

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D55/91

Salaries tax – secondment overseas from Hong Kong – whether still employed in Hong Kong or new contract overseas.

Panel: Robert Wei QC (chairman), Foo Tak Ching and Lester Kwok Chi Hang.

Dates of hearing: 30 August and 12 September 1991.

Date of decision: 30 October 1991.

The taxpayer was employed by a company in Hong Kong. He was sent on secondment to work for another group company in India. The assessor assessed him to tax on the basis that he had only one employment contract which was a Hong Kong employment contract and as he had worked in Hong Kong under that contract of employment, he was subject to Hong Kong salaries tax in respect of the income which he earned whilst on secondment in India. The taxpayer appealed to the Board of Review and submitted that he had two employment contracts. The first was with a company in Hong Kong under which he provided services in Hong Kong. When he was seconded to India, his employment with the Hong Kong employer was suspended and he was temporarily employed by a different company in India.

Held:

On the facts the taxpayer was correct in maintaining that he had two separate employment contracts. As all of the remuneration which he had received for his services in India arose under the second and separate employment contract and as all of the services which he had provided under that contract were provided outside of Hong Kong, he was not subject to salaries tax thereon.

Appeal allowed.

Case referred to:

D67/89, IRBRD, vol 5, 52

J R Smith for the Commissioner of Inland Revenue.

Taxpayer in person.

INLAND REVENUE BOARD OF REVIEW DECISIONS

Decision:

This is an appeal by a taxpayer against the salaries tax assessment raised on him for the year of assessment 1988/89. He claims that the income earned by him when he was assigned to work for a project in India is not subject to tax by reason of section 8(1A)(b) of the Inland Revenue Ordinance.

2. On 1 February 1985 the Taxpayer began his employment with X Ltd, a subsidiary of Y Ltd group on certain terms and conditions relating to remuneration, membership of a retirement benefit scheme, notice of termination and other terms and conditions in the standard conditions of service.

3. As notified by a letter dated 31 August 1985 from X Ltd to the Taxpayer, the Taxpayer was transferred on 1 September 1985 to the project division of Y Ltd ('Y Ltd'), another subsidiary of Y Ltd group. Apart from notifying the transfer, the letter merely stated that 'all your other terms and conditions of service will remain unchanged'.

4. On 8 September 1986 the Taxpayer was assigned to work for projects in China. The assignment lasted until 9 August 1987. A memo dated 2 September 1986 from the personnel and administration manager to the Taxpayer with regard to the assignment is in the following terms:

'This is to give you official notification that you will be assigned to work as [post title cited] for China projects with effect from 8 September 1986. It is anticipated that your assignment will continue until the end of September 1987.

During the period of assignment, you will be paid, in addition to your basic salary, an overseas allowance of \$3,900 per month. Accommodation and meals expenses will be reimbursed to you by the company.

You will be granted one calendar week leave for every three months service and be provided with return passage to Hong Kong. You will not earn leave at the rate of three weeks per year during your period of overseas assignment and your accrued leave as at 8 September 1986 will be carried forward until the completion of your overseas assignment. Overseas allowance is not payable for leave periods during your assignment.'

The memo was copied to the general manager of Z Ltd, another subsidiary of Y Ltd group, the head of the Taxpayer's division, the chief accountant and the insurance officer.

5. The services rendered by the Taxpayer in China during the period of assignment mentioned above were rendered on behalf of Z Ltd. The business of Z Ltd was to provide technical services to third parties outside the Y Ltd group of companies.

INLAND REVENUE BOARD OF REVIEW DECISIONS

6. During his assignment in China Y Ltd paid the Taxpayer in Hong Kong his remuneration which was reimbursed to Y Ltd by Z Ltd.

7. Both Y Ltd and Z Ltd were companies incorporated in Hong Kong and the management of both companies was in Hong Kong.

8. In respect of the years of assessment 1986/87 and 1987/88 Y Ltd filed employer's returns with the Inland Revenue Department stating that the Taxpayer continued to be employed by it throughout the period of his assignment in China.

9. In his tax returns for those two years the Taxpayer also stated that his employer was Y Ltd during the accounting period.

10. The Taxpayer appealed to a Board of Review against the salaries tax assessments raised on him for the years of assessment 1986/87 and 1987/88 on the grounds that he was employed by Z Ltd to render his services in China during the period of his assignment, that in connection with that employment he had rendered all the services outside Hong Kong and that his income derived from those services should not be subject to salaries tax. On 30 October 1989 the Board who heard the appeal dismissed it on the grounds that the Taxpayer was employed by Y Ltd throughout the accounting period, including the period of assignment (D67/89).

11. In the meantime the Taxpayer had been seconded from Y Ltd to Z Ltd to work in India. The secondment was in the first place from 10 May 1988 to 9 January 1989 and was later extended to 30 June 1989. On 5 May 1988 Z Ltd on its own letterhead wrote to the Taxpayer in the following terms:

‘This is to give you official notification that you will be seconded to [Z Ltd] to work as [post title cited] on [name of project cited] in India. Your duties will be performed in India.

Commencement Date

The commencement date of the secondment will be 10 May 1988.

Duration of Contract

The duration of your secondment will be eight months.

Site Allowance and Gratuity

During the period of secondment when you are working in India, you will be eligible for a site allowance at the rate of \$17,000 per month. Payment of this allowance will be in the form of \$10,500 payable monthly, and \$6,500 to be retained as gratuity and will be released on completion of the secondment.

INLAND REVENUE BOARD OF REVIEW DECISIONS

Salaries Tax

Salaries tax in India, if required, will be borne by the company. Salaries tax in Hong Kong, if requires, will be borne by yourself.

Transport, Accommodation and Meal

Travelling, accommodation and meals will be provided free when you are working in India.

Leave and Passage

You will be granted a total of one month paid leave with return passage to Hong Kong for the whole secondment period. You will not earn leave at the rate of three weeks per year during your period of secondment and your accrued leave as at the commencement date of your secondment will be carried forward until the completion of your secondment. Site allowance is not payable for leave periods during your secondment.

[Y Ltd] Employment Terms

As your overseas assignment is on secondment basis, your other terms and conditions of employment with [Y Ltd] will remain unchanged.

Your sincerely,
[Z Ltd]

(signed)
Manager (Personnel & Administration)'

The letter was copied to the general manager of Z Ltd, the head of the Taxpayer's division, which was a reference to Y Ltd, and the staff accountant. At the foot of page 2 of a copy of the letter the Taxpayer signed a form of acceptance which reads:

' I [the Taxpayer's name stated] hereby accept the offer of employment set out in the original letter of which this is a copy and agree to abide by the terms thereto.

Signature: [Taxpayer's signature]

Date: 6 May 1988'

12. During the secondment in India the Taxpayer was paid in Hong Kong by Y Ltd has remuneration which was later reimbursed by Z Ltd.

INLAND REVENUE BOARD OF REVIEW DECISIONS

13. On 23 October 1989 Z Ltd wrote to the Commissioner of Inland Revenue supplying the following information in answer to his inquiry:

- ‘ 1. [The Taxpayer’s duties and responsibilities in India are stated.]
2. All his duties and responsibilities were wholly devoted to that project in India during the period of secondment. His occasional return to Hong Kong was merely for renewal of visa to India.
3. We enclose copies of the employment contract relating to [the Taxpayer’s] secondment for your perusal.’

14. On 20 November 1989 Y Ltd wrote to the Commissioner of Inland Revenue about the Taxpayer’s secondment as follows:

- ‘ During the period of his secondment to India from 10 May 1989, [the Taxpayer] had been under the sole administration of [Z Ltd] and operational wise was regarded as [Z Ltd] staff accordingly. In this respect you may refer to the [Z Ltd] employment contract which we have previously copied to you as covered by the [Z Ltd] letter dated 23 October 1989. There is no termination of employment from our view-point of the staff establishment, therefore we do not issue any termination document on this matter.’

15. There was correspondence between the Inland Revenue Department and Y Ltd on the matter of employer’s returns in connection with the secondment to Z Ltd of another employee of Y Ltd. Y Ltd was seeking the advice of the Inland Revenue Department as to which company should file an employer’s return with regard to that employee’s secondment. The Inland Revenue Department responded on 9 November 1988 as follows:

- ‘ As [Z Ltd] ultimately bears the remuneration for [the said employee], this remuneration should be reported under the employer’s return file for [Z Ltd], to which please note.’

That advice was followed not only in the said employee’s case, but also in the Taxpayer’s case in respect of the year of assessment 1988/89. Thus, in respect of that year Y Ltd filed an employer’s return with the Inland Revenue Department stating that it was the Taxpayer’s employer from 1 April 1988 to 9 May 1988 while Z Ltd filed an employer’s return stating that it was the Taxpayer’s employer from 10 May 1988 to 31 March 1989.

16. In his salaries tax return for the year of assessment 1988/89 the Taxpayer stated that Y Ltd was his employer from 1 April 1988 to 9 May 1988 and that Z Ltd was his employer from 10 May 1988 to 31 March 1989. During the latter period the Taxpayer visited Hong Kong for 47 days. He did no work during those visits.

INLAND REVENUE BOARD OF REVIEW DECISIONS

17. The Taxpayer's case is this: during the secondment he was employed in Hong Kong by Z Ltd, but he rendered all the services in connection with that employment outside Hong Kong, and only visited Hong Kong for 47 days during which he did no work. By reason of section 8(1A)(b), he claims that he is not liable to pay salaries tax in respect of his remuneration derived from services rendered in connection with that employment. On the other hand, Mr Smith, the representative of the Commissioner of Inland Revenue, contends that the Taxpayer was employed by Y Ltd throughout the accounting period, that since he worked in Hong Kong from 1 April 1988 to 9 May 1988, he did not render all the services in connection with his employment outside Hong Kong, that therefore section 8(1A)(b) does not apply and that his remuneration in question is assessable to salaries tax.

18. The question in this case is who was the Taxpayer's employer during his secondment. Put another way, with which company did he enter into the contract of service which governed his employment during the secondment?

19. There is no definition of a secondment, but we think it is correct to say that it is a period of temporary employment at the end of which the employee returns to his general employment. Depending on the circumstances of the case, the secondment may be based on a contract of service made between the temporary employer and the employee with the consent of the general employer, or it may be simply a case of the general employer directing the employee to go and do some work for the temporary employer without involving the creation of a contract of service between the temporary employer and the employee. D67/89, in which the same Taxpayer as in this case, is a case of the latter class: the Taxpayer's assignment to work in China (see paragraphs 4 to 10 above) did not affect the contract of service with Y Ltd; in fact the employer's returns filed by Y Ltd and the tax returns filed by the Taxpayer were all to the effect that Y Ltd was the employer of the Taxpayer throughout the two years of assessment 1986/87 and 1987/88. However, in the present case, for reasons we shall state later, we find that a contract of service was made between Z Ltd and the Taxpayer with the consent of Y Ltd in respect of the Taxpayer's secondment to India and that the Taxpayer's employment with Y Ltd was suspended for the duration of the Taxpayer's temporary employment with Z Ltd.

20. The terms of the secondment are set out in the letter dated 5 May 1988 from Z Ltd to the Taxpayer (the secondment letter)(see paragraph 11 above). That Z Ltd was regarding the secondment as a matter of contract is demonstrated by the fact that in the body of the secondment letter the duration of the secondment is referred to as 'duration of contract'. The Taxpayer signed a typewritten form of acceptance appearing in the lower left hand corner of a copy of the secondment letter to the effect that he thereby accepted the offer of employment set out in the secondment letter and agreed to abide by the terms thereof. We find that the form of acceptance was put there by Z Ltd for the Taxpayer's signature which he duly signed. The signed acceptance form is in our view clear evidence of the conclusion of a contract of service between Z Ltd and the Taxpayer and we accept that evidence. If the Taxpayer had been simply directed by Y Ltd to go and work for a while in India for Z Ltd, the acceptance form would have been unnecessary, and the expression 'duration of contract' would have been incorrect. The secondment letter was copied to Y Ltd, the words '[the head

INLAND REVENUE BOARD OF REVIEW DECISIONS

of the Taxpayer's division]' under 'c.c.' being a reference to Y Ltd. Furthermore, both Z Ltd and Y Ltd in their respective letters to the Inland Revenue Department (see paragraphs 13 and 14 above) referred to the secondment letter as 'the employment contract relating to [the Taxpayer's] secondment' and 'the [Z Ltd] employment contract'. There is no doubt in our minds that all three parties concerned regarded the secondment letter together with the acceptance as constituting a contract of service between Z Ltd and the Taxpayer.

21. Mr Smith relied on the last paragraph of the secondment letter which reads:

'As your overseas assignment is on secondment basis, your other terms and conditions of employment with [Y Ltd] will remain unchanged.'

He quoted those words in support of his contention that the secondment letter did not constitute a contract of service with Z Ltd, but only a variation of the Y Ltd contract of service which continued to apply, as varied, during the secondment, with the result that Y Ltd, not Z Ltd, was the Taxpayer's employer during the secondment. We do not agree. Similar phraseology had been used before: the letter dated 31 August 1985 from X Ltd to the Taxpayer (see paragraph 3 above) notifying him of his transfer to the Y Ltd ends with the words 'All your other terms and conditions of service will remain unchanged'. It is not disputed that upon the transfer a contract of service was created between Y Ltd and the Taxpayer; so the words can only mean that all the other terms and conditions of the X Ltd contract would apply mutatis mutandis within the framework of the new Y Ltd contract. Likewise here: we are concerned with a secondment, a temporary transfer, but all the three parties concerned, Y Ltd, Z Ltd and the Taxpayer, took it on the basis of a temporary contractual relationship arising between Z Ltd and the Taxpayer. That being so, the words in the last paragraph of the secondment letter cannot bear the meaning contended for by Mr Smith; in our view, the true construction is that the other terms and conditions of employment with Y Ltd were to apply mutatis mutandis within the framework of the new contract of service with Z Ltd.

22. We cannot leave this case without mentioning the employer's returns filed by Y Ltd and Z Ltd (see paragraph 15 above). Mr Smith submitted that the returns were made on the basis that the company which ultimately bore the cost of the Taxpayer's remuneration during the secondment period should file an employer's return for that period, and therefore that the employer named in the return was not necessarily the company which was contractually bound to the Taxpayer to pay him. We accept that, and have placed no reliance on those employer's returns in determining which company was the Taxpayer's employer during the secondment, although we cannot help observing in passing that in this case, it so happened that the company which ultimately bore the cost of the remuneration was in fact also the company which owed a contractual obligation to the Taxpayer to pay him that remuneration.

23. For all these reasons, we conclude as follows:

INLAND REVENUE BOARD OF REVIEW DECISIONS

- (1) For the period from 1 April 1988 to 9 May 1989 the Taxpayer was in the employment of Y Ltd;
- (2) For the period from 10 May 1988 to 31 March 1989 the Taxpayer was in the employment of Z Ltd;
- (3) All his services in connection with his employment with Z Ltd were rendered outside Hong Kong; and
- (4) His income derived from his services rendered in connection with his employment with Z Ltd is not subject to salaries tax.

24. It follows that this appeal is allowed and that the assessment in question is to be reduced in accordance with paragraph 23(4) above.