

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D25/94

Salaries tax – source of income.

Panel: Denis Chang Khen Lee QC (chairman), Vincent Lo Wing Sang and Eric Lo King Chiu.

Date of hearing: 9 March 1994.

Date of decision: 12 July 1994

The taxpayer claimed that he was employed outside of Hong Kong and accordingly that his income should not be taxed as Hong Kong source income.

Held:

The Board found as a fact that the taxpayer was employed in Hong Kong and that the source of his income was accordingly a Hong Kong source. As obiter dicta the Board commented that it was not of the opinion that the case of CIR v Goepfert [1987] 2 HKTC 210 had been overruled by the Hang Seng Bank case [1990] 3 HKTC 351.

Appeal dismissed.

Cases referred to:

CIR v Goepfert [1987] 2 HKTC 210

CIR v Hang Seng Bank Ltd [1990] 3 HKTC 351

Chan Wai Mi for the Commissioner of Inland Revenue.

Taxpayer in person.

Decision:

1. The Taxpayer has objected to his 1990/91 salaries tax assessment on the ground that part of his income was derived from services rendered outside Hong Kong. The Taxpayer's case is that he should pay tax only in respect of the services which he rendered in Hong Kong, that is, on a 'days-in-days-out' basis.

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2. In his 1990/91 salaries tax return the Taxpayer reported that he was employed by Company A (Far East) Ltd as a 'consultant' from 1 April 1990 to 31 March 1991 and that he received during the period \$387,160 by way of salaries/wages plus \$93,544 by way of 'commission'.

3. Subsequently the Taxpayer contended, and has maintained in his evidence, that he was employed not by Company A (Far East) Ltd, a Hong Kong company, but by its parent company Company A (USA) Inc.

SALIENT FACTS

4. On the evidence before us we find the following facts.

5. Company A (USA) Inc, the parent company of Company A (Far East) Ltd, was at all material times engaged principally in selling and servicing high-technology equipment. Its Head Office was in USA.

6. Company A (Far East) Ltd was incorporated in Hong Kong on 20 August 1985. Based in Hong Kong it was principally engaged in providing technical support to customers of Company A in the Asia-Pacific Region, including China and Hong Kong. Company A (Far East) Ltd operated from rented premises in Hong Kong and did not have any branch office outside the territory.

7. By 'customers of Company A' we refer to dealers who had purchased equipment for resale from Company A (USA) Inc and, since 1990, also from Company A (Far East) Ltd as well as to end-users of Company A equipment throughout the Asia-Pacific Region.

8. At the time when the Taxpayer received the offer of employment referred to below he was working in Hong Kong with Company B as a manager. He had previously worked as an engineer in Company C.

9. Around April or May 1989 one Mr X, managing director of Company A (Far East) Ltd (who was formerly a colleague of his in Company C) negotiated with the Taxpayer the terms of his employment as consultant with Company A (Far East) Ltd. The negotiations were held in Hong Kong although the Taxpayer also talked over the phone to a Mr Y of Company A (USA) Inc.

10. Pursuant to the negotiations a letter dated 13 June 1989 on Company A (USA) Inc notepaper was addressed to and received by the Taxpayer in Hong Kong setting out terms of employment. Accompanying the letter was an 'Employee Non-Disclosure Statement' the opening words of which read: 'This is to confirm the conditions of your employment with Company A (Far East) Ltd as follows: ...'

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11. The said 'Employee Non-Disclosure Statement' was signed by the Taxpayer in Hong Kong on 15 June 1989. The Taxpayer also on the same day countersigned the said letter of 13 June 1989 and faxed the countersigned letter to Company A (USA) Inc.

12. The Taxpayer commenced work as a consultant as from 17 July 1989. By a letter dated 23 May 1991 to the Revenue the said Mr X as managing director of Company A (Far East) Ltd confirmed that the Taxpayer was thus employed by Company A (Far East) Ltd as consultant 'to provide high-level support' to their customers in Asia-Pacific and that his job included frequent travelling outside Hong Kong to perform his duties in the region and to attend 'training sessions'.

13. For the period from 1 April 1990 to 31 March 1991 (both dates inclusive) the Taxpayer, as part of his job, spent an aggregate of 134 days outside the territory. During this period he visited customers of Company A in South Korea, Japan, Singapore, Taiwan, Thailand and Indonesia. Most trips lasted around three to four days each but some were for eight to thirteen days. From 26 February 1991 to 27 March 1991 he was away from Hong Kong; during those 30 days he spent time attending training sessions with the parent company in the States.

14. The Taxpayer's salaries were in Hong Kong currency and wholly paid by Company A (Far East) Ltd in Hong Kong. Company A (Far East) Ltd in its tax returns to the Revenue made deductions in respect of the salaries paid when computing its assessable profits. In the Employer's Return filed by Company A (Far East) Ltd in respect of the Taxpayer's income for the year ended 31 March 1990 no part of the salaries was stated as having been paid by the parent company as 'an overseas concern' in the space reserved for the purpose.

15. When the Taxpayer first joined Company A (Far East) Ltd the company had a staff of some 9 or 10 people working from rented premises of some 1,200 square feet in Wanchai (compared with about 65 people as at the date of the hearing, with some 6,000 square feet of office accommodation).

16. Company A (Far East) Ltd's managing director, based in Hong Kong, was and remained the Taxpayer's superior. There was at first no support manager employed by Company A (Far East) Ltd but one was recruited towards the end of 1990 and became the Taxpayer's immediate superior [NB.: The Taxpayer as at the date of the hearing occupied the position of support manager; the Company A group had now been taken over by Company D; Company A (Far East) Ltd's name had been changed to Company D (Far East) Ltd].

17. The Taxpayer was assigned by Company A (Far East) Ltd to service what he described as 'carrier-type customers' - meaning carrier communication organisations. During some two-thirds of the year the Taxpayer would remain in Hong Kong servicing customers here. He would also where possible without leaving Hong Kong answer technical queries received from customers in other parts of the Asia-Pacific Region. He

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would not 'escalate' these queries to Company A (USA) Inc unless the technical staff of Company A (Far East) Ltd in Hong Kong was unable to deal with them.

SOURCE OF INCOME

18. We have no difficulty in rejecting the Taxpayer's contention that he was employed not by Company A (Far East) but by the parent company. This contention, made in his letter to the Inland Revenue Department dated 26 November 1991 and repeated in his evidence, was in our view very much a self-serving afterthought. We likewise rejected the assertions made in Company D (Far East) Ltd letter dated 26 April 1992 to the same effect. These assertions were quite inconsistent with the facts and contradicted what Company A (Far East) Ltd itself had earlier stated by letter and in the Employer's Returns.

19. On the whole of the evidence we find as facts that the Taxpayer was recruited and engaged in Hong Kong by and to work for Company A (Far East) Ltd, was accountable to the management of the company in Hong Kong, was based in the territory and was remunerated by Company A (Far East) Ltd in Hong Kong under a single indivisible contract of employment effectively concluded in Hong Kong.

20. The basic charge to salaries tax is contained in section 8(1) of the Ordinance and is, subject to the provisions of the Ordinance, levied 'on every person in respect of his income arising in or derived from Hong Kong from the following sources: (a) any office or employment of profit ...'

21. Section 8(1A) provides that for present purposes 'income arising in or derived from Hong Kong from any employment (a) includes, without in any way limiting the meaning of the expression and subject to paragraph (b), all income derived from services rendered in Hong Kong including leave pay attributable to such services; and (b) excludes income derived from services rendered by a person who: (i) is not employed by the Government or as master or member of the crew of a ship or as commander or member of the crew of an aircraft; and (ii) renders outside Hong Kong all the services in connection with his employment.'

22. Section 8(1B) provides that in determining whether or not all services are rendered outside Hong Kong for the purposes of subsection (1A) no account shall be taken of services rendered in the Colony during visits not exceeding a total of 60 days in the basis period for the year of assessment.

23. Quite clearly the present case does not fall within the exclusionary provisions of section 8(1A) and (1B). Since the inclusionary provision of section 8(1 A) is expressly stated to be without in any way limiting the meaning of the expression 'income arising in or derived from Hong Kong from any employment' the bringing into the charge of 'all income derived from services rendered in Hong Kong' does not mean that income derived from services rendered outside Hong Kong is necessarily outside the scope of the charge or indeed that the location where services are rendered is necessarily relevant to a

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consideration as to whether the income was derived from Hong Kong from any employment for the purposes of the basic charge under section 8(1).

24. The High Court in CIR v Goepfert [1987] 2 HKTC 210 has held that although section 8(1) must be construed in the light of and in conjunction with section 8(1 A), section 8(1A)(a) creates a liability to tax additional to that which arises under section 8(1). It has also held that ‘the place where the services are rendered is not relevant to the enquiry under section 8(1) as to whether income arises in or is derived from Hong Kong from any employment’ and ‘should therefore be completely ignored’.

25. The Goepfert decision was delivered on 10 April 1987, in other words a few years before the Privy Council delivered judgment on 8 October 1990 in the Hang Seng Bank case [1990] 3 HKTC 351. We have not had the benefit of full argument on whether the Hang Seng Bank case - which concerned a different charging section, namely section 14 (profit tax) - has any bearing on the issue before us, in particular on the possibility of apportionment. There is, however, a commentary in the Hong Kong Law Journal (HKLJ) [1992] at 319 et seq. which suggests that Goepfert has effectively been undermined by the reasoning in the Hang Seng Bank case.

26. We are not, however, persuaded that this is so. At any rate, whatever might be the position in other cases, we are here concerned with a single indivisible contract of employment with a Hong Kong company under which the Taxpayer rendered his services for the company and in respect of which he was remunerated. There is, in our view, on the facts of this case a single indivisible source of income - the employment - irrespective of the fact that the Taxpayer, who was clearly based in Hong Kong and who spent two-thirds of the year here, had to spend the time which he did spend outside Hong Kong to carry out his duties under the self-same contract. The employment, we find, is a Hong Kong employment and the income is sourced in Hong Kong notwithstanding his trips abroad. We would have reached the same conclusion on all the facts even if the place where the services were performed were a relevant factor in determining source of income for present purposes.

27. Compare the position under the profits tax charging provision (section 14) where the territorial principle is carried to the point where it is necessary to show not only that the profits arose in or were derived from Hong Kong but that it must be from a trade, profession or business carried on in Hong Kong. Where a multi-source situation arises under section 14 the question of apportionment may become relevant but we are not persuaded that, in the case of a single indivisible contract of employment, we can extrapolate from the test, for purposes of profits tax under section 14, of ‘what the taxpayer has done to earn the profit in question’ to the proposition that, for purposes of salaries tax under section 8(1), ‘income from an employment arises in or is derived from the place where the employee’s services are performed.’

28. The appeal is accordingly dismissed and the assessment confirmed.