Case No. D45/86

Board of Review:

Denis K. L. Chang, *Chairman*, Andrew J. Halkyard and Edmund T. C. Lau, *Members.*

27 January 1987.

Salaries Tax—Income arising in or derived from Hong Kong under Section 8(1) and (1A) of the Inland Revenue Ordinance—Appellant employed by a company incorporated in the United States and having an office in Hong Kong—Appellant required to look after the employer's business in Hong Kong and the Far East through Hong Kong Branch—whether the Appellant's salary for the period spent out of Hong Kong liable to tax.

The Appellant who was in the employ of a multi-national service organisation incorporated in the United States claimed that he should be assessed to tax only on that part of his remuneration attributable to the periods he was present in Hong Kong on a time-in, time-out basis. In 1981/82 the Appellant spent 220 days in Hong Kong and 53 business days outside Hong Kong, and in the following year 292 days in Hong Kong and 73 business days outside Hong Kong.

Held:

The salary in question arose or was derived from a Hong Kong source, applying the "totality of facts" test. The rendering by the Appellant of services in other regions in the Far East could not be dissociated from the duties of the Hong Kong Post.

Appeal dismissed.

D. J. Gaskin for the Commissioner of Inland Revenue.
Antonio A Amador of A. A. Amador and Associates for the Appellant.

Reasons:

This is an appeal against Salaries Tax Assessments for the years of assessment 1981/82 and 1982/83. The Taxpayer claims that he should be assessed to tax only on that part of his remuneration which is attributable to the periods he was present in Hong Kong on a time-in, time-out basis.

The Taxpayer was at the relevant times in the employ of RA, Inc. (the Company). The Company is, and was at all material times, a multi-national service organisation incorporated in the United States of America engaged in the recruitment of business executives.

Before coming to Hong Kong in 1981 the Taxpayer was employed as Vice President in the Company's head-office in New York. With effect from 1 June 1981 he was assigned to the Company's branch office in Hong Kong (the Hong Kong Branch) which had an office in Prince's Building, a prime location in Hong Kong. He occupied a position described as "Managing Director" although as a matter of fact he was not on the Board of Directors. It is, however, not in dispute that he was and is the chief executive of the Hong Kong Branch which has working within it consultants, research managers, associates and ancillary staff. It was he who was responsible for establishing the branch office here and for looking after the employer's business in Hong Kong and the Far East through the Hong Kong Branch and from his base in Hong Kong.

The Taxpayer's salary for the period 1. 6.81 to 31. 3.82 was US$68,668.99; for the period 1. 4.82 to 31. 3.83 it was US$87,999.96. From 1 June 1981 to 31 December 1981 he also received a bonus of US$10,000 and another bonus of US$7,000 for the period 1. 4.82 to 31. 3.83. The Taxpayer was paid in New York but all his emoluments were charged as an expense account against the Branch's income in the Branch's Profit and Loss Account. The Hong Kong Branch was also responsible for his accommodation rental and business expenses incurred on behalf of the Company in Hong Kong and Asia.

It is not in dispute and we find that in 1981/82 the Taxpayer spent 220 days in Hong Kong and 53 business days outside Hong Kong. In 1982/83 he spent 292 days in Hong Kong and 73 business days outside Hong Kong.

Section 8(1) of the Inland Revenue Ordinance provides that salaries tax shall, subject to the provisions of the 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 (*b*) any pension.

Section 8(1A) provides that "for 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; 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 (Added, 2 of 1971, s. 5)

(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 (Added, 2 of 1971, s. 5).

The law is clear. To determine whether the income has its source in Hong Kong, the Board has to look at the "totality of the facts", not just at the location of services rendered or the place where the contract of employment was signed or the place where payment for the services is made: see Board of Review Case No. BR14/75 and Case No. BR6/72. All the factors must be considered, including the nature of the employer's enterprise, the job in which the taxpayer is engaged and where he is based.

The Taxpayer, in support of his contention that he should be assessed on a time-in, time-out basis, has placed particular emphasis on the nature of the employer's enterprise and his duties to develop and service executive recruiting consulting assignments throughout Asia on behalf of the employer's offices in the United States and Europe. It was argued that the role played by the Hong Kong Branch was no more than that of a place where administrative matters could be conveniently managed, not "the focus and magnet for the generation of income", that the Company's assets were its people, that the Taxpayer could just have easily (although) not as conveniently) generated income operating from a hotel room and leasing computer time for his record purposes, that "profit was generated not by and through the deployment of capital and the management of labour but purely and simply by the performance of a service" and thus it was argued that the source of salary income in the present case was the place where the services were performed.

It was further argued that the Taxpayer's duties when on assignment outside Hong Kong (while generating assessable income for the Hong Kong Branch) were totally separate from his duties in Hong Kong: his assignments, it was argued, were "by the very nature of his responsibilities of recruiting executives within and without Hong Kong, performed on the request of clients within and without Hong Kong." The Taxpayer pointed out that although the income secured by the Taxpayer's services outside Hong Kong formed part of the income of the Hong Kong Branch, the income from a particular assignment overseas by the Taxpayer would be shared between the Hong Kong Branch and the referring office of the Company based on the effort-input of both offices and that the expenses incurred on overseas business trips would normally be for the account of the clients and that while he was abroad he would be "responsible to a Mr. D stationed in the U.S. Head Office and also the person from the specific office referring the assignment".

It was also argued that as the Hong Kong Branch has no separate legal existence the fact that the salary was charged to the Hong Kong Branch's Profit and Loss Account did not mean that the economic burden was not ultimately borne by the foreign corporation in New York.

The Revenue, on the other hand, argues that apportionment on a time-in, time-out basis is permissible only where the Board is satisfied that the Taxpayer's remuneration neither arose nor was derived from a source in Hong Kong; that in determining the source of income for salaries tax purposes, neither the place of service nor the place of payment is conclusive; that the Taxpayer's services rendered outside Hong Kong could not be dissociated from the duties of the Hong Kong post; those duties included servicing assignments in other parts of the Far East from the Hong Kong base.

All factors considered, we find that the salary in question arose or was derived from a Hong Kong source. We are fortified in our conclusion by a consideration of the decided cases cited to us although each case must turn on its own particular facts. The basic test in Section 8(1) is source in *income*. In Board of Review case D11/82 (HKIRBRD, Vol. 2 page 11 at p. 17 the Board says:

> "while it is an agreed fact that the contract of employment was entered into out of the Colony …. We do not think that this affects the fundamental or originating cause of the Taxpayer's means of earning income which was, in our view, his assignment to work …. from a base in Hong Kong; and at p. 19:
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> "….. Where income from an employment stems mainly from Hong Kong based activities all the remuneration will be assessable to Salaries Tax without any right to apportionment."

In the present case, we have no difficulty in finding that the Taxpayer's income was derived from an employment which stemmed mainly from *Hong Kong based activities*. That he was based in Hong Kong is not in dispute. It was from this base, from and through his post in Hong Kong, that he furthered his employer's business and service clients in Hong Kong and elsewhere in the Far East. There is in evidence and as part of the agreed facts (see Appendix A to the Commissioner Determination) a copy of the Company's letter dated 25th February 1980 appointing the Taxpayer as Vice President of its New York Office. Although the Taxpayer was recruited in New York and the contract presumably made and enforceable there, it is quite clear from the letter that even at that stage the Company was contemplating the setting up in the Far East of a Branch Office: Hong Kong was judged to be ideal and as the most suitable location because of its "business environment, freedom of markets, and general climate" which were considered to be "the most favourable for a Western-oriented service organisation to prosper". The move to Hong Kong was described as the second phase of the Taxpayer's career with the Company and the hope was already expressed that "revenues generated from an office in Hong Kong could be in the area of (US) $600,000 to (US) $700,000 by the end of 1981, (US) $1.5 million by the end of 1982 …." The letter also observed, and among other things, that "a development of an adequate number of assignments to support a Hong Kong Office would be limited only to the ability of the individual responsible for it to realize what his own potential is."

We agree with the Revenue that the rendering by the Taxpayer of services in other regions in the Far East could not be dissociated from the duties of the Hong Kong post. We

agree with the Commissioner's Determination. We accordingly dismiss the appeal and confirm the assessments.