

Case No. D28/08

Salaries tax – whether the source of income located in Hong Kong – sections 8(1)(a), 8(1A)(c) and 12(1)(a) of the Inland Revenue Ordinance ('IRO') – was the rental expenses deductible.

Panel: Colin Cohen (chairman), Benny Kwok Kai Bun and Leung Hing Fung.

Date of hearing: 14 August 2008.

Date of decision: 30 September 2008.

Company A and Company B are related companies and carried out business in Hong Kong. Company A employed the Taxpayer as Merchandising Director with effect from 24 February 2003. During the period from 1 April 2004 to 31 December 2004, the Taxpayer rendered services to Company B. The Taxpayer had worked for Company B in Country E during October to December 2004.

The Taxpayer appealed against the salary tax assessment. The Board has to decide on the questions that: (1) Whether the Taxpayer had a liability to pay tax for the year of assessment 2003/04? (2) Was the source of the Taxpayer's income received from Company A and Company B located in Hong Kong? (3) Was the Taxpayer entitled to exemption section 8(1A)(c) of the IRO in respect of her salary income for the period from October to December 2004? (4) Was the rental expenses paid by the Taxpayer in respect of her residence deductible for the year of assessment 2003/04?

Held:

1. Although the Taxpayer rendered service in Country E during the three months from October to December 2004, it is an irrelevant fact in determining the source of her employment income. It is clear that the source of the Taxpayer's income received from Company A and Company B was located in Hong Kong and as such, her income fell within section 8(1)(a) of the IRO and in turn, she would be fully chargeable to salaries tax unless she was entitled to exemption under section 8(1A)(c) of the IRO (CIR v George Andrew Geopfert 2 HKTC 210 and Lee Hung-kwong v CIR 6 HKTC 543 followed).
2. In order to fall within the exemptions provided under section 8(1A)(c) the Taxpayer must prove (i) the salary income for the three months from October to

(2008-09) VOLUME 23 INLAND REVENUE BOARD OF REVIEW DECISIONS

December 2004 was derived from services rendered by her in the territory outside Hong Kong; (ii) by the laws of Country E, the subject income was chargeable to tax of substantially the same nature as salaries tax under the IRO; and (iii) the Deputy Commissioner is satisfied that the Taxpayer had paid tax of that nature in Country E in respect of the subject income.

3. Having carefully reviewed all the documents that were presented to the Board, there was no evidence whatsoever to support or illustrate any of the contentions that the Taxpayer or her representative showed the tax of that nature in Country E has been paid in respect of the subject income.
4. The rental expenses were obviously not incurred in the performance of the duties of the Taxpayer's employment. It is quite clear that these are private or domestic expenses. Hence, her attempt to deduct rental expenses paid by her for the year of assessment cannot be made out and as such, she was unable to satisfy the stringent conditions laid down under section 12(1)(a) of the IRO (CIR v Humphrey 1 HKTC 451 followed).

Appeal dismissed.

Cases referred to:

CIR v George Andrew Goepfert 2 HKTC 210
Lee Hung-kwong v CIR 6 HKTC 543
D34/01, IRBRD, vol 16, 303
CIR v Humphrey 1 HKTC 451

Taxpayer in absentia.

Chan Shun Mei and Chan Tak Hong for the Commissioner of Inland Revenue.

Decision:

1. This is an appeal by the Taxpayer who has not resided and worked in Hong Kong since September 2004. The Taxpayer sent an email on 3 July 2008 to the Board indicating that she was not sure when she would be back in Hong Kong and asked that her appeal be heard in her absence.

2. After considering her application pursuant to section 68(2D) of the Inland Revenue Ordinance (Chapter 112) ('IRO'), the Board was prepared to consent to her application being

(2008-09) VOLUME 23 INLAND REVENUE BOARD OF REVIEW DECISIONS

heard in her absence.

3. By the determination dated 29 April 2008, the Deputy Commissioner of Inland Revenue ('the Deputy Commissioner') made a determination as follows:

- '(1) *Salaries Tax Assessment for the year of assessment 2003/04 under Charge Number X-XXXXXXX-XX-1, dated 6 October 2004, showing Net Chargeable Income of \$604,000 with Tax Payable thereon of \$101,015 is hereby reduced to Net Chargeable Income of \$592,000 with Tax Payable thereon of \$98,795.*
- (2) *Salaries Tax Assessment for the year of assessment 2004/05 under Charge Number X-XXXXXXX-XX-2, dated 14 October 2005, showing Net Chargeable Income of \$608,000 with Tax Payable thereon of \$110,800 is hereby reduced to Net Chargeable Income of \$434,000 with Tax Payable thereon of \$76,000.'*

4. By a Notice of Appeal submitted to the Board on 29 May 2008, the Taxpayer appealed against the Deputy Commissioner's determination.

5. Her grounds of appeal are not clear. However, it seems as if the Taxpayer has taken the view that she has settled all the tax on her income derived from employment in Hong Kong she does not need to pay a further sum of HK\$31,380. The Taxpayer has entered into correspondence with Inland Revenue Department ('IRD') and from the correspondence, she has put forward, the following issues which need to be decided by the Board:

- (a) She takes the view that she has no liability to pay tax for the year of assessment 2003/04 since she is of the view that she has already settled her tax under charge no X-XXXXXXX-XX-3.
- (b) She contends that the employment income she received from a Hong Kong company for the period from October to December 2004 should not be chargeable to salaries tax. Her contention is that she had left Hong Kong in September 2004.
- (c) She contends that various rental expenses paid by her in respect of her residence should be deductible for the year of assessment 2003/04.

6. The facts of this matter are set out in the determination dated 29 April 2008. The salient facts are as follows:

- (a) Company A and Company B are private companies incorporated in Hong

(2008-09) VOLUME 23 INLAND REVENUE BOARD OF REVIEW DECISIONS

Kong. At all relevant times, both of them were related companies and carried out business in Hong Kong.

- (b) By an employment letter dated 19 February 2003 ('the Employment Letter'), Company A offered to employ the Taxpayer as Merchandising Director at a monthly salary of HK\$60,000 with effect from 24 February 2003. During the period from 1 April 2004 to 31 December 2004, the Taxpayer rendered services to Company B.
- (c) The Taxpayer subsequently filed tax returns for the years of assessment 2003/04 and 2004/05 in which she declared the following employment income particulars:

Year of Assessment	2003/04	2004/05
Name of employer:	Company B	Company A
Capacity employed:	Sales/Merchandising Director	
Period:	'Up to DEC 2004 8 months'	1-4-2004 – 30-9-2004
Total amount:	\$540,000	\$366,000

- (d) The Taxpayer also declared in her tax return for the year of assessment 2003/04 that she had paid rent of \$301,500 for her residence at Address C for 'DEC 2004'.
- (e) In reply to various enquiries raised by the assessors, Company B provided a breakdown of the Taxpayer's remuneration for the period from October to December 2004 as follows:

Month	Amount (HK\$)	Equivalent in Amount (US\$)
October	60,000	7,564
November	60,000	7,564
December	<u>60,000</u>	<u>7,564</u>
	<u>180,000</u>	<u>22,692</u>

- (f) Therefore, it is clear that the Taxpayer had worked for Company B in Country E during October to December 2004.

7. Section 8(1)(a) of IRO is the basic charging section for salaries tax. It provides as follows:

(2008-09) VOLUME 23 INLAND REVENUE BOARD OF REVIEW DECISIONS

'(1) 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 profits;

8. Section 8(1A)(c) excludes income derived by a person from services rendered by him in any territory outside Hong Kong where he has paid tax of substantially the same nature as salaries tax in respect of the income in that territory:

'(1A) For the purposes of this Part, income arising in or derived from Hong Kong from any employment –

.....

(c) excludes income derived by a person from services rendered by him in any territory outside Hong Kong where –

(i) by the laws of the territory where the services are rendered, the income is chargeable to tax of substantially the same nature as salaries tax under this Ordinance; and

(ii) the Commissioner is satisfied that that person has, by deduction or otherwise, paid tax of that nature in that territory in respect of the income.'

9. Section 12(1)(a) allows outgoings and expenses, other than expenses of a domestic or private nature and capital expenditure, which are wholly, exclusively and necessarily incurred in the production of the assessable income to be deducted in ascertaining the net assessable income of a person for any year of assessment:

'(1) In ascertaining the net assessable income of a person for any year of assessment, there shall be deducted from the assessable income of that person-

(a) all outgoings and expenses, other than expenses of a domestic or private nature and capital expenditure, wholly, exclusively and necessarily incurred in the production of the assessable income;'

10. Section 68(4) places on the Taxpayer the burden of proving that the assessment appealed against is excessive or incorrect:

(2008-09) VOLUME 23 INLAND REVENUE BOARD OF REVIEW DECISIONS

'(4) The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.'

11. The IRD in its written submissions drew to our attention the following authorities:

- (a) CIR v George Andrew Goepfert 2 HKTC 210 at page 238;
- (b) Lee Hung-kwong v CIR 6 HKTC 543;
- (c) D34/01, IRBRD, vol 16, 303;
- (d) CIR v Humphrey 1 HKTC 451.

12. Whether the Taxpayer had a liability to pay tax for the year of assessment 2003/04?

The Taxpayer contended that she was not obliged to any taxes under the relevant charge since there was nothing outstanding. It is quite clear that in accordance with the employer's return of remuneration filed by Company A for the year of assessment 2003/04, the Taxpayer had earned salaries of HK\$708,000 for the year. There can be no doubt in our mind that she was chargeable to salaries tax for that year of assessment.

13. Was the source of the Taxpayer's income received from Company A and Company B located in Hong Kong?

- (a) Again, we have no difficulties in concluding that the source of income received from Company A and Company B was located in Hong Kong. Both these companies were incorporated in Hong Kong and carried on business in Hong Kong throughout the Taxpayer's employment in Hong Kong during the period from 1 April 2003 to 31 December 2004, the Employment Letter was the contract in force. It was addressed to the Taxpayer at a Hong Kong address. She was paid in Hong Kong dollars and the remuneration was expressed in Hong Kong dollars. The relevant returns by Company A and Company B were filed for the respective years of assessment.
- (b) Although the Taxpayer left Hong Kong on 30 September 2004, she was still paid by Company A and Company B into her bank account here in Hong Kong.
- (c) We accept the submissions of the Deputy Commissioner's representative that although the Taxpayer rendered service in Country E during the three months from October to December 2004, it is an irrelevant fact in determining the source of her employment income. Having regard to the authorities, CIR v George Andrew Goepfert and Lee Hung-kwong v CIR, we accept that it is clear that the source of the Taxpayer's income received from Company A and

(2008-09) VOLUME 23 INLAND REVENUE BOARD OF REVIEW DECISIONS

Company B was located in Hong Kong and as such, her income fell within section 8(1)(a) of the IRO and in turn, she would be fully chargeable to salaries tax unless she was entitled to exemptions under section 8(1A)(c) of the IRO.

14. Was the Taxpayer entitled to exemption section 8(1A)(c) of the IRO in respect of her salary income for the period from October to December 2004?

- (a) In order to fall within the exemptions provided under section 8(1A)(c), the Taxpayer must prove:
 - (i) the salary income for the three months from October to December 2004 was derived from services rendered by her in the territory outside Hong Kong (that is, Country E in this case);
 - (ii) by the laws of Country E, the subject income was chargeable to tax of substantially the same nature as salaries tax under the IRO; and
 - (iii) the Deputy Commissioner is satisfied that the Taxpayer had paid tax of that nature in Country E in respect of the subject income.
- (b) The Taxpayer through her correspondence and through her representative in Country E contended that she paid all taxes both personal and corporate in full and according to Country E law. However, on close examination, there was no evidence to support such a proposition. Indeed, Country E tax return forms filed by the Taxpayer only indicated that she had reported salaries of US\$3,000 derived from a company known as Company D. It is quite clear that Company D is a separate legal entity. How Company D deals with its tax affairs in Country E is neither here nor there in illustrating whether the Taxpayer was entitled to claim exemptions under section 8(1A)(c) of the IRO.
- (c) Having carefully reviewed all the documents that were presented to us, there was no evidence whatsoever to support or illustrate any of the contentions that the Taxpayer or her representative showed the tax of that nature in Country E has been paid in respect of the subject income.

15. Was the rental expenses paid by the Taxpayer in respect of her residence deductible for the year of assessment 2003/04?

The authority of CIR v Humphrey 1 HKTC 451 concluded that the rental expenses were obviously not incurred in the performance of the duties of the Taxpayer's employment. It is quite clear that these are private or domestic expenses. Hence, her attempt to deduct rental expenses paid by her for the year of assessment 2003/04

(2008-09) VOLUME 23 INLAND REVENUE BOARD OF REVIEW DECISIONS

cannot be made out and as such, she was unable to satisfy the stringent conditions laid down under section 12(1)(a) of the IRO.

16. Therefore, having reviewed all the evidence, documents and submissions put before us, we have no hesitation in dismissing the Taxpayer's appeal and confirm the Deputy Commissioner's determination.