INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D28/04

Salaries tax – apportionment of income to services rendered outside of Hong Kong within meaning of section 8(1A)(a) of the Inland Revenue Ordinance ('IRO') – whether the time apportionment basis should be accepted – whether taxpayer discharged burden of proof in demonstrating that services rendered in Hong Kong was less than that calculated on the time apportionment basis.

Panel: Colin Cohen (chairman), Robin M Bridge and James Wardell.

Date of hearing: 20 May 2004.
Date of decision: 15 July 2004.

By a contract of employment dated 12 March 1998, the taxpayer was employed by Company B-I which was incorporated in a country outside Hong Kong. Pursuant to the contract, the taxpayer performed services as an investment officer both within and outside of Hong Kong.

In evidence, the taxpayer confirmed that the number of business days he spent outside Hong Kong in the year of assessment 1999/2000 was 164 days.

The issue before the Board was the quantum of income derived from services rendered in Hong Kong. The taxpayer submitted that only 20% of his income was attributable to his activities in Hong Kong.

Held:

1. Ordinarily, if a taxpayer's source of employment is in Hong Kong, the taxpayer is liable to salaries tax on the whole of his income from such employment, even though he is required to perform some of his duties outside Hong Kong.

2. Even if the taxpayer's income does not fall under the general charge under section 8(1) of the IRO, he is only liable to pay salaries tax on the whole of the income derived from services actually rendered in Hong Kong. The IRO does not, however, specify how such income should be apportioned as to arrive at the amount of remuneration attributable to services rendered in Hong Kong under section 8(1A)(a).

3. In practice, the quantum of income is usually determined by the Inland Revenue Department ('IRD') on a time apportionment basis having regard to the number of days in the year of assessment a taxpayer spends in Hong Kong. This is an acceptable basis for apportionment particularly where the employment contract does not contain express provisions which attributes specific amounts of remuneration to duties performed abroad.

4. There was no evidence before the Board to support the contention that only 20% of the taxpayer's income should be attributable to activities performed in Hong Kong. Accordingly, the appeal was dismissed.

Appeal dismissed.

Cases referred to:

CIR v George Andrew Goepfert 2 HKTC 210
Varnam (Inspector of Taxes) v Deeble [1985] STC 308
Plattan (Inspector of Taxes) v Brown [1986] STC 514
Coxon v Williams (Inspector of Taxes) [1988] STC 593
Leonard v Blanchard (Inspector of Taxes) [1993] 259, CA
D49/94, IRBRD, vol 9, 285
D1/96, IRBRD, vol 11, 290
D53/96, IRBRD, vol 11, 586

Tsui Siu Fong for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

Introduction

1. This is an appeal by Mr A ('the Taxpayer') in respect of the determination of the Deputy Commissioner of Inland Revenue dated the 15 January 2004. In that determination, the Deputy Commissioner assessed the Taxpayer to salaries tax in respect of assessable income of HK$3,398,444 with tax payable thereon of HK$509,766. The Taxpayer appealed the assessment on the grounds that he had a contract with a Country I – based company and as such intended that the services rendered by him were not in Hong Kong but outside Hong Kong.

2. The issue therefore to be decided by the Board is the quantum of the Taxpayer's income derived from such services rendered by him in Hong Kong in the year of assessment 1999/2000.

The facts

3. The Taxpayer did not dispute the facts as set out in the Deputy Commissioner's determination. The salient facts relevant to this appeal are as follows:

(a) The Taxpayer was employed by Company B – I. Company B – I is a company incorporated in Country I. It is jointly owned by three companies, namely Company B – II (incorporated in Country II), Company B – III (incorporated in Country III) and Company B – IV (incorporated in Country IV).

(b) The Taxpayer entered into a contract of employment on the 12 March 1998. He was the chief executive officer of the management company Company B – I. He was a member of the Board of Directors of Company B – HK and one of the representatives of the management company of the investment committee which had the authority to approve all investment and divestment decisions relating to an intended new Asian fund ('the Fund').

(c) The Taxpayer's employment was on a full time basis. He had an initial term of three years commencing on the 1 April 1998 and thereafter automatically extended for a one year period. The Taxpayer maintained a dual presence both in Country I and Hong Kong.

(d) The Taxpayer's remuneration was (i) a base salary of US$750,000 per annum and this was in aggregate for any and all duties performed under the employment contract and was payable by equal monthly instalments; (ii) a monthly housing allowance of US$5,000 each for Country I and Hong Kong; and (iii) a car at his disposal in Hong Kong.

4. The Taxpayer gave evidence before the Board. He confirmed that he was recruited by Company B – II. He was interviewed in Country II and an offer of employment was made to him. He is a Country IV citizen and was resident in City C. He advised us that he spent most of his time in three places, Hong Kong, Country I and City C. He accepted that the terms of his written contract of employment did not specify or particularize the way in which his salary was to be apportioned between the time spent in Hong Kong and the time spent in Country I or elsewhere. However, he indicated that during his discussions with his employer, there was a general agreement that twenty percent (20%) of his time would be allocated to work done in Hong Kong. Although, he had a housing allowance, whilst in Hong Kong he stayed at his sister's place and did not pay her any rent. However, he made some contribution to household expenses each month. The Fund

which he was employed to establish never got off the ground. He confirmed that the number of business days he spent outside Hong Kong for the year of assessment was 164 days. In his evidence, he again asserted that he should pay tax only on the salary he drew from Hong Kong, that is, HK$1,162,500 which he believed was a fair salary allocated to his Hong Kong activities and this reflected the value of such activities. He again asserted that given his numerous roles, his office in multiple locations and the need for him to travel extensively, his employer had agreed on a fair salary allocation or assessment for Hong Kong. However, he accepted and confirmed that his contract did not particularize or specify any such allocation of time spent in Hong Kong.

Our analysis

5. Section 68(4) of the Inland Revenue Ordinance ('IRO') provides that:

> *'The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.'*

Hence, the burden of proof is on the Taxpayer.

6. The basic charging section for salaries tax is section 8(1) of the IRO which provides as follows:

> *'Salaries tax shall, subject to the provisions of this Ordinance, be charged for each year of assessment 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; and'*

7. Section 8(1A)(a) of the IRO extends the basic charge to cover employment income from services rendered in Hong Kong including any leave pay attributable to such services:

> *'For the purposes of this Part, 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;'*

8. Section 9(1)(a) of the IRO sets out a non-exhaustive definition of 'income from employment' as follows:

> *'Income from any office or employment includes –*

(a) any wages, salary, leave pay, fee, commission, bonus, gratuity, perquisite, or allowance, whether derived from the employer or others ...'

9. Regard should be had to section 3 of the Apportionment Ordinance which provides as follows:

'3. Rents, etc. to accrue from day to day

All rents, annuities, dividends, and other periodical payments in the nature of income (whether reserved or made payable under an instrument in writing or otherwise) shall, like interest on money lent, be considered as accruing from day to day, and shall be apportionable in respect of time accordingly.'

10. In section 2 of the Apportionment Ordinance, the word 'annuities' is defined to include salaries and pensions.

11. The relevant legal principles are clearly set out in the leading case of CIR v George Andrew Goepfert 2 HKTC 210. Macdougall J summarized the operation of the subsections in section 8 of the IRO as follows:

'If during a year of assessment a person's income falls within the basic charge to salaries tax under section 8(1), his entire salary is subject to salaries tax wherever his services may have been rendered, subject only to the so called "60 days rule" that operates when the taxpayer can claim relief by way of exemption under section 8(1A)(b) as read with section 8(1B). Thus, once income is caught by section 8(1) there is no provision for apportionment.

...

On the other hand, if a person, whose income does not fall within the basic charge to salaries tax under section 8(1), derives income from employment in respect of which he rendered services in Hong Kong, only that income derived from the services he actually rendered in Hong Kong is chargeable to salaries tax. Again, this is subject to the "60 days rule".'

12. Macdougall J found that the taxpayer's employment had a locality outside Hong Kong and, in dismissing the appeal of the Commissioner against the decision of the Board of Review by excluding the taxpayer's emoluments attributable to the 41 days spent outside Hong Kong, he stated the following:

> *'Thus, the respondent, who in the light of the Board's findings does not fall within the basic charge imposed under section 8(1), is only liable to pay salaries tax on the whole of the income derived from the services he actually rendered in Hong Kong. Since he rendered services outside Hong Kong for 41 days he is not liable to salaries tax in respect of the income attributable to those services. In other words his income for salaries tax purposes is apportioned on a "time in time out" basis.'*

13. Therefore, it can be seen that if a person's source of employment is in Hong Kong, he is liable to salaries tax on the whole of his income from such employment, even although he is required to perform some of his duties outside Hong Kong in connection with his employment. The IRO, however, does not contain any provisions to regulate how income should be apportioned or calculated so as to arrive at the amount of remuneration attributable to services rendered in Hong Kong under section 8(1A)(a).

14. The quantum of such income is in practice usually determined by the Inland Revenue Department on a simple time apportionment basis having regard to the number of days in the year of assessment a taxpayer spent in Hong Kong, that is, an apportionment of remuneration including leave pay on a time-in and time-out basis.

15. The adoption of such a basis has been supported by various cases (Varnam (Inspector of Taxes) v Deeble [1985] STC 308, Plattan (Inspector of Taxes) v Brown [1986] STC 514, Coxon v Williams (Inspector of Taxes) [1988] STC 593 and Leonard v Blanchard (Inspector of Taxes) [1993] 259, CA). The time apportionment basis was adopted in the Goepfert case as well as in Board of Review Decisions Nos D49/94, IRBRD, vol 9, 285, D1/96, IRBRD, vol 11, 290 and D53/96, IRBRD, vol 11, 586. It is of interest to note that in those cases where the taxpayer's contracts of employment did not contain provisions which attributed specific amounts of remuneration to duties performed abroad, the Boards unanimously held that the time apportionment basis adopted by the Commissioner was an acceptable one for salaries tax assessment.

16. We accept that the time apportionment method is an acceptable basis and has been followed consistently in the majority of cases to which section 8(1A)(a) applies.

17. In the case before us, the Taxpayer contends only twenty percent (20%) of his total income should be attributable to his service to Company B – HK and as such, this is attributable to tax. However, we find that there is no evidence to support the basis of how such an alleged allegation was derived or arrived at. Therefore, we conclude that the Taxpayer's claim that only twenty percent (20%) of his remuneration should be subject to tax in Hong Kong was not supported by any evidence before us. In respect of housing allowance, it is quite clear and the Taxpayer confirmed that his remuneration was wholly cash based and that the allowances he received each month of US$10,000 were cash allowances and as such, they were income from the

employment as defined in section 9(1)(a) and therefore should be included in the computation of his taxable income under section 8(1A)(a). Hence, we agree that the same basis of apportionment should apply to the Taxpayer's whole remuneration, that is, the base salary as well as the housing allowances.

Conclusion

18. We therefore dismiss the Taxpayer's appeal as it is quite clear that the time apportionment basis adduced by the Commissioner of Inland Revenue in computing the Taxpayer's income was a fair, objective, reasonable, and an appropriate basis in the circumstances of the present case.