have included payment for the use of the trademark on the goods in the manufacturing of them before sale in the US by necessary implication.

The law

Section 14 of the Inland Revenue Ordinance (Cap. 112) (IRO) is the general charging provision to profits tax. The relevant parts are:

> "… on every person carrying on a trade … or business in Hong Kong in respect of his assessable profits, arising in or derived from Hong Kong … from such trade … or business …"

There are deeming provisions in s.15(1)(b) in respect of sums received outside Hong Kong for the use of a trademark in Hong Kong which are not otherwise chargeable to tax. Section 15(1)(b) in its relevant parts provides:

> "15. Certain amounts deemed trading receipts
>
> (1) For the purposes of this Ordinance, the sums described in the following paragraphs shall be deemed to be receipts arising in or derived from Hong Kong from a trade … or business carried on in Hong Kong-
>
> (a) …

(b) sums, not otherwise chargeable to tax under this Part, received by … a person for the use of or right to use in Hong Kong a patent, design, trademark …"

The issues

As I see it, there are two live issues. I do not find it necessary to deal any further with Mr Kotewall SC's argument concerning the use by the US parent in licensing. I agree with the Recorder and Rogers JA that the submission fails for the reasons they have given.

The first issue is whether on the facts and within the meaning of s.15(1)(b) of the Ordinance, the sums received by Emerson, or any part of them, under the royalty agreement were for the use of the trademark *in Hong Kong*. Any such sums are chargeable to tax.

The second issue is whether the sums received by Emerson under the royalty agreement, or any part of them, were for the "right to use" the trademark *in Hong Kong*.

The right to use the trademark in Hong Kong

It is convenient to deal with the second issue first. In short, the submission is that by organising the whole of the business from Hong Kong including arrangements for the trademark to be fixed elsewhere before delivery and sale in the United States, part of the royalty payments were for the use of the trademark in Hong Kong. This is an attractive submission.

The search for the answer does not lend itself to any elaborate examination. It is a matter of mixed fact and law. In reaching an answer, I am influenced by the principle of "territoriality" of the tax regime established in Hong Kong. In my judgment, the proper approach is that the royalties received for goods manufactured abroad to which the trademark is affixed are received for the use of the trademark in other places and not for the right to use the trademark in Hong Kong. On this view of the matter, there is no difference between the payments received "for the use of" and for the "right to use" the trademark in Hong Kong.

The use of the trademark in Hong Kong

Following the same approach I would hold that part of the royalty payments are for the use of the trademark in Hong Kong. That is for the use of the mark when it is affixed to the goods during the manufacture of the goods made in Hong Kong. I agree with and adopt the reasons advanced by Rogers JA.

Conclusion

For these reasons, I would uphold the Recorder's decision and dismiss the appeal. I feel driven to this conclusion with some reluctance because the assessment of the correct sums chargeable to tax may not be straightforward and convenient.

It follows by a majority both the appeal and the cross-appeal are dismissed. In the absence of agreement between the parties on costs, this matter should be re-listed for submissions within the next 28 days.

(Barry Mortimer)	(Gerald Godfrey)	(Anthony Rogers)
Vice President	Justice of Appeal	Justice of Appeal

Mr. Robert G. Kotewall, Q.C., S.C. & Mr. Herbert Li (Department of Justice) for Appellant

Mr. Barrie Barlow (M/s. Baker & McKenzie) for Respondent