



## Hong Kong Tax Newsflash

### Apportionment method for calculating exempted income for salaries tax purpose



On April 14, 2021, the Court of First Instance (CFI) concluded that for the purpose of calculating "exempted income" under Section 8(1A)(c) of the Inland Revenue Ordinance (IRO), income attributed to weekends and statutory holidays in the secondment location for non-work purposes during the secondment period should also qualify for income exemption, irrespective of where the Taxpayer physically happened to have been. In addition, any apportionment method should be justified by its facts and circumstances.

#### Case background

- The Taxpayer was an employee of a Hong Kong company and was seconded to Mainland China (the PRC) between August 1, 2014 and March 31, 2015.
- The Taxpayer had a work base in the PRC during the secondment period.
- There was no provision in the secondment letter stating any contractual allocation between services rendered in Hong Kong and services rendered in the PRC.

- The Taxpayer occasionally had to return to Hong Kong for work and spent more than 60 days in Hong Kong during a year of assessment. As such he was not eligible to claim full income exemption under Section 8(1A)(b)(ii) in conjunction with Section 8(1B).
- The Taxpayer was entitled to statutory public holidays in the PRC.
- The Taxpayer visited Hong Kong on Saturdays, Sundays, statutory PRC holidays and during annual leave; all were for non-work purposes.
- The Inland Revenue Department (IRD) adopted the "day in, day out" approach in calculating income qualifying for income exemption under section 8(1A)(c). Under the approach adopted by the IRD, income in relation to the Taxpayer's days spent in Hong Kong for non-work purpose was not exempt from salaries tax.
- The Board of Review (BoR) did not agree with the "day in, day out" approach adopted by the IRD and viewed that the approach was *"arbitrary and led to injustice"*. In the case of the Taxpayer, the Saturdays, Sundays and PRC statutory holidays that the Taxpayer spent in Hong Kong for non-work purposes should not be counted against his claim under section 8(1A)(c) of the IRO as the Taxpayer did not render any services in Hong Kong during these holidays.

### The CFI's judgement

- In line with the BoR's view, the CFI considered that the facts and situation did not justify that the "day in, day out" basis as being a fair approach in calculating the amount of income qualifying for income exemption under section 8(1A)(c).
- When deciding the apportionment for income exclusion, regard can be given to any contractual attribution, and time apportionment is not impermissible if the facts and evidence justify its adoption.
- In the present case, the approach agreed by the CFI is that the part of the Taxpayer's income allocated to weekends and PRC statutory holidays should qualify for exclusion for the purpose of section 8(1A)(c), irrespective of where the Taxpayer physically was over those weekends and PRC statutory holidays.
- The CFI agreed with the BoR's approach and dismissed the appeal from the IRD.

### Our comment

We should note that the CFI's apportionment approach for calculating exempted income under Section 8(1A)(c) of the IRO may vary from the IRD's existing practices (i.e. "day in, day out"). In general, the CFI's approach may give a taxpayer, who is on secondment overseas but physically spends weekends/holidays in Hong Kong, a greater extent of tax relief. The apportionment method will be based on the facts and circumstances of each case and this would be a good reference point.

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