

INLAND REVENUE BOARD OF REVIEW DECISIONS

**Case No. D2/87**

*Board of Review:*

William Turnbull, *Chairman*, Benjamin C. Kwok and R. J. McAulay, *Members*.

**8 May 1987.**

Salaries Tax—Section 12(1) of the Inland Revenue Ordinance—whether payment in lieu of notice allowable as a deduction from the assessable income.

The Appellant was employed by A on a monthly basis and his contract of employment could be determined by his giving 3 months' notice of termination or by his paying one month's salary in lieu of notice. The Appellant found alternative employment with B on better terms and since he had not given the requisite 3 months' notice he was required to pay to A one month's pay in lieu of notice.

*Held:*

In a similar case BR 9/78 it was decided that such payment was not incurred for the purpose of producing assessable income. In that case the Appellant first terminated his contract and then, as a separate matter, obtained a new employment, whereas in the present case he obtained the offer of employment with B and could only accept that offer by terminating his employment with A.

Appeal allowed.

(Note: Commissioner has appealed to the High Court.)

T. J. Richmond for the Commissioner of Inland Revenue.  
Appellant in person.

*Reasons:*

The facts of this case, so far as they are relevant to the point at issue can be summarized briefly.

The Appellant was employed by employer A on a monthly basis. His contract of employment could be terminated at any time by his giving 3 months' notice of termination to his employer or by his paying one month's salary in lieu of notice.

The Taxpayer sought and found alternative employment with employer B on better terms and conditions than he was receiving from employer A. The employment offered by employer B commenced on 5 June 1979 at which time the Taxpayer was still in the service of employer A. The Taxpayer had not given the requisite 3 months' notice to terminate his employment with employer A and to obtain his release from his employment with employer A, the Taxpayer paid to employer A one month's pay in lieu of notice.

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There was at one time some confusion as to whether or not the payment made by the Taxpayer to employer A was a refund of one month's wages or was a payment in lieu of notice to secure his release from his employment. The Taxpayer gave evidence on his own behalf and the Inland Revenue Commissioner's Representative produced certain documentary evidence, all of which made it clear that employer A had paid the Taxpayer his full wages up to and including the day on which he left the employment of employer A and that the Taxpayer had paid to employer A a sum equal to one month's pay being the contractual sum required to terminate the service of the Taxpayer with employer A.

The Taxpayer argued that he should be entitled to deduct from the taxable emoluments which he received from employer B the amount which he had been obliged to pay to employer A to secure his release from his previous contract.

The representative for the Commissioner submitted that the payment in question was not an expense wholly, exclusively and necessarily incurred in the production of the assessable income. The Commissioner's representative cited as authority for his proposition the Board of Review decision B/R 9/78 which was a case having apparently similar facts.

The Board of Review in case B/R 9/78 decided that a payment in lieu of notice was not incurred for the purpose of producing assessable income from employer A but was a payment to finalise severance of the relationship of the Taxpayer with employer A. That Board of Review said:—

“As the Appellant had terminated his services with the Government, failure to pay the \$6,600.00 to his former employer would not preclude him from taking up employment with his new employer. It would merely give to the Government a right of action for payment of damages.”

We do not know what were the full facts of the case decided by the Board of Review B/R 9/78. It would appear that there may have been a fundamental difference between that case and the case now before us. In the present case the Taxpayer had a contractual obligation to work for employer A until such time as he either had given 3 months' prior notice of termination or paid an amount equal to one month's wages. The Taxpayer wanted to accept an offer of employment with employer B but could not lawfully do so because of his existing contractual commitment to employer A. The only way in which he could lawfully accept employment with employer B was to agree to pay a sum equal to one month's wages to employer A. This he decided to do and this was in accordance with the terms of his contract with employer A.

We agree with the Board of Review in case B/R 9/78 that the payment made to employer A was not incurred in the production of earning any emoluments from employer A. However that begs the question. The question to be decided and the argument put forward by the Taxpayer was that the payment made to employer A was wholly, exclusively and necessarily incurred to enable him to take up employment with and earn taxable emoluments from employer B. With due respect to the Commissioner and possibly to the Board of

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Review in case B/R 9/78, we decide on the facts of this case in favour of the Taxpayer. The Taxpayer could not lawfully have obtained employment with employer B if he did not terminate his contractual obligations with employer A. He could not lawfully have earned his emoluments from employer B without paying a sum equal to one month's wages to employer A.

The distinction between this appeal and the previous decision B/R 9/78 would appear to lie in the fact that in B/R 9/78 the Taxpayer first terminated his contract with employer A and then, as a separate matter, obtained employment with employer B where as in this case he obtained the offer of employment with employer B and could only accept that offer by terminating his employment with employer A.

For the reasons given and on the facts of this case we find in favour of the Taxpayer and order that the taxable emoluments for the year in question be reduced by the amount which the Taxpayer paid to employer A to terminate his service contract with employer A and that the assessment appealed against be reduced accordingly.