Case No. D27/85

Board of Review:

H. F. G. Hobson, *Chairman*; Y. C. Jao, B. H. Tisdal, *Members.*

25 October 1985.

Profits Tax — Section 14 of the Inland Revenue Ordinance — profits on the resale of goods overseas—whether derived from Hong Kong.

The Appellant was a Hong Kong Company. It bought aluminium from a Taiwan supplier and resold them to a Japanese sub-buyer. Subsequent to negotiations made in Taiwan, the sub-buyer placed orders with the appellant in Hong Kong, accompanied by a Letter of Credit. The Appellant in turn applied for back to back credit facilities locally in favour of the supplier. Other necessary documentation work was also performed by the Appellant in Hong Kong while the goods were shipped directly from Taiwan to Japan. The Commissioner determined profits tax on the profits arising from the transactions. The Appellant appealed.

Held:

Following the approach in Sinolink Overseas Ltd. v. C.I.R., I.R.A. No. 1 of 1985, the Board found on the evidence before them that the profits on the transactions arose in Hong Kong; the Appellant acted as a principal and performed work beyond that of a passive middleman.

Appeal dismissed.

So Chau Chuen for the Commissioner of Inland Revenue.
T. M. Ho of Messrs T. M. Ho & Co. for the Appellant.

Reasons:

The issue before the Board was whether profits made by the Appellant Hong Kong company on the resale of aluminium, bought from a Taiwan source and resold to a buyer in Japan, arose in or were derived from Hong Kong.

The Appellant was represented by Mr. T. M. Ho and Mr. SO Chau-chuen, Assessor (Appeals), appeared for the Revenue.

The transaction to which the Board's attention was drawn occurred in the 1980/81 year of assessment. We were told that it followed a pattern established over about three preceding year, via the Chairman of the company would go to Taiwan towards the last quarter of each year to meet a representative of the Japanese sub-buyer to settle the latter's requirements for the subsequent year. It was submitted that this would be followed by a

tripartite meeting between the aforementioned chairman, the Japanese representative and the Taiwan supplier, however no evidence whatsoever was adduced of any such meeting with the Taiwan supplier for any transaction let alone the one under review. However Mr. Ho produced a minute of a meeting held on the 8 January 1982 between the Chairman (with another representative of the Appellant) a representative of the sub-buyer and a K of a company in Taiwan who, we were told, would act for the Appellant in overseeing supplies by the Taiwan supplier. That meeting dealt with the procurement of aluminium for 1982 to be supplied "latest by May 20, 1982". We were prepared to accept this 1982 minute as indicative of the type of minute recorded for the 1980 transaction, though it does not bear out the assertion that meetings were regularly held towards the end of the last quarter of each year. Mr. Ho maintained that the minute was evidence of an oral contract between the sub-buyer and the Appellant, however the minute itself presupposes formal orders, with detailed specifications and breakdown, and a letter of credit are to be issued by the sub-buyer. Without further convincing evidence—the Chairman we were told was not available to give evidence—we do not think that a binding oral contract was concluded in Taiwan. We believe that the arrangement was subject to the sub-buyer actually laying precies and detailed orders: however we accept that this is to judge the legal position according to Hong Kong Law, but in the absence of evidence upon Taiwan law we feel bound to assume it is the same as the former.

In the event the sub-buyer did place orders for the transaction concerned at least to the extent of 100 m.t. of aluminium. We were shown copies of the various documents which are summarized thus.

—7.5.80 Indent (entitled "2nd amended") by the Appellant for 206 metric tons split into various categories of specifications on C & F terms at a gross price of US$2,370 per metric ton. No evidence was led as to how the quantities and specifications were arrived at, it may be that they were determined in accordance with the minute of a preceding meeting between the Appellant and sub-buyer in Taiwan followed by telex exchanges between them and then with the Taiwan supplies. That seems logical, though it is speculation on our part. However one item for 100 m.t. is shown with the specification "2.5 × 322 × 1282 mm". It is this which is the subject of the following papers. No evidence was available as to whether the further 106 m.t. were intended for the Japanese sub-buyer or for some other party.

—9.5.80 Order by the sub-buyer on the Appellant for 100 m.t. at US$2,490 per m.t. on CIF terms.

—15.5.80 Sanwa Bank, Tokyo, opened an L/C for the sub-buyer in favour of the Appellant, the Chartered Bank in Hong Kong acting as the advising bank. The L/C covered 100 m.t. 2.5 × 322 × 1282 mm at US$2,614.50 per m.t., partial shipments were permitted. Negotiation was against customary document, viz. sight draft, clean O/B freight prepaid B/Ls, commercial invoice, packing list and insurance (at 110% of invoice value).

—17.5.80 Chartered Bank advised the Appellant of the incoming L/C and offered to negotiate the documents and drafts to be drawn thereunder.

—20.5.80 the Appellant applied to the Chartered Bank to open an L/C in favour of the Taiwan supplier for the 100 m.t. (2.5 × 322 × 1282 mm)—partial shipments permitted—the value of this being US$231,098.70. The Appellant to be responsible for insurance, thereby conforming with the sub-buyer's CIF terms and the Taiwan suppliers 2nd amended indent wherein CIF terms are specified.

Though it is evident from other papers that the Chartered Bank did open an L/C (no. 253/1146(B) pursuant to this application the L/C itself was not produced. However we believe it is reasonable to assume that it was back-to-back with Sanwa's L/C in all respects except price and the invoices evidencing the price.

—Two undated invoices by the Taiwan supplies no. 69154 for 51 m.t. (which refers to Chartered Bank L/C 253/11466B 21 May 1980), no. 69157 for 34 m.t. with the same notation. With each invoice is a B/L for the same ship and same voyage, a certificate of origin, a certificate of inspection and a packing list—all eminating from Taiwan. In short the 85 m.t. was evidently on account of the 100 m.t. ordered by the sub-buyer: there are however no papers showing that if anything happened to the 15 m.t. balance.

—On a date we cannot decipher, but is must have been before the Taiwan supplier drew down on Chartered Bank's L/C, the Appellant signed a request to the Chartered Bank to negotiate the Sanwa L/C and the corresponding bill (i.e. the Taiwan supplier's bill of exchange) under Chartered Bank's L/C.

—3.6.80 Insurance certificate issued in Hong Kong for 85 m.t. for US$232,815 (i.e. 110% of the Appellant invoice, see below).

—4.6.80 Appellant's invoice on sub-buyer for 85 m.t. at a total of US$211,650.

—4.6.80 Appellant's bill of exchange for US$211,650 drawn on Sanwa Bank.

—4.6.80 Packing list made up by Appellant in Hong Kong. This embodies all the details shown in the packing lists accompanying the Taiwan supplier's invoices.

We were referred by Mr. So to a recent High Court decision—Sinolink Overseas Ltd. -v- CIR (IRA No. 1 of 1985) which deals with the fundamental considerations on the determination of factual issues in a case such as the one before us. We intended to adopt that approach in this case:—

1. The pre-contract preparation and management, so far as the relationship between the Appellant and the sub-buyer is concerned, took place in Taiwan, No evidence

was adduced regarding any pre-contract arrangements with the Taiwanese supplier—all we have is a copy of the indent placed by the Appellant with the Taiwan supplier for 206 m.t. A representative, not an employee but a commissioned supervisor in Taiwan, would supervise the Taiwan's supplier's part in the transaction.

2. The making of the contract of purchase. The only evidence of the purchase by the Appellant from the Taiwan supplier, is the Indent, which confirms the purchase and requests that a duplicate be signed by the supplier and returned for record purposes. The Indent appears therefore to be confirmatory of a commitment already made. Possibly the latter was made in Taiwan—and we are inclined to that view because of K's presence in Taiwan: we accept however that this inference has the thinnest of foundations.

3. The making of the contract of sale. We believe that a firm binding contract only arose between the Appellant and the sub-buyer when the subbuyer placed an order with the Appellant.

4. Post-contract performance and management. The goods themselves were supplied directly from Taiwan to Japan: this aspect therefore took place outside Hong Kong. However the other ingredients of the post-contract performance by the Appellant were (*a*) the opening in Hong Kong of a back-to-back L/C in favour of the Taiwan supplier and (*b*) presentation in Hong Kong of documents, including insurance arranged by the Appellant in Hong Kong and the Appellant's packing list, to enable collection under the incoming L/C.

In our opinion the profit on the transaction arose in Hong Kong and is represented by the difference between that which is received in Hong Kong by Chartered Bank, as advising bank for the Japanese bank, and the amount of the L/C opened by Chartered Bank on behalf of the Appellant: in short the profit manifested itself in the books of the Chartered Bank Hong Kong. In addition the Appellant's part in the transaction was not simply that of a passive middle man—it had to open an L/C and it did that in Hong Kong. In order for the Appellant to get paid it had to present documents in Hong Kong and it needed to prepare some of those documents itself.

Mr. Ho for the Appellant at one point suggested that the Appellant was merely an agent and referred to CIR -v- International Wood Products Ltd. (HK Supreme Court 1971) which was concerned with an agency situation. However we rejected any suggestion of agency, being satisfied that in both the buying and the selling the Appellant was acting as a principal, Mr. Ho thereupon retracted the contention.

Mr. Ho also referred to BR case No. D15/82 but in that case Hong Kong was merely a place where liaison took place, Macau being the base where the transactions were effected by a Macau sole proprietorship which had functioned previously without reference to Hong

Kong until the proprietor was induced to set up a Hong Kong company for the convenience of the buyers. That case is therefore distinguishable.

Accordingly this appeal is dismissed.