

**ING Baring Securities (Hong Kong) Limited [formerly known
as Baring Securities (Hong Kong) Limited and presently
known as Macquarie Securities Limited]** *(Appellant)*

and

The Commissioner of Inland Revenue *(Respondent)*

**Court of First Instance
(Inland Revenue Appeal No. 1 of 2003)**

**Hon Barma J
Dates of Hearing : 6-11 October 2003
Date of Judgment : 1 June 2005**

**Court of Appeal
(Civil Appeal No. 202 of 2005)**

**Hon Rogers VP, Le Pichon JA and Stone J
Dates of Hearing : 6-7 June 2006
Date of Judgment : 7 June 2006
Date of Handing Down Reasons for Judgment: 20 June 2006**

**Court of Final Appeal
(Final Appeal No. 19 of 2006 (Civil))**

**Mr Justice Bokhary PJ, Mr Justice Chan PJ, Mr Justice
Ribeiro PJ, Mr Justice Nazareth NPJ and Lord Millett NPJ
Dates of Hearing: 3, 4 and 15 May 2007
Date of Judgment : 5 October 2007**

Inland Revenue Ordinance (Cap. 112) – Profits Tax – whether profits derived directly or indirectly from transactions in securities traded or intended to be traded on stock exchanges outside Hong Kong arose in or were derived from Hong Kong and chargeable to profits tax under section 14.

The Taxpayer was incorporated in Hong Kong in 1984. It carried on the business of agency brokerage in Hong Kong as a member of a multinational group of companies which carried on a global business in many different countries. At all material times it was a wholly owned subsidiary of Baring Securities Ltd, itself a wholly owned subsidiary of Baring Brothers & Co Ltd which was a long established merchant bank in London. Baring Securities Ltd and its subsidiaries formed the group's securities trading arm.

The Baring group carried on an agency business, namely to act exclusively for clients and earned commission by carrying out their instructions. The Taxpayer acted for clients in Hong Kong; it also acted on the instructions of the Baring group given on behalf of clients outside Hong Kong. The Taxpayer claims that profits from transactions on foreign markets fell outside the charge to profits tax. The Taxpayer divided the disputed profits into three categories:

- (a) Commission income – represented the net commission retained by the Taxpayer after deducting commission paid.
- (b) Placement income – represented commission earned from allotment, on behalf of client, of new shares issued or listed outside Hong Kong.
- (c) Marketing income – in most cases simply represented an introductory commission received from overseas subsidiaries for the introduction of clients.

The Board of Review dismissed the appeal on the Taxpayer's failure of discharging the onus of proving that the determination appealed against is excessive or incorrect.

The Taxpayer appealed to the Court of First Instance. The Court of First Instance allowed the appeal holding that the profits neither arising in nor derived from Hong Kong.

The Commissioner appealed to the Court of Appeal. The Court of Appeal allowed the appeal and upheld the Board's decision. The Taxpayer appealed to the Court of Final Appeal.

Held by the Court of Final Appeal, allowing the appeal, that:

- (1) The question of source of profits is a hard practical matter of fact to be judged as a practical reality. It is, in other words, not a technical matter but a commercial one.
- (2) The broad guiding principle, attested by many authorities, is that one looks to see what the taxpayer has done in earning the profits in question and where he has done it. It is necessary to consider the nature of the different transactions by which the profits are generated.
- (3) The focus is on effective causes without being distracted by antecedent or incidental matters.
- (4) The source of profits must be attributed to the operations of the taxpayer which produced them and not to the operations of other members of the group. The relevant operations do not comprise the whole of the taxpayer's operations but only those which produce the profit in question.
- (5) Where the taxpayer employs others to act for him in carrying out a transaction for a client, his profit is earned in the place where they carry out his instructions whether they do so as agents or principals. It is not necessary for the taxpayer to establish that the transaction which produced the profit was carried out by him or his agent in the full legal sense. It is sufficient that it was carried out on his behalf and for his account by a person acting on his instructions. Nor does it matter whether the taxpayer was acting on his own account with a view to profit or for the account of a client in return for a commission.
- (6) The Court concluded that where a broker carrying on business in Hong Kong receives profits in the form of commission or analogous income earned only upon the successful execution of a securities transaction he has caused to be effected on his client's behalf in a securities market outside Hong Kong, it is that offshore trading transaction which ought to be regarded as the relevant profit-generating transaction on his part so that the resultant profits neither arising in nor derived from Hong Kong.

In the Court of First Instance

Mr Barrie Barlow (instructed by Messrs Kwok & Yih) for the appellant

Ms Gladys Li SC (instructed by the Department of Justice) for the respondent

In the Court of Appeal

Mr Barrie Barlow (instructed by Messrs Mallesons Stephen Jaques) for the appellant

Ms Gladys Li SC (instructed by the Department of Justice) for the respondent

In the Court of Final Appeal

Mr David Goy QC and Mr Barrie Barlow SC (instructed by Messrs Mallesons Stephen Jaques) for the appellant

Ms Gladys Li SC (instructed by the Department of Justice) for the respondent

Cases referred to in the judgment of the Court of Final Appeal:

Commissioner of Income Tax, Bombay Presidency and Aden v Chunilal B Mehta of Bombay (1938) LR 65 Indian Appeals 332

Commissioner of Income Tax, Bombay Presidency and Aden v Chunilal B Mehta of Bombay 1935 AIR Bombay 423

Commissioner of Inland Revenue v HK-TVB International Ltd [1992] 2 AC 397, [1992] 3 WLR 439

Commissioner of Inland Revenue v Hang Seng Bank Ltd [1991] 1 AC 306

Commissioner of Inland Revenue v Orion Caribbean Ltd [1997] HKLRD 924

Commissioner of Inland Revenue v Wardley Investment Services (HK) Ltd (1992) 3 HKTC 703

FL Smidth & Co v Greenwood (Surveyor of Taxes) [1921] 3 KB 583

ING Baring Securities (Hong Kong) Ltd v Commissioner of Inland Revenue [2006] 2 HKLRD 6

ING Baring Securities (Hong Kong) Ltd v Commissioner of Inland Revenue [2006] 3 HKLRD 315

Kennedy v De Trafford & Others [1897] AC 180

Kim Eng Securities (Hong Kong) Ltd v Commissioner of Inland Revenue [2007] 2 HKLRD 117

Kwong Mile Services Ltd v Commissioner of Inland Revenue (2004) 7 HKCFAR 275