Case No. D8/92

Salaries tax – source of income – taxpayer overseas – procedure to be followed – whether source in Hong Kong.

Panel: William Turnbull (chairman), Chen Yuan Chu and Eleanor Wong.

Date of hearing: 4 March 1992.
Date of decision: 29 April 1992.

The taxpayer was resident in USA when he received a written offer of employment from a company in Hong Kong. The taxpayer accepted the employment contract by signing and returning to Hong Kong the offer which he had received. The employer was a member of a multi-national group and the services of the taxpayer was to be a Far East Internal Controls Manager. The duties of the taxpayer included responsibility not only for the Hong Kong company which employed him but also other companies within the Group in the Far East.

At the hearing of the appeal the taxpayer was unable to be present and asked for the appeal to be heard in his absence. The taxpayer submitted that his remuneration should be apportioned on a days-in/days-out basis because his source of employment was outside of Hong Kong.

Held:

Where a taxpayer is unable to be present and the appeal is heard in his absence an appropriate procedure is for the Commissioner's representative to place before the board the case for both the taxpayer and the Commissioner.

On the facts before it the Board found that the source of income which was the employment was located in Hong Kong.

Appeal dismissed.

Case referred to:

CIR v George Andrew Goepfert 2 HKTC 210

S P Barns for the Commissioner of Inland Revenue.
Taxpayer in absentia.

Decision:

This is an appeal by a Taxpayer against an additional salaries tax assessment. The Taxpayer claimed that his employment had a source outside of Hong Kong and that he should only pay tax in respect of the services which he rendered in Hong Kong, that is, on a 'days in-days out' basis. The facts are as follows:

1. The Taxpayer was a resident in the USA. He received a written offer of employment from a company ('the company') incorporated in Hong Kong which was a member of an international group of companies ('the group') with their holding company or headquarters in the USA. The offer of employment was in the form of a letter dated 7 December 1988 and was sent from an address in Hong Kong. It was addressed to the Taxpayer at his address in the USA where he received it and he accepted it by signing the acceptance on 12 December 1988 and returning the same to the company in Hong Kong.

2. The employment letter dated 7 December 1988 provided, inter alia, that the Taxpayer would be paid a monthly salary in Hong Kong dollars calculated on a thirteen month basis with the thirteenth month considered as annual bonus payable in the following January after he had completed one full calendar year of service and pro rata for any broken periods. The letter stated that other employee benefits would be the same as those currently enjoyed by other employees of the company in Hong Kong.

3. The Taxpayer commenced his employment with the company on 9 February 1989 and the company filed with the Inland Revenue Department an employer's tax return in respect of the Taxpayer showing his taxable emoluments for the year of assessment 1988/89 as a total of $52,672.

4. The nature of the employment of the Taxpayer was as a Far East Internal Controls Manager. Though his employment was by the company which was incorporated in and carried on business in Hong Kong his duties included responsibility not only for the company but also other companies within the group in other countries of the Far East. He was required in the course of his employment to visit and work in these other countries.

5. The Taxpayer filed a salaries tax return for the year of assessment 1988/89 in which he reported his gross remuneration for the period from 9 February 1989 up to 31 March 1989 as $52,672 and deducted therefrom the sum of $7,385 which he claimed was the due proportion of his remuneration attributable to the services which he provided outside of Hong Kong. On 5 December 1989 a salaries tax assessment for the year of assessment 1988/89 was raised on the Taxpayer wherein the assessor assessed the Taxpayer to tax on taxable income of $45,287 being the net amount returned by the Taxpayer.

6. Following further enquiries the assessor was of the opinion that the employment of the Taxpayer had a Hong Kong source and that accordingly he was not entitled to deduct a pro rata amount from his taxable income for services rendered overseas. Following correspondence and representations by the taxpayer the assessor on 22 August 1990 raised an additional salaries tax assessment on additional assessable income of $7,385 which after adjustment became additional net chargeable income of $8,124 with additional tax payable thereon of $488.

7. The Taxpayer lodged an objection against this additional assessment. By his determination the Deputy Commissioner confirmed the additional salaries tax assessment against which the Taxpayer had objected.

8. The Taxpayer duly appealed to this Board of Review.

At the hearing of the appeal the Taxpayer was unable to be present because he is again resident in the USA. He made written application to the Board to hear his appeal in his absence pursuant to section 68(2D) of the Inland Revenue Ordinance. The Board agreed to hear the appeal in the absence of the Taxpayer as requested.

There is no procedure laid down by the Inland Revenue Ordinance as to how the Board of Review should handle appeals under the section 68 (2D) procedure. Following previous cases the representative for the Commissioner indicated that he would place before the Board, to the best of his ability, the case for the Taxpayer as it appeared from the Commissioner's determination, and the notice and statement of grounds of appeal as lodged by the Taxpayer. We would like to place on record our appreciation to Mr S P Barns who was the representative for the Commissioner who not only read to us the Commissioner's determination and the notice and statement of grounds of appeal by the Taxpayer but used his best effort to present before us a balanced case both for the Taxpayer and for the Commissioner.

In the representations which the Taxpayer had made to the Commissioner the Taxpayer had submitted that his employment did not have a Hong Kong source but had its source in the USA. He stated that his contract of employment was negotiated and entered into and was enforceable in the USA and was signed and accepted by himself in the USA on 12 December 1988. He said that he was employed by a division subsidiary of a United States corporation whose central management and control were located in the USA. He submitted that his remuneration should be apportioned on the basis of the days which he spent in Hong Kong versus the days he spent abroad and that the fact that he had been paid for his oversea services in Hong Kong was not material and only a matter of convenience. He pointed out that he worked directly for 'the Far East Region' and not for the company which he submitted exercised no jurisdiction or control over his work. He said that he was the Business Controls Manager for the Far East Region and that he supervised the business controls programme in various subsidiary companies which were owned by the United States parent. He further submitted that the business controls programme was supervised by

the parent in the USA. He went on to state that there was no relationship of master and servant between himself and the company. He said that all his duties related to the 'regional entity' and that he took direction from the personnel in the USA. These submissions were repeated to us by the representative for the Commissioner on behalf of the Taxpayer in the course of our hearing this appeal.

The facts which the Taxpayer submitted as part of his notice and statement of grounds of appeal were read before us. In summary they are to the effect that the Taxpayer was not employed by the company but by either the group or the parent of the group in the USA. Unfortunately for the Taxpayer we are not able to accept the submission that he was not employed by a company in Hong Kong under a Hong Kong contract of employment enforceable in Hong Kong. He was resident and physically present in the United States when he received and signed the employment contract. Though in certain cases the acceptance of a contract in a particular country may be of great significance, in the present case it has little significance. The offer of employment was made by a company in Hong Kong and from Hong Kong. The offer was to take up employment in Hong Kong and to perform duties in Hong Kong and elsewhere. Though the Taxpayer might consider himself to have been an employee of a multinational group of companies, we must be precise when considering employment contracts for taxation purposes. There is no such thing recognized as 'a group of companies' for employment or taxation purposes. In the case before us it is very clear that the Taxpayer was offered employment by a company incorporated in Hong Kong which carried on its business in Hong Kong. He was paid in Hong Kong dollars in Hong Kong by that company. He was required to locate himself in Hong Kong. He was not employed by any company in the United States and he was not subject to any master and servant relation with any United States company. His master and servant relation was clearly with the company in Hong Kong with whom he entered into an employment contract. In the circumstances of this case the fact that he was physically in the United States when he received the employment contract is not material.

Both the Taxpayer and the Commissioner made reference to the case of CIR v George Andrew Goepfert 2 HKTC 210. The Goepfert case is an important decision which is binding on this Board. However the facts of the Goepfert case are very different from the facts of this case. In the Goepfert case the Taxpayer was employed by a company in the USA and was seconded to work for another group company in Hong Kong. The master and servant relationship was with the USA company and not the Hong Kong company. In the present case we have the opposite situation. Macdougall J said at page 237:

> ' Specifically, it is necessary to look for the place where the income really comes to the employee, that is to say, where the source of income, the employment, is located.'

In the case before us it is clear that the source of income, namely, the employment, was located in Hong Kong.

One of the submissions made by the Taxpayer supports the decision which we have reached. He pointed out that multinational organisations endeavour to reduce their

taxes and social legislation responsibilities. He submitted that this is what had happened in the present case and that the group had classified himself as a Hong Kong employee to avoid a number of taxes in the USA such as workers' compensation, FICA, unemployment compensation etc. We do not know the reason why the group decided that the company should employ the Taxpayer. It may or may not have been for the reasons submitted by the Taxpayer. However if we accept what the Taxpayer submitted then it makes it clear that the intention of the employer and it follows likewise the acceptance by the employee, was that the employment of the employee was situated in Hong Kong. It is not necessary for us to point out that the relationship of master and servant is a formal one because the Taxpayer in this submission has done so for us. It is not open to him to accept a Hong Kong contract of employment and then subsequently argue that really it should be considered to be an American contract of employment because this would give the Taxpayer a more favourable tax treatment in Hong Kong. The management of the group decided that the Taxpayer would be offered employment by the company which was a Hong Kong company and that the Taxpayer would be employed in Hong Kong on Hong Kong terms and conditions. This the Taxpayer accepted and it is not now open to him to try to argue that in reality he worked for someone else or on different terms and conditions.

For the reasons given we dismiss this appeal and confirm the additional salaries tax assessment against which the Taxpayer has appealed.