INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D29/95

Salaries tax – employee seconded to work overseas – whether income assessable to salaries tax.

Panel: Kenneth Kwok Hing Wai QC (chairman), Raymond Faulkner and Larry Kwok Lam Kwong.

Date of hearing: 27 April 1995.
Date of decision: 14 June 1995.

The taxpayer was employed as a quantity surveyor. He was seconded to work full-time out of Hong Kong. The taxpayer argued that his original employment contract had been terminated and that he had entered into a new employment contract.

Held:

The employment was not terminated but continued throughout the period.

Appeal dismissed.

Cases referred to:

Meek v Port of London Authority [1918] 2 Chapter 96 (CA)
The Marley Tile Co Ltd v Johnson [1982] IRLR 75 (CA)

Chiu Kwok Kit for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

1. This is an appeal against the determination dated 6 October 1994 by Mr Anthony Au Yeung, Commissioner of Inland Revenue, confirming the salaries tax assessment for the year of assessment 1992/93 which included the Taxpayer's income for the period from 17 August 1992 to 31 March 1993 ('Period B') when the Taxpayer was seconded to work overseas and which the Taxpayer contended should not be subject to Hong Kong salaries tax.

The Facts

2.1 The Taxpayer was first employed by Company A as a quantity surveyor on 25 June 1990. The contract of employment was in the form of a letter of that date ('the 1990 Letter') from Company A to the Taxpayer and countersigned by the Taxpayer agreeing and accepting Company A's offer.

2.2 By letter dated 17 August 1992 ('the 1992 Letter') from Company A to the Taxpayer and countersigned by the Taxpayer agreeing the terms and conditions, Company A confirmed that 'the terms of [the Taxpayer's] appointment by Company A for Project X' were as set out in the letter. The starting date of the Taxpayer's appointment was 17 August 1992 and the duration of the Taxpayer's appointment was 'related to the appointment of Company A' by Company B for Project X which was due to be completed in 1995.

2.3 The employer's return of remuneration and pensions for the year ended 31 March 1993 dated 12 April 1993 filed by Company A in respect of the Taxpayer showed that the Taxpayer was employed as an assistant quantity surveyor, that his period of employment was from 1 April 1992 to 31 March 1993; that his income for such period was $251,165; and that the Taxpayer was not paid by an overseas concern.

2.4 In a letter dated 27 May 1993 ('the 1993 Letter') to the Inland Revenue Department, Company A certified that the Taxpayer had 'been employed by Company A since 25 June 1990 as quantity surveyor'; that he had been seconded to work on a full time basis in Country M for Project X from 17 August 1992; and that the Taxpayer's remuneration for Period B totalled $177,469.

2.5 In his salaries tax return for the year of assessment 1992/93 dated 1 June 1993, the Taxpayer declared income of $73,696 received from Company A for the period from 1 April 1992 to 16 August 1992 ('Period A').

2.6 In a letter also dated 1 June 1993, the Taxpayer applied for exemption from salaries tax in respect of his income for Period B, claiming that during this period he was working full time in Country M based on a new secondment contract having different working hours, holiday, salaries and notice of termination from those set out in the original employment contract, and that no service had been rendered in Hong Kong. The Taxpayer also relied on the 1992 Letter and the 1993 Letter.

2.7 On 30 November 1993, the assessor raised on the Taxpayer salaries tax assessment for the year of assessment 1992/93 with principal income of $251,165, with tax payable thereon of $37,674. The assessor noted that time-basis claim had not been allowed as the Taxpayer's secondment to Country M was not considered as a separate employment and the Taxpayer's stay in Hong Kong exceeded 60 days.

2.8 By letter dated 13 December 1993, the Taxpayer objected to the assessment on the ground that his income for Period B should be exempted from salaries tax. The Taxpayer contended that the original employment contract was terminated on 18 August

1992 and that the secondment contract was a new contract and not just an extension of the original one.

2.9 At the request of the assessor, Company A supplied a copy of a letter dated 21 July 1992 issued by Company B to Company A appointing the latter as sub-consultant in the Project X, under which Company A was to supply a team of 3 staff, made up of a head of cost control and 2 quantity surveyors.

2.10 Company A also confirmed that during the period of the Taxpayer's secondment to Country M, no service had been rendered by the Taxpayer in Hong Kong and that Company B had total jurisdiction and exercised control over the Taxpayer's work. Company A also advised that the secondment contract would be automatically terminated upon completion of Project X and the Taxpayer would then join the Hong Kong office for other projects.

2.11 By his determination dated 6 October 1994, the Commissioner confirmed the salaries tax assessment for the year of assessment 1992/93.

2.12 By notice dated 3 November 1994, the Taxpayer appealed against the Commissioner's determination.

Identity of the Taxpayer's employer during Period B

3.1 The Taxpayer contended that his employer during Period B 'should be considered as "Company A on behalf of Company B"'.

3.2 The Taxpayer gave oral evidence on oath. His evidence in no way supported any suggestion that Company B or any person/consortium other than Company A had at any time during Period B been the Taxpayer's employer.

3.3 During cross-examination he said that:

> 'I am not telling the Board or the Judge I am not employed by Company A. What I said is that at 1992, August, the nature of the employment was changed. I am still paid under Company A. Because the proper channel is I need to inform Company A, Company A informed the consortium, that is the proper channel because it is the channel they employed us to Country M…'

3.4 When asked if he had any point which he wished to clarify as a result of the questions asked by the representative of the Commissioner, he said that:

> 'I just want to repeat one thing is I never say the relationship … or Company A is no longer my employer but just I would want to say at 1992 August, the form of the employment was changed. Nothing further.'

3.5 In his letter dated 1 June 1993 to the assessor, the Taxpayer stated that in 'August 1992, myself **and Company A** arrived at a mutual agreement to start a new **secondment** contract with Company B …' (emphasis added).

3.6 The 1992 Letter confirmed in writing the terms of the Taxpayer's 'appointment by Company A'.

3.7 The 1993 letter certified that the Taxpayer 'has been employed by Company A since 25 June 1990 as quantity surveyor and was seconded to work full time basis in Country M…'.

3.8 On the evidence before us, we find that Company A had been the Taxpayer's employer throughout Period B.

The Taxpayer's grounds of appeal

4. The Taxpayer contended that his original employment contract with Company A was terminated or rescinded or discharged when he entered into a new employment contract with Company A contained in or evidenced by the 1992 Letter; that for the purposes of salaries tax, what was material was an employment contract, not employment; and that in any event, he entered into new employment on or about 17 August 1992.

Section 8(1), (1A) & (1B)

5. Section 8 of the Inland Revenue Ordinance (the IRO), chapter 112, provides that:

> *'(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 profit…*
>
> *(1A) 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;*
>
> *(b) excludes income derived from services rendered by a person who-*
>
> *(i) …*
>
> *(ii) renders outside Hong Kong all the services in connection with his employment'.*

(1B) 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 Hong Kong during visits not exceeding a total of 60 days in the basis period for the year of assessment.'

Our Decision

6.1 It is clear that from the charging section, that is, section 8, that salaries tax is charged on income arising in or derived from Hong Kong from 'employment', not 'contract of employment'.

6.2 There is a good reason why salaries tax is charged with reference to employment, and not employment contract. The fact of life is that an employment contract is often varied. If what is relevant is the employment contract, and not employment, this means that every time an employment contract is varied (and variations of employment contracts are not infrequent), both the Taxpayer and the assessor will have to consider whether it is variation or rescission, a question of some nicety in quite a number of cases. On the other hand, if what is relevant is employment, then it is immaterial whether there is a new employment contract in substitution of the original employment contract, so long as the Taxpayer continues to be employed by the same employer. The charging section should be simple and easy to apply. We have not overlooked section 11B which aggregates income from all sources, but income from each source has to be computed first, the simplier and the easier, the better.

7. We find that the Taxpayer had been in the employment of Company A for the whole of the year of assessment 1992/93, that is, Period A and Period B. We are not persuaded by the Taxpayer that his employment during Period B was a new employment and we reject this ground of appeal.

8. Thus the fact that all the services rendered during Period B were rendered outside Hong Kong does not assist the Taxpayer as the Taxpayer's employment by Company A was from 1 April 1992 to 31 March 1993, that is, Period A and Period B. It is common ground that Period A exceeded 60 days. By reason of subsection (1B), subsection (1A) does not assist the Taxpayer.

9.1 Having held that what is relevant for salaries tax purposes is employment, and not employment contract, and having rejected the Taxpayer's contention that his employment during Period B was new employment, it is unnecessary for us to deal with the question whether the Taxpayer was employed under a new contract of employment during Period B.

9.2 Neither party cited any authority on this point.

9.3 Chitty on Contracts, 27th Edition, Volume 1, paragraph 22-025, states the general principals in these terms:

> *'Substituted contract. A rescission of the contract will also be implied where the parties have effected such an alternation of its terms as to substitute a new contract in its place. The question whether a rescission has been effected is frequently one of considerable difficulty, for it is necessary to distinguish a rescission of the contract from a variation which merely qualifies the existing rights and obligations. If a rescission is effected the contract is extinguished; if only a variation, it continues to exist in an altered form. The decision on this point will depend on the intention of the parties to be gathered from an examination of the terms of the subsequent agreement and from all the surrounding circumstances. Rescission will be presumed when the parties enter into a new agreement which is entirely inconsistent with the old, or, if not entirely inconsistent with it, inconsistent with it to an extent that goes to the very root of it. The change must be fundamental and "the question is whether the common intention of the parties was to 'abrogate,' 'rescind,' 'supersede' or 'extinguish' the old contract by a 'substitution' of a 'completely new' or 'self-subsisting' agreement."'*

9.4 In Volume 2, paragraph 37-115, the learned Editors state the general principles in relation to employment contracts in these terms:

> *'Termination by agreement. In accordance with general contractual principles, it is open to an employer and employee at any time during the currency of a contract of employment to terminate the contract by agreement … A termination of a contract of employment by agreement occurs also where there is an agreed change in the terms and conditions of employment, for instance by way of promotion, which is sufficiently fundamental to constitute the rescission of the original contract and its replacement by a new contract on different terms.'*

9.5 In Meek v Port of London Authority [1918] 2 Chapter 96 (CA), a case cited in the passage quoted above, the court of appeal held that promotion and increase in salaries for 3 employees and increase in salary (which was not an automatic increase under the previous contract) for the 4th employee constituted new contracts.

9.6 The Marley Tile Co Ltd v Johnson [1982] IRLR 75 (CA) is a case which seems to have escaped the attention of the learned Editors of Chitty on Contracts. In this case, the court of appeal held that promotion from area contracts manager to unit manager, increase in salary from £5,050 by £950 to £6,000; and requiring the employee to move from St Austell in Cornwall – where his home was – to the Plymouth area in Devon were mere variations of the last formal contract, so that it continued on the old terms except as it was varied.

9.7 These 2 court of appeal cases demonstrate how difficult the question of whether there was variation or rescission is. Since we have received no assistance on this

point and since it is unnecessary for the purpose of this decision to decide the issue whether there was a new contract, we will express no opinion on it.

10. For the reasons given above, the Taxpayer has not discharged the onus under section 68(4) of proving that the assessment appealed against is excessive or incorrect. We dismiss the appeal and confirm the assessment appealed against.