Subsection (2) falls well within the words in 14A, "... the offence is declared to be ... punishable either on summary conviction or on indictment, the offence shall be triable either on indictment or summarily". Mr McCoy advanced to us an argument, albeit faintly, that since each of the summonses alleged the offences to be contrary to s.3(1)(a) and s.3(2)(b) those offences must be summary ones. The answer to that is that the manner of trial does not determine the category of the offence.

There is no time limit generally imposed for the prosecution of indictable offences. Given that s.3 of the LFBTO creates an indictable offence the answer to the second certified question depends entirely upon the proper construction of s.67 of the same Ordinance. It begins with the words, "Notwithstanding s.26 of the Magistrates Ordinance ...". That section deals exclusively with offences other than indictable offences which are mentioned only to remove them from its ambit. That being so, the opening words of s.67 show that it, also, is dealing with offences other than indictable offences. It is also to be noted that it appears to have been the policy of the legislature to extend the time for prosecutions under the LFBTO having regard to the complexities usually involved. Any construction of s.67 that it includes both summary and indictable offences necessarily means that a time limit has been introduced to the more serious offences fit to be tried on indictment, which will presumably be even more complex, when none existed before. It would also mean that the gravity of cases fit to be tried summarily and those fit to be tried upon indictment has been equated. That construction cannot be accepted. The Judge was right in her conclusion.

The first question certified must be answered in favour of the appellants and the appeal is upheld on that ground with costs both here and upon their application on motion to the Judge in the Court of First Instance. They fail on the second question certified but, on the basis that the motion should have been granted and that the case stated should never have been heard, they will also have their costs on the case stated. They have not sought an order for their costs in the Magistracy and none is ordered.

Nazareth NPJ:
I agree with the judgment of Mr Justice Ching PJ.

Lord Hoffmann NPJ:
I agree.

Li CJ:
The Court unanimously allows the appeal with costs both in this appeal and in the proceedings before the Court of First Instance.

Commissioner of Inland Revenue
and
Emerson Radio Corp

Li CJ, Litton and Ching PJJ and Nazareth and Lord Hoffmann NPJJ
Final Appeal Nos 3 and 6 of 1999 (Civil) (Consolidated)
23 November and 14 December 1999

Taxation — profits tax — royalties derived from use of trade mark — application of trade mark to goods manufactured both in and outside Hong Kong but only sold outside Hong Kong — whether royalty payments were sums received for use of trade mark in Hong Kong under s.15(1)(b) of Inland Revenue Ordinance (Cap.112)

Intellectual property — trade marks — taxation — royalties derived from use of trade mark
[Inland Revenue Ordinance (Cap.112) s.15(1)(b); Trade Marks Ordinance (Cap.43) s.39]

The respondent, an American corporation, received royalties from its Hong Kong subsidiary, X, for the use of the respondent's trade mark on goods manufactured within and outside Hong Kong but only sold outside Hong Kong. The Commissioner of Inland Revenue considered that, in accordance with s.15(1)(b) of the Inland Revenue Ordinance (Cap.112), the royalties were for the use of the trade mark in Hong Kong and assessed the respondent to profits tax on the royalty income. The respondent, however, contended that the royalties were not assessable as profits derived in Hong Kong. On appeal, the Board of Review upheld the assessment. The Court of First Instance held that only those royalties for goods manufactured in Hong Kong constituted use of the trade mark in Hong Kong and ordered an apportionment of the amounts paid (see [1999] 1 HKLRD 250). The Court of Appeal upheld this view (see [1999] 2 HKLRD 671). The Commissioner appealed, arguing that all the royalties were taxable, whether or not the goods had been manufactured in Hong Kong. The respondent cross-appealed. It conceded (the concession) that there was an implied term in the royalty agreement giving X the right to use the respondent's trade mark registered in countries other than the US, in particular in Hong Kong. However, it argued that the royalty income was for the actual use of the trade mark, namely the right to sell the goods bearing the mark, and there had been no sales in Hong Kong.

Held, unanimously dismissing both the appeal and the cross-appeal (Lord Hoffman NPJ giving the leading judgment), that:

(1) As a matter of construction, the express terms of the agreement dealt only with the US registered trade mark. However, on the basis of the concession, the royalty was received for the use of the mark in Hong Kong as well as

in the US. If the goods were manufactured in Hong Kong, the mark would be applied to the goods in Hong Kong. By s.39 of the Trade Marks Ordinance (Cap.43), the application of a mark in Hong Kong to goods to be exported from Hong Kong was deemed to constitute use of that mark. (See pp.506B–H, 508A–B.)

(2) The consideration for such use was referable to the royalties paid for sales in the US since this was how the royalties were calculated. In the absence of some form of apportionment between the use of a mark in and outside Hong Kong, the requirement of s.15(1)(b) in respect of goods manufactured in Hong Kong was satisfied. Conversely, the royalties referable to sales in respect of goods manufactured outside Hong Kong were not liable to profits tax under s.15(1)(b). (See pp.508B, 508H–509E.)

(3) (*Obiter*) The rights conferred by registration of trade marks were territorial so that rights in respect of products sold in the US must be rights under the US registered trade mark. It was unnecessary to imply the right to use the respondent's mark registered in countries outside the US into the royalty agreement since X already enjoyed those rights under wider agreements with the respondent. Nor would such a term have been implied by the court as a matter of necessity (*Liverpool City Council v Irwin* [1977] AC 239 applied). (See pp.506C–E, 507E–F.)

(4) (*Obiter*) If one disregarded the concession, as a matter of law and construction the agreement licensed only the US mark. Given the territoriality of the rights conferred by a trade mark, it was not possible for any of those rights to be used in Hong Kong. If none of the royalties were received or accrued for the use of a trade mark in Hong Kong, no tax would have been payable. (See p.507F–J.)

(5) (*Per* Litton PJ, disagreeing as to the construction of the agreement) Construing the agreement, it was implied that the fees were not only for the use of the US registered trade mark in the US but also for its use in those countries in which the goods were manufactured. Hence, part of the sums received by way of fees were sums received for the use in Hong Kong of a trade mark in terms of s.15(1)(b). (See p.504E–G.)

[Chinese translation of headnote.]

課稅——利得稅——得自使用商標的使用費——就香港以內及以外製造但只在香港以外出售的貨品使用商標——使用費是否在《稅務條例》(第 112 章)第 15(1)(b) 條下在香港內使用商標所收取的款項

知識產權——商標——課稅——來自使用商標的使用費
[《稅務條例》(第 112 章) 第 15(1)(b) 條；《商標條例》(第 43 章) 第 39 條]

答辯人為一美國公司，收取由香港的附屬公司 X 的專利費用。附屬公司使用答辯人的商標於香港境內外生產貨物上，而貨物只會在香港境外銷售。稅務局長認為，根據《稅務條例》(第 112 章) 第 15(1)(b) 條，專利費用的收取是由於在香港使用商標，並對答辯人就專利費用的收入作利得稅評估。答辯人則辯稱專利費用不應以源於香港來評估。上訴時，稅務上訴委員會維持需評估的決定。原訟法院的決定為祇是在香港境內生產的貨物，即構成在香港境內使用商標，並命令將已繳金額分攤。(見 [1999] 1 HKLRD 250)。上訴法庭採取相同觀點，(見 [1999] 2 HKLRD 671)。稅務局局長上訴，不論貨物是否香港境內製造，所有專利費用均需課稅。答辯人亦作交相上訴。答辯人接納專利協議內含一隱含條款，賦予 X 有權力除在美國以外在別的註冊國家使用答辯人的商標，特別是用於香港。但卻爭辯專利費用是實質使用商標，即銷售蓋上商標貨物的權利，但貨物並沒有在香港銷售。

裁決——一致裁定駁回上訴及交相上訴 (Lord Hoffman NPJ 下首席判決書)

(1) 就詮釋而言，協議的明訂條款涉及美國註明的商標。不過從特惠的基礎上看專利費用的收取是在香港及美國使用商標。倘若在香港製造貨物，商標便在香港蓋在貨物上。根據《商標條例》(第 43 章) 第 39 條，在香港將商標蓋在貨物上，然後從香港出口則當作為使用該商標。(見 506B–H，508A–B 頁)

(2) 使用該商標的約因是參照在美國的銷售是而支付的專利費用，亦是專利費用的釐定方法。在沒有任何形式來劃分在香港境內及境外使用商標，便符合第 15(1)(b) 在香港製造貨物。相反地，那些就有關非在香港境內所製造的貨物而收取的專利費用則無需根據第 15(1)(b) 課稅。(見 508B，508H–509E 頁)

(3) (附言) 因註冊商標所賦予的權力是地域性的，所以可在美國銷售貨物的權力必定是來自在美國已註冊商標的權力。由于 X 根據與答辯人達成的其他廣義性的協議，已享有答辯人在美國以外其他與註冊國家的商標使用權，故此毋須以隱含條款的方式來引進到該專利費協議。亦無需由法院以必需的原則引進該條款 (援引 *Liverpool City Council v Irwin* [1977] AC 239)。(見 506C–E，507E–F 頁)

(4) (附言) 在撤除該等優惠，在法律上及在詮釋上，該協議只特許美國商標。基於商標只賦予地域性的權力，該等權力是無法在香港使用的。倘若專利費用的收取或產生並非是於香港使用商標，便毋需支付稅款。(見 507F–J 頁)

(5) (Litton PJ 對協議的詮釋表示不贊同)
詮釋協議時，應引申為該等費用不單是在美國使用美國註冊的商標，而亦是貨物生產國使用商標。因此，部份款額的收取是於香港使用商標，即符合第 15(1)(b)。(見 504E–G 頁)

Mr Robert Kotewall SC and Mr Joseph Fok SC, instructed by the Department of Justice, for the appellant.
Mr Barrie Barlow, instructed by Baker & McKenzie, for the respondent.

Legislation mentioned in the judgment:
Inland Revenue Ordinance (Cap.112) ss.14(1), 15(1), (1)(b)
Trade Marks Ordinance (Cap.43) s.39
Trade Marks Act 1938 [Eng] s.31

Case cited in the judgment:
Liverpool City Council v Irwin [1977] AC 239

Li CJ:
I agree with the judgment of Lord Hoffmann.

Litton PJ:
I have had the advantage of reading in draft Lord Hoffmann NPJ's judgment. The background facts are fully set out in his judgment and need not be repeated here.

The royalty agreement in essence says two things: (1) The Hong Kong company wishes to continue to sell products carrying the trade mark "Emerson" to customers in the USA and (2) it agrees to pay fees to the US company for the use of the trade mark on those products, calculated as a percentage of the sales price.

On its face this agreement relates to the use of the US registered trade mark, as applied to goods sold in the USA. It says nothing about the use in Hong Kong of the trade mark registered here. But, in order that the Hong Kong company should be able to sell those goods to customers in the USA they have to be manufactured: It is common ground that, at the time of the royalty agreement, goods were manufactured in Hong Kong and in other parts of Asia on the Hong Kong company's order. These goods bearing the "Emerson" trade mark were shipped direct by the manufacturers to the customers in the USA. This is the context in which the words in the royalty agreement "[The Hong Kong company] *wishes* to *continue* to sell ... etc" were used. Inevitably, as part of the arrangement under which the fees were paid, the Hong Kong company used the "Emerson" trade mark in placing orders for the manufacture of the goods. Construing the agreement in this context it seems right to say that, by implication, it was a term of the royalty agreement that the fees were not only for the use of the US registered trade mark in the USA but also for the use of the trade mark in those countries where the goods were manufactured. The concession on this matter by Counsel for the taxpayer in the lower courts, and before us, makes it unarguable.

Once this point is reached, the conclusion is inevitable that part of the sums received by way of fees were sums *received for the use in Hong Kong of a trade mark*, in terms of s.15(1)(b) of the Inland Revenue Ordinance.

The Recorder, on appeal from the Board of Review, took a robust approach. He held that part of the fees were subject to the charge: That is, the fees received or accrued in relation to the sale of goods manufactured in Hong Kong: This, he was told by Counsel, presented no practical difficulty. It was, in fact, the "fall back" position adopted by both parties. The Recorder did not engage in any further refinement of the issue and ask himself whether, in relation to *those* goods (manufactured in Hong Kong and sold to customers in the USA), there had to be a *further* apportionment of the fees to distinguish between the use of the Hong Kong registered mark and the US registered mark. Rightly so, as this would have been a virtually impossible exercise.

In my view the Recorder had reached the right conclusion on the questions posed in the Stated Case and the majority of the Court of Appeal were also right to uphold his judgment.

Ching PJ:
I agree with the judgments of Litton PJ and Lord Hoffmann NPJ.

Nazareth NPJ:
I agree with Lord Hoffmann's judgment.

Lord Hoffmann NPJ:
Emerson Radio Corporation (Emerson) is an American corporation which manufactures and sells electronic equipment. It is the registered proprietor of trade marks consisting of the name "Emerson" in the United States, Hong Kong and many other countries. It has a wholly- owned subsidiary in Hong Kong called Emerson Radio (Hong Kong) Ltd (Emerson HK). Emerson HK contracts with manufacturers in various Asian countries, including Hong Kong, for the manufacture of electronic equipment which it exports mainly to the United States but also to other places. It does not however sell any goods in Hong Kong.

On 1 April 1984 Emerson entered into a "royalty agreement" with Emerson HK. The following are the relevant terms:

> 1. Emerson holds the rights for the use of the trade mark "Emerson" for electronic home entertainment products sold in the United States of America (US). Emerson HK wishes to continue to sell "Emerson" brand products to customers with locations in the US.
> 2. Emerson HK agrees to pay Emerson for the use of the "Emerson" trade mark on products it sells to its US customers ..."

There followed provisions concerning the amount and payment of a royalty on sales. The agreement was expressed to be governed by the law of New York. On 1 April 1987 the parties entered into a new agreement in identical terms save for an increase in the rate of royalty.

The Commissioner of Inland Revenue assessed Emerson to profits tax on its royalty income. In principle, profits tax is chargeable only on persons "carrying on a trade, profession or business in Hong Kong in respect of ... assessable profits arising in or derived from Hong Kong": see s.14(1) of the Inland Revenue Ordinance (Cap.112). Emerson does not carry on any business in Hong Kong. But by s.15(1), certain receipts are deemed to be "arising in or derived in Hong Kong from a trade, profession or business carried on in Hong Kong." They include, under para.(b):

> Sums ... received by or accrued to a person for the use of or right to use in Hong Kong ... a trade mark ...

The Commissioner said that the royalties were for the use of a trade mark in Hong Kong. The Board of Review upheld the assessment. On an appeal to the Court of First Instance by way of case stated, Mr Recorder Ribeiro SC (as he then was) held that only those royalties payable for goods manufactured in

Hong Kong (where the mark would have been applied) were for the use of the mark in Hong Kong. A majority of the Court of Appeal (Mortimer V-P and Rogers JA) agreed. Godfrey JA dissented, holding that none of the royalties were for the use of the mark in Hong Kong. The Commissioner has appealed, seeking to restore the decision of the Board of Review that all the royalties were taxable, whether the goods had been made in Hong Kong or not. Emerson has cross-appealed, seeking to uphold the judgment of Godfrey JA.

I shall deal first with the cross-appeal. In the Court of Appeal, Rogers JA said that as a matter of construction of the express terms of the royalty agreement, it dealt only with the United States registered trade mark. In my opinion, that was right. It is apparent from the recital in cl.1: "Emerson holds the rights for the use of the trade mark "Emerson" for electronic home entertainment products sold in the United States of America (US)." The rights conferred by the registration of trade marks are territorial. A trade mark registered in the United States enables the holder to complain of infringing acts in the United States but not elsewhere. To complain of infringing acts in Hong Kong, one must have a mark registered in Hong Kong. So the rights in respect of products sold in the United States must be rights under the United States registered mark. Therefore, in cl.2, when it is said that "Emerson HK agrees to pay Emerson for the use of the "Emerson" trade mark on products it sells to its US customers ...", the "Emerson trade mark" must mean the US registered trade mark. Trade marks registered elsewhere in respect of the same mark would be irrelevant to the sale of products to US customers.

In the Court of Appeal, however, Mr Barlow (for Emerson) conceded that it was an implied term of agreement that it also included the right to use the Emerson mark registered in other countries, and in particular in Hong Kong, if it was necessary to use the mark there for the purpose of manufacturing goods to be sold in the United States. If the goods are manufactured in Hong Kong, the mark will be applied to the goods in Hong Kong. By s.39 of the Trade Marks Ordinance (Cap.43), reproducing the effect of s.31 of the UK Trade Marks Act 1938, the application of a mark in Hong Kong to goods to be exported from Hong Kong is deemed to constitute use of that mark. Emerson HK did not manufacture anything itself. It contracted with independent manufacturers to do so. But they would apply the Emerson mark by direction of Emerson HK and it was not suggested that the use of third parties made any difference to the question of whether Emerson HK could be said to be using the Hong Kong registered mark in Hong Kong.

I should say that, speaking entirely for myself, I am not confident that Mr Barlow's concession of an implied term was correct. If Emerson and Emerson HK had simply been parties dealing at arms' length, I would have had no doubt that a licence to use the mark in the course of manufacture should be implied. It would be absurd for Emerson, having licensed the use of the US mark for exports to the US, then to be able to complain that the manufacture of the goods in Hong Kong was an infringement. But Emerson HK was a wholly-owned subsidiary of Emerson and there had clearly been other arrangements by which it was expressly or impliedly allowed to use the Emerson marks both

before and after the conclusion of the royalty agreement in 1984. The Case Stated mentions another agreement under which Emerson provided services to Emerson HK in return for a fee. These included "the promotion of the brand name" and one would therefore expect that, expressly or impliedly, that agreement gave Emerson HK the right to use the brand name. Clause 1 of the royalty agreement in 1984 recites that Emerson HK wished to "continue to sell 'Emerson' brand products to customers with locations in the US", which suggests that they had previously been doing so without paying a royalty. And the royalty agreement plainly did not impliedly authorise the use of the Emerson mark in other countries to which goods were exported. So the use of these marks in those countries must have been licensed under some other express or implied arrangements. There are accordingly grounds for supposing that it would have been unnecessary to imply into the royalty agreements any licence to use the Hong Kong or other non-US marks because Emerson HK already enjoyed those rights under the wider arrangements between the parties. The royalty agreements were what they purported on their face to be, namely a payment for the use of the Emerson mark in its principal market, the United States. This would be confirmed by the letter which Emerson wrote to Emerson HK on 11 July 1991, asking for an increase in the royalty rate. It said that "The value of the Emerson name *in the US* and the maintenance of that name *in the US* has seen a substantial cost increase since the last amendment." (Emphasis added.)

The test for the implication of a term into a written agreement is, as Lord Wilberforce said in *Liverpool City Council v Irwin* [1977] AC 239 at pp.253–4, one of necessity. A term will be implied only if it is necessary to make the contract work. I have considerable doubt as to whether, on the facts as found in the Case Stated, this test was satisfied. There is evidence to suggest that, by virtue of other subsisting understandings between the parties, the royalty agreement would have worked perfectly well without such an implication.

If no such implied term in question had existed, I would have agreed with Godfrey JA that none of the royalties were received or accrued for the use of a trade mark in Hong Kong. The agreement licensed only the US mark and, given the territoriality of the rights conferred by a trade mark, it was not possible for any of those rights to be used in Hong Kong. Mr Kotewall SC, who appeared for the Commissioner, said that it did not matter that the agreement did not license the use of the Hong Kong registered mark. One must look at what was actually done, which was that Emerson HK did use the Hong Kong mark. I do not agree. The question is whether the royalties were received "for" the use of the mark in Hong Kong. If the payments were wholly for the use of the US mark, then nothing was received for the use of the mark in Hong Kong. Of course in deciding whether the royalties were for the use of the Hong Kong mark, one looks at the realities of the situation. The Commissioner is not bound by the language used by the parties. But if the reality was that Emerson HK, as a wholly-owned subsidiary, was allowed to use the Hong Kong mark for nothing, or that the right to use that and other marks (excluding the US) was covered by the fee paid under the service agreement, then in my view no tax would have been payable on the royalties.

Mr Barlow however was firm in his concession before this Court, as in the Court of Appeal, that this appeal should be decided upon the footing that the royalty agreement impliedly licensed the use of the Hong Kong mark. Accordingly, that is how I think it should be decided. And on that basis, I do not see how it can be said that the royalty was not received for the use of a trade mark in Hong Kong. True, it was for something else as well, namely the use of a mark in the United States. But, in the absence of some form of apportionment, the requirement of s.15(1)(b) in respect of royalties paid on goods manufactured in Hong Kong is satisfied.

Mr Barlow said that royalties were charged only on goods sold to customers in the United States. Without such sales, no royalties would be payable. Therefore all that Emerson HK was paying for was the right to sell in the United States. It was not paying for the right to use the mark in Hong Kong. This seems to me a *non sequitur*. Once one says that it was an implied term of the agreement that Emerson HK should be able to use the Hong Kong mark, one has to identify the consideration for that term. And the only possible consideration is the royalty.

Mr Barlow submitted that the Hong Kong legislature, at the time when s.15(1)(b) was enacted, had no constitutional power to impose taxation upon events which occurred outside Hong Kong, such as the sale of goods to customers in the United States. Therefore the section should not be construed as having this effect. But that, as it seems to me, begs the question which I have just been considering. It is true that a sale in the United States was necessary before the royalty became payable and that it was calculated on the sale price. But that was not the basis on which the tax was imposed. It was charged because the royalty was also for the use of the trade mark within this jurisdiction.

Mr Barlow criticised a passage in the judgment of Mr Recorder Ribeiro SC in which he said that use of the trade mark in Hong Kong which "forms an essential step" in the process by which royalty was earned was sufficient to bring it within the charge under s.15(1)(b). Mr Barlow said that the concept of an "essential step" was relevant to locating the source of income for the purposes of a charge under s.14 but had no part to play in the application of s.15(1)(b). In my opinion, if one reads the whole paragraph, the Recorder was saying only that the royalties were taxable because they were received for the use of a trade mark in Hong Kong and it did not matter that they were also received for the use of a trade mark in the United States. That seems to me a correct analysis.

I would therefore dismiss the cross-appeal.

I turn then to the Commissioner's appeal. Mr Kotewall put the point in various ways. First, he said that by authorising manufacturers outside Hong Kong (say, in Thailand) to apply the Emerson mark, Emerson HK was using the mark and since it was carrying on business in Hong Kong, it was using it in Hong Kong. In my view that ignores the territoriality of each mark. In authorising the use of the mark in Thailand, Emerson HK was using the Thai mark and the only place where the Thai mark could be used was Thailand. Secondly, Mr Kotewall said that by licensing Emerson HK to use the mark in Hong Kong and elsewhere, Emerson was itself using the mark (wherever

registered) in Hong Kong. I think that this argument fails for the same reason as the first one and for the additional reason that s.15(1)(b) does not apply to income received by Emerson *from* its own use of the mark in Hong Kong (which would be taxable, if at all, under s.14), but *for*, ie in return for, the use of or right to use the mark in Hong Kong. This implies that the use is by, or the right to use has been conferred upon, someone else. Thirdly, Mr Kotewall said that the royalties were for the *right to use* the mark anywhere. If Emerson HK chose to use the mark in Hong Kong, that was its business. The royalty was for the right to use the mark wherever registered. There was some discussion about whether the Commissioner was entitled to raise a question based upon the royalties being received for the right to use the mark as opposed to for its use. It was not included in the questions of law stated for the court by the Board of Review. The Recorder was willing to entertain it but Mr Barlow said that he had no jurisdiction to do so. I prefer to express no view on this disputed point because it seems to me that the question is entirely academic. The royalty agreement contemplated that the royalties would be paid on goods which had been made and sold; that is, in respect of which the mark had actually been used. And in any case, the argument breaks down at the same point as the submissions on the actual use of the mark, namely that the right to use a Thai trade mark can be exercised only in Thailand and not in Hong Kong. I would therefore dismiss the appeal as well.

Li CJ:

The Court unanimously dismisses the appeal and also the cross-appeal. The Court makes an order *nisi* that there be no order as to costs. Such order will become absolute unless any party makes written submissions copied to the other side within 14 days.