Case No. D11/24

Salaries tax – termination of employment – three sums of payment described as 'year end bonus', 'three months' notice payment' and 'other payment' made to appellant by former employer assessed to be chargeable to salaries tax – true purpose(s) of payments – burden on appellant to show assessment excessive or incorrect – whether sums chargeable to salaries tax – sections 8, 9 and 68(4) of the Inland Revenue Ordinance (IRO)

Panel: Ma Yiu Tim Jimmy (chairman), Lau Chi Yan Kerby and Zhang Wei Yin Vivian.

Dates of hearing: 15 July 2024 & 7 August 2024.
Date of decision: 14 October 2024.

In the taxpayer (appellant)'s appeal against the determination dated 4 January 2024 (the determination) of the Deputy Commissioner of Inland Revenue (the Commissioner) wherein three sums of payment (the Sums) made to him by his former employer, a company registered in Hong Kong (the company), were assessed to be chargeable to salaries tax in respect of the year of assessment 2016/17, the Board adopted and applied the principles set out in Fuchs v CIR (2011) 14 HKCFAR 74 (confirmed in CIR v Poon Cho-ming, John [2019] HKCFA 38), and asked: 'In light of the terms of the appellant's employment and the circumstances of his termination, what is, in substance, the true purpose(s) of the individual items of payment that constituted the Sums?'

The Sums comprised a 'Year end bonus' (Sum-YEB) of $150,538, a 'Three months' notice payment' (PILON) of $911,016 and 'Other payment' of $911,016 (Sum-OP) and the salaries tax assessed to be payable was $562,664.

The facts to which the Board gave consideration included the appellant's employment agreement dated 19 April 2013, in particular at clauses 14.1 and 14.2, which provided respectively, 'The Employment Agreement could be terminated by either party by giving 3 months' notice in writing or payment in lieu of such notice' and 'If the Appellant is released without cause, he will be provided with 3 months' severance, consisting of base salary, housing allowance, car allowance, and medical insurance, subject to any further obligation', and a letter dated 10 July 2016, by which the appellant was notified that his employment with the company was being terminated with immediate effect and that the company would honour the terms of the employment agreement. Further, as the company had previously confirmed, the appellant was released from the company without cause but by mutual agreement.

Before the Board, the appellant contended that the Sums were cash compensation for his agreeing to the terms in a separation agreement, ie the abrogation of his rights thereunder, and other obligations he had agreed with the company. The company stated that payment in the sum of $2,376,515.21 had been remitted to the appellant in recognition of the appellant's past contribution and settling the termination in a smooth and friendly manner. The Commissioner had suggested that no obligations were created under the separation agreement, but all were common law duties that the appellant had long been subjected to.

The applicable legal provisions included section 68(4) IRO under which it fell upon the appellant to prove that the assessment appealed against was excessive or incorrect. Additionally, section 8 IRO was the charging provision for salaries tax, catching any 'income arising in or derived from Hong Kong from any office or employment', which itself was defined under section 9 IRO as including 'any wages, salary, leave pay, fee, commission, bonus, gratuity, perquisite, or allowance, whether derived from the company or others'.

Held:

1. The appellant had effectively agreed with the company's classification of his departure as a termination without cause and that it was by mutual consent for the benefit of the appellant's future career that the termination was described as resignation. It was not a voluntary resignation. Consequently, in accordance with clause 14.2 of the employment agreement, the company was obliged to provide base salary, housing allowance, car allowance, and medical insurance to the appellant.

2. The arrangement of the appellant receiving payment of $2,376,515.21 prior to the signing of the separation agreement did not support his claim that such payment was made as consideration for signing the separation agreement, particularly since the company never received a signed version. Instead, it reinforced the company's position that the payment was made in accordance with legal obligations then existing.

3. The Sums were income from employment and were taxable. The PILON was paid by the company pursuant to clause 14.1 of the employment agreement to effect termination by providing a payment in lieu of notice. The Sum-OP amounted to three months of the appellant's salary and housing allowance, and came within clause 14.2 of the employment agreement. The Sum-YEB was a pro-rated guaranteed 13^{th}-month salary payable to the appellant. The appellant had failed to discharge his burden of proof to show that the assessment for the year of assessment 2016/17 imposed on him was excessive or incorrect. Accordingly, the determination that the salaries tax payable for 2016/17 in the amount of $562,664 would be affirmed.

Appeal dismissed and costs order in the amount of $20,000 imposed.

Cases referred to:

Fuchs v Commissioner of Inland Revenue (2011) 14 HKCFAR 74 at 81
Commissioner of Inland Revenue v Poon Cho-ming, John [2019] HKCFA 38
Robb v Green [1985] 2 QB 315

Appellant in person.
Ho Lut Him, Cheng Po Fung and Lam Kwun Wing, for the Commissioner of Inland Revenue.

Decision:

A. The Appeal

1. The question in this appeal is whether three sums of payment made to the Appellant by his former employer (defined as '**Sums**' below), a company registered in Hong Kong (the '**Company**'), are chargeable to Salaries Tax.

2. By the Determination dated 4 January 2024 ('**Determination**'), the Deputy Commissioner of Inland Revenue decided that the Sums are chargeable with the salaries tax payable being $562,664. The Appellant contended otherwise and he lodged this appeal against the Determination.

3. The three sums, collectively referred to as the '**Sums**' are:

Particulars of income	$	Sum
Year end bonus	150,538	Sum-YEB
Three months' notice payment	911,016	PILON
Other payment	911,016	Sum-OP

B. Legal Principles

4. Pursuant to section 68 of the Inland Revenue Ordinance (the '**Ordinance**'), the Appellant bears the onus of proving that the assessment, that is the Determination, appealed against is excessive or incorrect.

5. Section 8 of the Ordinance is the charging provision for Salaries Tax, which provides that income arising in or derived from Hong Kong from any office or employment of profit and any pension is chargeable to Salaries Tax.

6. '*Income from any office or employment*' is defined in section 9 of the Ordinance to include '*any wages, salary, leave pay, fee, commission, bonus, gratuity,* perquisite*, or allowance, whether derived from the company or others*'.

7. A payment received by an employee from his company is not necessarily income 'from his employment' within the definition of section 9 of the Ordinance. (See: Fuchs v Commissioner of Inland Revenue (2011) 14 HKCFAR 74 at 81 [16])

8. Income chargeable under section 8(1) of the Ordinance is not confined to income earned in the course of employment but also embraces:

a. payment made 'in return for acting as or being an employee';

b. payment made 'as a reward for past services'; and

c. payment made 'as an inducement to enter into employment and provide future services'.

[Fuchs [17]; Commissioner of Inland Revenue v Poon Cho-ming, John [2019] HKCFA 38 [14]]

9. In considering the nature of payment, one shall look at the substance, but not merely the form, and shall not be 'blinded by some formulae which the parties may have used'. One is to look at the true purpose for which the payment was made, but not the parties' characterisation of such payment. [Fuchs [17-18]]

10. In cases where payment was made to an employee when the employment is brought to an end, it will often be plausible for an employee to assert that the payment was made to compensate for his abrogation of his employment rights and argue that the payment was not subject to salaries tax. The Court of Final Appeal in Fuchs acknowledged this situation and held that to decide whether the above argument should be accepted, the operative test must be:

> '*In the light of the terms on which the taxpayer was employed and the circumstances of the termination, is the sum in substance "income from employment"? Was it paid in return for his acting as or being an employee? Was it an entitlement earned as a result of past services or an entitlement accorded to him as an inducement to enter into the employment? If the answer is "yes", the sum is taxable and it matters not that it might linguistically be acceptable also to refer to it as "compensation for loss of office" or something similar. On the other hand, the amount is not taxable if on a proper analysis the answer is "No". As the "abrogation" examples referred to above show, such a conclusion may be reached where the payment is not made pursuant to any entitlement under the employment contract but is made in consideration of the employee agreeing to surrender or forgo his pre-existing contractual rights.*' [Fuchs [22]]

11. The principles and approaches set out in Fuchs were confirmed by both the Court of Appeal and Court of Final Appeal in Poon's case. We respectfully adopted and applied these principles, and asked ourselves the question:

In light of the terms of the Appellant's employment and the circumstances of the termination, what is, in substance, the true purpose(s) of the individual items of payment that constituted the Sums?

C. Facts

Chronology of Key Events

12. The facts that are relevant to the issue to be determined in this appeal are set out below.

13. By a letter dated 18 April 2013 (the '**Offer of Employment**'), the Company offered to employ the Appellant as Position A commencing from 22 July 2013. The Offer of Employment was accepted by the Appellant with the following proposed terms of employment that are relevant to the present appeal:

a. Basic Salary: The Appellant will receive a gross base salary of $2,751,250 per annum, which is payable monthly.

b. Housing Allowance: The Appellant will be offered up to $45,000 per month for suitable housing support in Hong Kong.

c. Discretionary Bonus: The Appellant will be eligible to participate in the broad-based bonus scheme, subject to its terms and conditions as determined by the Company, and the targeted award level is 40% of the annual base salary.

d. Company Car: The Appellant will be provided a paid vehicle for his use.

e. Notice of Termination: Either party may terminate the employment by giving 3 months' written notice or payment in lieu of notice.

f. Severance: In the event the Appellant is released from the Company without cause, he will be provided with 3 months' severance, consisting of base salary, housing allowance, car allowance, and medical insurance, subject to any further obligation.

g. Confidentiality: All client information related to the Company's business operation is strictly confidential.

14. An agreement dated 19 April 2013 (the '**Employment Agreement**') was signed between the Appellant and the Company to employ the Appellant as Position A, commencing on or before 22 July 2013. The terms of employment relevant to the present appeal are:

a. Remuneration at Clause 5

i. The Appellant will receive a gross base salary of $2,751,250 per annum which is payable monthly with $45,000 per month for suitable housing support in Hong Kong. The Appellant is also eligible to participate in the Executive 'B' Share Stock Program, Company L Long-Term Incentive Plan, Broad-based bonus scheme.

b. Confidential Information at Clause 10

i. In addition to common law duties, the Appellant neither during his employment nor after termination shall use or disclose any trade secrets or confidential information relating or belonging to the Company or its associated company.

c. Termination of Employment at Clause 14

i. The Employment Agreement could be terminated by either party by giving 3 months' notice in writing or payment in lieu of such notice.

ii. If the Appellant is released without cause, he will be provided with 3 months' severance, consisting of base salary, housing allowance, car allowance, and medical insurance, subject to any further obligation.

15. By a letter dated 10 July 2016 (the '**Termination Letter**'), the Appellant was informed at a meeting by his immediate supervisor, Mr B (the '**Position C**'), that his employment with the Company would be terminated with immediate effect. The Termination Letter further informed the Appellant that the Company would honour the terms of the Employment Agreement.

16. The Company filed two Notification Forms (IR56F) on two occasions in respect of the Appellant for the year of assessment 2016/17 and 2017/18. A breakdown calculation of the amount furnished in the IR56F is provided in Attachment D of the Company's reply to the Assessor dated 15 March 2018, as set out in paragraph 24 below. The two IR56F provided, *inter alia*, the following particulars:

	11 April 2017	8 March 2018
Nature of Notification	Original	Additional
Period of employment	1-4-2016 – 31-7-2016	1-3-2018 – 1-3-2018
Capacity in which employed	Position A, AP	
Reason for cessation	Resignation	
Particulars of Income ($)		
Salary	1,034,688	
Leave Pay	101,772	
Payment in Lieu of Notice	1,552,032	
Other rewards	150,538	(share) 1,169,548
	2,839,030	

17. The Appellant failed to file his Tax return for the year of assessment 2016/17 by 29 September 2017. As a result, the Assessor issued a Notice of Estimated Salaries Tax Assessment for the year of assessment 2016/17 (the '**Notice**') on 29 September 2017. The Notice raised the following:

	$
Income	3,122,933
Less: Allowances	132,000
Net chargeable income	2,990,933
Tax Payable at standard rate	448,439

18. The Appellant objected to the above estimation on the ground, as set out in the Form IR831 dated 9 November 2017, that the sum $2,990,933 was estimated to be excessive. The Appellant also enclosed the Termination Letter when submitting the Form IR831, though the Termination Letter was only signed by the Company but not the Appellant.

19. On 9 November 2017, the Appellant submitted a Form BIR60 to the Inland Revenue Department declaring the following income for the year of assessment 2016/17:

Period	Amount ($)
1-4-2015 – 31-7-2016	1,074,688

20. He also claimed in the Form BIR60 deduction of retirement scheme contributions, child allowance in respect of his child as well as single parent allowance.

21. After being notified of the Appellant's objection, the Assessor sent two letters in December 2017 - one dated 4 December 2017 to the Company, and another dated 6 December 2017 to the Appellant. Both letters requested additional information from the Company and Appellant respectively to facilitate the processing of the objection.

22. On 8 January 2018, the Appellant sent an email to the Assessor ('**the Email**') enclosing a document entitled 'Separation Agreement' dated 14 July 2016 (the '**Separation**

Agreement I'). Separation Agreement I was signed by the representative of the Company but not the Appellant, and included the following terms, among others:

a. In consideration of the premises and mutual covenants contained therein, the Company and the Appellant mutually desire to terminate the appointment of the Appellant to any and all positions under the Employment Agreement on terms and conditions set out in the separation agreement[1].

b. The Company and the Appellant agreed that the Appellant voluntarily resigned from his position. (Clause 1)

c. The Appellant is entitled to all the remuneration, MPF contribution, and allowances as agreed to under the Employment Agreement accrued up to and including the Last Working Day subject to his compliance with the Employment Agreement (Clause 3)

d. The Company agreed to provide to the Appellant payment in a sum of $2,514,515.21 as separation package. The Appellant specifically understood and agreed that the separation package thereunder included all the payment of salaries, remuneration, allowances, compensation and any other amounts accrued up to and including the Last Working Day. (Clause 4)

e. The Appellant confirmed that no further or additional payment, compensation, leave time, allowance, or other benefits would be furnished or paid to him in connection with his appointment or employment for any position at the Company, including Position A, Asia Pacific or otherwise, or termination thereof. (Clause 5)

f. Confidentiality obligation under the Employment Agreement survived the termination of appointment of the Appellant by the separation agreement[2]. (Clause 8)

g. The Appellant agreed that for a period of one year after the Last Working Day, he would not solicit or endeavour to entice away any business and/or customers from the Company or its affiliates, and he would not cause any other employee or officers of the Company or its affiliates to leave his/her employment or position with the Company or its affiliates. (Clause 9)

h. The Appellant expressly waived, released, discharged and acquitted any and all claims against the Company and its affiliates from all causes of action. (Clause 10)

[1] The separation agreements are the same, except for their respective amounts of compensation and signatures depicted.
[2] *ibid*.

23. In the Email, the Appellant advanced the following:

a. He received the Termination Letter on 10 July 2016, which stated that all terms of the Employment Agreement would be honoured.

b. He asked for the termination date to be 31 July 2016, and the Company agreed. As a result, his full July 2016 salary was reported as chargeable income.

c. The Company asked him to sign Separation Agreement I. However, after seeking advice from a legal advisor and tax accountant, he realized that signing it would increase his legal and tax liabilities. Therefore, he decided not to sign Separation Agreement I because he disagreed with its terms.

24. In response to the Assessor's enquiries, the Company, through a tax advisor, sent a letter dated 15 March 2018 to the Assessor, which enclosed the following:

a. The Company Organizational Announcement, Asia Pacific;

b. A document entitled 'Separation Agreement' (the '**Separation Agreement II**');

c. Final Salary Payment Breakdown attached to Separation Agreement II;

d. Breakdown of calculations furnished in IR56F;

e. Offer of Employment;

f. Employment Agreement; and

g. A letter from the Company to the Appellant dated 4 April 2017.

25. The Company also provided in the letter, among others, the following information:

a. Since the Appellant's joining the Company, the management was of the view that he could not fit in the Company's culture.

b. In the termination meeting on 10 July 2016 (the '**Termination Meeting**'), the Appellant agreed to terminate his employment and did not come back to office since then despite his last working day being 31 July 2016.

c. A Separation Agreement II and a Final Salary Payment Breakdown attached to Separation Agreement II were prepared for his signature subsequent to the Termination Meeting. Although the Company had requested the Appellant to sign on both documents, he did not do so. However, the $2,376,515.21 was remitted to the Appellant despite both documents remained unsigned as the Company was obliged to pay Appellant not later than 7 days from the end of wage period.

d. The termination package including the terminal award was negotiated during the Termination Meeting. Details of which had been documented in the Separation Agreement II and the Final Salary Payment Breakdown.

e. The Company agreed to pay 6 months' housing allowance (including 3 months' payment in lieu of notice plus 3 months' special payment) to the Appellant as part of the separation package. The special payment was made in view of his contribution to the Company and to settle the employment termination in a smooth and friendly manner.

f. The Final Salary Payment Breakdown, which contained the following particulars:

Nature	**Details**	**Amount ($)**
Salary	1-7-2016 – 31-7-2016	258,672.00
Housing Allowance	1-7-2016 – 31-7-2016	45,000
Outstanding Annual Leave	12 days	101,772.59
Three months' notice payment	(Salary + Housing) x3	911,016
Special Payment	(Salary + Housing) x3	911,016
Year end bonus	213 days	150,538.62

26. Upon review, the Assessor did not accept the Appellant's computation of the assessable amount. In a letter dated 13 September 2018, the Assessor informed the Appellant that the sum of $1,552,032 was considered assessable for two reasons:

a. in view of the Appellant's past contribution to the Company and the Company would like to settle the termination in a friendly and smooth manner; and

b. the payment in lieu of notice.

27. In the same letter, the Assessor also proposed the following revised tax computation for the year of assessment 2016/17:

	$
Income	2,839,030 Salary (1,034,688) Leave (101,722) Payment in lieu of notice (776,016) Special Payment (776,016) Year-end bonus (150,538)
Housing Allowance	270,000
Value of place of residence provided	310,903
Less: Retirement Scheme Contribution	6000
Less: Allowances (Basic)	132,000
Less: Allowances (Single Parent)	132,000
Less: Allowances (Child)	100,000
Net chargeable income	3,049,933
Tax Payable at standard rate	492,089

28. On even date, the Assessor sent a letter to the Company requesting additional information regarding the place of residence provided to the Appellant for the period from 1 April 2016 to 31 July 2016.

29. On 21 September 2018, the Appellant sent a letter to the Assessor objecting to the revised assessment and advancing the following contentions:

a. The sum of $1,552,032 and the sum of $270,000 were compensation for the abrogation of his rights in the separation agreement[3] and other orally agreed obligations with the Company.

b. He fulfilled the requirements of the separation agreement[4] and met the other additional obligations agreed with the Company.

c. He did not personally sign the separation agreement[5] based on advice from non-qualified tax advisors.

d. The total six months' compensation recognized his lost employment opportunities with potential competitors ('**non-compete**') and additional obligations, and should considered non-taxable.

30. On 21 September 2018, the Company sent a letter to the Assessor enclosing rental receipts, Separation Agreement II, Final Salary Payment Breakdown attached to

[3] *ibid*.
[4] *ibid*.
[5] *ibid*.

Separation Agreement II and the additional Notifications Form (IR56F) filed on 8 March 2018 and advanced the following information:

a. Information on the amount of rent paid to landlord by the Appellant was based on the rental receipts issued by the landlord.

b. It was part of the separation package of Separation Agreement II that following termination of the employment contract the housing allowance would continue to be payable up to 31 January 2017.

c. The Company would pay $450,000 to the Appellant whether he rented a place of residence or not.

d. $169,648.91 was paid to the Appellant as the shares rewarded.

31. On 29 October 2018, the Assessor sent a letter to the Company requesting additional information regarding the report of these other rewards, eg the shares amount of $1,169,648 for the year of assessment 2017/18.

32. On 6 November 2018, the Company sent a letter to the Assessor enclosing the Appellant's 'B' Share Statement, and the two documents attached to the additional Notification Form (IR56F) filed on 8 March 2018 and advanced the following information:

a. The Appellant as the Position A was eligible to participate in the 'B' Shares Stock Program annually.

b. The programme was not granted to him because of his termination of employment in the year of assessment 2016/17.

c. The right to vest B Shares was exercised with the shares transferred to the Appellant on 1 March 2018 at $1,169,648 and was reported in the additional Notifications Form (IR56F) filed on 8 March 2018 as the exercise date falls into that assessment year.

33. On 23 May 2023, the Assessor sent a letter to the Company requesting additional information regarding the Appellant's Salaries Tax Assessment for the year of assessment 2016/17.

34. In response to the Assessor's further enquiries, the Company sent an email to the Assessor on 1 August 2023 providing, among others, the following information:

a. In the Termination Meeting, the Company agreed to terminate the Appellant's employment by mutual consent though the underlying reason for such termination is that the management was of the view that the Appellant could not fit in the Company's culture. The termination of employment by consent was made for the good sake of the Appellant's future career development. The Company had asked the Appellant's to provide a resignation letter, but such letter was never tendered by him.

b. The annual base salary of Hong Kong employees was paid by 13-month instalments. The 13th month salary was named 'Year-End-Bonus' in the Company's remuneration structure which was a guaranteed one month's basic salary. Employees who left the Company would be entitled to a pro-rated Year-End-Bonus. Therefore, the Taxpayer was entitled to the Sum-YEB.

c. The special payment was made in accordance with Clause 14.2 of the Employment Agreement but also for the purpose of recognizing the Appellant's past contribution and for settling the termination in a smooth and friendly manner.

35. In the email to the Assessor, the Company also enclosed documents relating to the Appellant's vested 'B' Shares.

36. On 23 May 2023, the Assessor sent a letter to the Appellant requesting for additional information regarding his objection.

37. In furtherance of the objection, the Appellant sent a letter and submitted a document entitled 'Separation Agreement' which was signed by both the Appellant and the Company (the '**Separation Agreement III**') on 13 June 2023 to the Assessor, and advanced the following:

a. Without prior notice, he was asked to meet the Position C on July 10, where he was informed of his immediate termination.

b. The Employment Agreement had no restriction on non-compete and non-solicitation.

c. The non-compete clause in Clause 9 of the separation agreement[6] prevented him from serving any the Company's customers, as the Company was a global market leader with clients across various industries. This effectively prevented him from participating in the market and competing using his skills.

d. The separation agreement[7] included provisions that restricted him from suing, competing, soliciting, and disclosing information to other companies he had worked with. In return, the Company agreed to provide assistance with his transition.

e. After being informed of his termination, he was upset and considered filing a lawsuit, as the reasons given by Mr B for the termination were

[6] *ibid*.
[7] *ibid*.

unclear and unjustifiable. However, after receiving the termination agreement and further consideration, he decided not to proceed with the intended lawsuit.

f. Upon receiving the request from the Assessor to present additional documents, he found the signed copy of the Separation Agreement III and submitted the original for examination.

g. He did not submit any resignation letter to the Company.

h. He also provided a copy of the signed Separation Agreement III, which stated an amount of $2,511,462.03.

38. Despite the Appellant's objection, the Respondent maintained its view in the Determination that the Sums and the 2016 Stock Award are taxable. The Respondent considered the Salaries Tax Assessment for the year of assessment 2016/17 should be as follows:

	$
Income	3,890,010
Net Assessable Income	3,520,430
Tax Payable thereon (at standard rate and after tax reduction)	562,664

39. On 5 February 2024, the Appellant lodged a Notice of Appeal against the Determination with the Board by sending an email to the Assessor. The email included a copy of the Notice of Appeal as well as a document titled 'Final Salary Payment Breakdown'.

40. The ground of appeal raised by the Appellant in the Notice of Appeal was that the Respondent had relied on incorrect facts and information to come up with the conclusions in the Determination. The specifics of these grounds of appeal will be detailed in paragraph 48 below.

41. The Appellant submitted further documents including 2 awards, three bonus confirmation statement and a letter from Company on 5 July 2024, and advanced the following:

a. In July 2016, the Position C informed the Appellant of the termination of the Employment Agreement, and they agreed 31 July 2016 as the last working day.

b. The Appellant initially considered suing the Company, feeling he was treated unfairly, but decided against it due to the lengthy and costly process.

c. The Appellant signed the separation agreement, which included cash compensation and modified use of the company car.

d. In the following months, the Appellant tried to move past the negative experience, which may have led to confusion in the information provided to the IRD later.

e. Upon receiving the tax assessment, the Appellant objected, as the Sums were compensation from the separation package, including non-compete payments.

f. The Company clearly stated in a letter that the final payment was not a severance payment (ie not according to the Employment Agreement) but as part of the separation agreement/package and that the letter was already provided to the IRD.

D. Findings of the Determination

42. The facts on which the Determination made in relation to the Sums was based are summarized below.

43. Since there was no evidence presented by the Appellant to demonstrate otherwise or to show how the Company had fulfilled its contractual obligation to terminate the employment without notice, it is found that PILON was made by the Company pursuant to Clause 14.1 of the Employer Agreement to terminate the employment.

44. As confirmed by the Company in response to the Assessor's inquiries, the Appellant was released from the Company without cause but by mutual agreement. Therefore, the Company was contractually obliged to make the payment mentioned in Clause 14.2 of the Employment Agreement to the Appellant. As a result, it was found that the SUM-OP, amounting to three months of the Appellant's salary and housing allowance, was clearly a payment made under the Employment Agreement.

45. It was found that the Sum-YEB effectively represented the guaranteed 13th month salary payable to Hong Kong employees, including those who left the Company during the year on a pro-rata basis. This should be distinguished from the discretionary bonus outlined in Clause 5.5 of the Employment Agreement and Clause 3 of the separation agreement[8].

46. The Appellant's contention regarding a 'non-compete' clause in the separation agreement[9], purportedly restricted his ability to compete and practise his skills post-employment, was not accepted. In the Determination, it was held that the outline obligations are apparent common law obligations typically expected of employees in senior management roles. Additionally, the Determination highlighted the lack of conclusive

[8] *ibid*.
[9] *ibid*.

evidence supporting the Appellant's assertion that any portion of the remuneration was designated to fulfill the alleged restrictive covenants.

47. The Determination also highlighted the inconsistency on the Appellant's own accounts regarding the separation agreement. Initially, when the Appellant was enquired, the Appellant stated that he decided not to sign Separation Agreement I because he disagreed with the terms. However, he later claimed to have located Separation Agreement III, which he had signed in 2016, but of which the Company had no knowledge. The Determination further commented that if Separation Agreement III were intended to be given effect, the Appellant would not have received without complaint a payment (ie $2,376,515.21[10]) that was less than $2,511,462.03 as appeared on such agreement.

E. Appellant's Grounds of Appeal and His Case

48. In the Notice of Appeal against the Determination lodged by the Appellant, his central argument was that the Determination relied on what he described as incorrect facts and information, in particular:

a. The Determination incorrectly concluded that the reason for cessation was resignation when in fact it was due to termination by mutual agreement based on Separation Agreement III.

b. The Determination incorrectly stated that the Appellant did not sign Separation Agreement I because he disagreed with its terms. According to the Appellant, he signed Separation Agreement I after initially considering a lawsuit and wanting to consult a legal advisor, but ultimately decided not to file a lawsuit. He also mentioned that there was no reason not to sign, as he was prepared to accept and comply with the terms and conditions. In fact, he fulfilled the obligations outlined in the separation agreement[11].

c. The Determination incorrectly concluded[12] that the payment he received was severance pay of six months, whereas the true purpose of the payment was compensation for all obligations to the Company listed in the separation agreement[13].

d. The Determination's view on PILON, Sum-OP, and Sum-YEB was incorrect, as these were compensation for acceptance of and compliance with the terms and conditions of the separation agreement[14], and should not be considered as taxable income.

[10] See paragraph 63 below.
[11] See footnote 1 above.
[12] At point (9)(a)(v) of the Determination.
[13] See footnote 1 above.
[14] *ibid*.

e. The Determination incorrectly concluded that the Appellant could not have received a payment lesser than the amount agreed upon in the Agreement. The Appellant explained that compensation of $2,514,515.21 was the agreed amount, which included compensation of $138,000 for the early-return of the company car. However, the Appellant and the Company later agreed that he would forgo the $138,000 car compensation and continue using the car. As a result, the actual payment the Appellant received was less than the $2,514,515.21 stated in Separation Agreement I, due to his forfeiture of the $138,000 car compensation.

49. The Appellant on 15 July 2024 submitted an Opening Statement and advanced the following:

a. The Appellant is a senior international executive with over 25 years of successful experience. He joined the Company as the Position A in 2014.

b. The Appellant was informed by the Position C during the Termination Meeting that his employment with the Company was terminated immediately. This was a significant shock, particularly since the Position C had praised his leadership, commitment, and performance in managing the Company's business just a few months earlier.

c. During the Termination Meeting, the Position C suggested the Appellant consider resigning instead, as termination could adversely affect his employment record and future reference checks. Concerned about his career prospects, the Appellant agreed to a mutually accepted separation arrangement with the Position C.

d. The separation agreement[15] stated that the Appellant would receive compensation equivalent to six months and 21 days of his salary, with all terms clearly documented. The Appellant stated that this arrangement was confirmed by the Company in a letter submitted to the Assessor on 15 March 2018 through the tax advisor.

e. The Appellant stated that he was unable to consult an advisor before the Termination Meeting and did not receive adequate professional advice during it. He felt he was treated unfairly throughout the termination process and considered pursuing legal action against the Company. However, he ultimately decided against it, believing that the legal process would be lengthy, complicated, and costly. Consequently, he signed the Separation Agreement and returned a fully signed copy to the Company.

[15] *ibid*.

f. The Appellant noted that the separation agreement[16]includes restrictive obligations, such as a non-solicitation clause in Clause 9 and a non-sue clause in Clause 10. Therefore, the payment he received was in exchange for his agreement to refrain from competing with the Company after his departure, rather than for services rendered during his employment.

g. The Appellant also mentioned that the Company confirmed these obligations in the separation agreement and that he had not breached them.

50. In the Opening Statement, the Appellant also explained the reasons for the existence of three versions of separation agreement[17] in which their respective amounts of compensation and signatures were different:

a. After an agreement was reached in the Termination Meeting, two copies of the Separation Agreement with different signatures were sent to the Appellant.

b. To facilitate his consultation regarding the separation agreement[18], he made several copies and provided Separation Agreement I to his advisors, who advised him not to sign it until he decided whether to pursue legal action.

c. Ultimately, he chose not to take legal action against the Company and signed the copies of Separation Agreement I he had made, returning one to the Company.

d. Separation Agreement I was honoured, and the final payment was made according to its terms.

e. He acknowledged that he had confused himself when he informed the officers that he did not have the original copy of Separation Agreement I.

F. The Testimony of the Appellant

51. Apart from the facts referred to above, the Appellant gave evidence during the hearing before this Board.

52. The Appellant holds a bachelor’s degree in Chemistry from University D, as well as a master’s degree in Science from the University E, City F, Country G, and a master’s degree in Nuclear Engineering from University H.

[16] *ibid*.
[17] *ibid*.
[18] *ibid*.

53. Prior to joining the Company, the Appellant served as the Position J of Asia for Company K. He joined the Company in 2013 as the Position A for the Asia Pacific region, where he was responsible for overseeing the entire organization in that area.

54. He expressed his surprise that the Position C handed him the termination letter, as he had been one of the top performers in the Asia-Pacific region and had successfully led operations to achieve growth.

55. The Position C informed him that the decision to terminate his employment had already been made. He attempted to persuade the Appellant to resign, suggesting that it would be better for his future career, as being terminated could raise doubts with potential companies.

56. The Appellant testified that he felt a mix of disappointment at being terminated despite his strong performance. However, he appreciated the Position C's concern and willingness to serve as a reference for him. This consideration contributed to the negotiation of a separation package between the Position C and the Appellant during that meeting.

57. According to the Appellant, the negotiation process was back-and-forth, but ultimately, an agreement was reached.

58. After the meeting, the Appellant realized that he had agreed to non-solicitation, non-compete, and non-litigation obligations. He understood that had he received proper legal advice, he could have negotiated for more, as he later recognized that his termination was unjust after consulting with professional contacts.

59. The Appellant further testified that he considered filing a lawsuit against the Company for unfair treatment. However, he ultimately decided against it due to the high costs and potential consequences of pursuing legal action, which he could not afford.

60. Regarding the separation agreement[19], the Appellant stated that he received two different versions following his meeting with the Position C. The Separation Agreement I included a total payment of $2,514,515.21, which was executed and signed by a representative of the company and bore the company seal. The Appellant indicated that he signed the original copy but did not submit it to the Board in his Notice of Appeal due to time constraints while preparing his documents. He submitted the original copy of Separation Agreement I as an exhibit, marked as Exhibit A1.

61. The Appellant explained that the discrepancy in the final payment compared to the amount specified in the separation agreement[20] arose because of the subsequent agreement entered into in relation to the use of a car that the Appellant was provided by the Company. Initially a car allowance was intended to be paid as cash compensation. Ultimately, he decided to retain the car, resulting in a deduction of $138,000 from the stated amount.

[19] *ibid*.
[20] *ibid*.

62. Additionally, the Appellant mentioned that he received Separation Agreement III containing all the same information as Exhibit A1, but reflecting a different figure of $2,511,462.03. This document also bears the signature of a company representative and features the company seal. The Appellant submitted this original copy as an exhibit, marked as Exhibit A2.

63. The Appellant confirmed that the final payment he received amounts to $2,376,515.21, ie the total amount set out in Separation Agreement II.

64. Under cross-examination, the Appellant stated that he did not recall the date on which he signed Separation Agreement III, but he believed the date next to his name indicated when he signed the document. He also mentioned that he thought the document was returned to the Company after he signed it, but he could not remember the date or the method of return.

65. He further clarified that, although he confirmed the final amount paid to him is $2,376,515.21, he reiterated that no consensus was reached between him and the Company. He noted that this amount was confirmed following a conversation with a staff member from the Human Resources Department via phone call. During the call, it was established that he would keep the car instead of receiving compensation for the car allowance. While the Appellant could not specify when this phone call occurred, he believed it was after he received the separation agreement and the breakdown, but he could not confirm whether it was before or after he signed Separation Agreement III.

66. Under cross-examination, the Appellant confirmed that when Separation Agreement III was signed by both the Company and himself, both parties honoured the Separation Agreement III. He reiterated that the amount he received from the Company was $2,514,515.21 and explained that the discrepancy between this final payment and the specified amount was due to the deduction of the car allowance.

67. Under cross-examination, the Appellant confirmed that he had already received the amount of $2,376,515.21 in April 2017. He also confirmed that on the date he signed Separation Agreement I, he was aware of the difference between the actual amount paid and the amount specified in the Separation Agreement I.

68. He confirmed that he was aware of clauses 14.1, 14.3, and 14.4 in the Employment Agreement. However, he thought that the Company terminated him without good reason, as he had been performing well in his position.

69. The Appellant also mentioned that while he was working at the Company, he was involved in some of the termination of the employee in the Asia-Pacific region. During that time, he was not aware of the Company having a policy of entering into separation agreements with colleagues exiting the company.

G. Disputed Facts

70. The key disputed facts are summarized below:

71. The Appellant contends that the Sums were the cash compensation for agreeing to the terms in the separation agreement[21]. However, the Company made it clear that the payments were made in accordance with the terms of the Employment Agreement. The Company stated that the special severance payment was made for the purpose of recognizing the Appellant's past contribution and settling the termination in a smooth and friendly manner.

72. The Appellant contends that he considered filing a lawsuit as he thought the reason for the termination given by the Company was unjustifiable. However, the Company contends that the underlying reason for the termination of the Appellant's employment is that the management was of the view that the Appellant could not fit in the Company's culture. The termination of employment by consent was made for the good sake of the Appellant's future career development. The Company had asked the Appellant to provide a resignation letter but such letter was never tendered by him.

73. The Appellant was of the view that his outstanding leadership and performance delivered lots of success for the years that he was in charge.

74. The Appellant suggests that the Sums were the compensation for the abrogation of his rights in the separation agreement[22] and other obligations he had agreed orally with the Company. While the Commissioner suggests that no obligations were created under the separation agreement[23], but all are common law duties that the Appellant had long been subjected to.

H. Decision

Non-compete and non-solicitation obligations

75. It is the Appellant's case that he was not subject to any non-compete or non-solicitation restrictions during his employment with the Company, as outlined in the Employment Agreement. Therefore, upon entering into Separation Agreement I with the Company, he became bound by the stated terms prohibiting him from competing and from soliciting employees who had worked under him.

76. It is well established that an employee owes to his employer a duty of good faith and fidelity throughout the course of employment. Even in the absence of explicit contractual terms, courts will imply such a duty (Robb v Green [1985] 2 QB 315). As the Position A, the Appellant clearly owed fiduciary duties to the Company.

77. Furthermore, Clause 10 of the Employment Agreement states, '*In addition to common law duties, the Appellant neither during his employment nor after termination shall use or disclose any trade secrets or confidential information relating to or belonging to the Company or its associated companies.*' The expression '*in addition to common law duties*'

[21] *ibid*.
[22] *ibid*.
[23] *ibid*.

reaffirms that the Appellant's responsibilities extend beyond mere confidentiality obligations. Therefore, there is no doubt that the Appellant was also subject to fiduciary duties along with the duty of good faith and fidelity imposed by common law. These duties were to persist after termination of the Employment Agreement.

78. Consequently, the Appellant's fiduciary duty and duty of good faith would almost invariably be breached if he engaged in competition with his employer or solicited Company employees to leave while he was still under contract with the Company.

79. Therefore, the Board finds that Separation Agreement I, executed between the Appellant and the Company, did not introduce new non-compete or non-solicitation obligations. The express terms of Separation Agreement I do not impose additional restrictions on the Appellant. Instead, they merely reaffirm the existing common law duties and confidentiality obligations that were expressly provided in, or incorporated into, the Employment Agreement.

80. Furthermore, there is a lack of evidence presented by the Appellant to support his claim that during the course of his employment he was not subject to those post-employment restrictive obligations that he alleges.

81. In any event, for the reasons set out below, it is not strictly necessary to determine this issue as the Sums are amounts which the Company was obliged to pay the Appellant in any event pursuant to the Employment Agreement.

***Termination without cause or termination based on separation agreement*[24]**

82. The Company's position is that while it agreed to terminate the Appellant's employment by mutual consent, the underlying reason for this decision was management's assessment that the Appellant did not fit in the Company's culture. The mutual consent for termination was intended to benefit the Appellant's future career development. In contrast, the Appellant contends that the cessation of employment was due to termination by mutual agreement based on the separation agreement[25]. Therefore, he argues that the sums paid were compensation for the restrictive obligations imposed by the separation agreement[26] and were not payments made by the Company under Clause 14 of the Employment Agreement. Essentially, he asserts that the termination was the result of his voluntary resignation.

83. While the Appellant disagreed with the Company's view on the nature of the sums, he confirmed in his testimony and in the Opening Statement that he felt a mix of disappointment and appreciation. He was disappointed because he believed he was terminated despite his strong performance. Nevertheless, he appreciated that his seniors were willing to classify the termination as a resignation.

[24] *ibid*.
[25] *ibid*.
[26] *ibid*.

84. Based on the above, the Board finds that the Appellant effectively agreed with the Company's classification of his departure as a termination without cause and that it was by mutual consent for the benefit of the Appellant's future career that the termination was described as resignation. Therefore, the Board is not satisfied that the departure resulted from a voluntary resignation. The evidence presented does not sufficiently support the Appellant's assertion that his resignation was voluntary, as the circumstances surrounding the termination indicate that it was primarily driven by the Company's assessment and decision.

Discrepancy in the Amount Received by the Appellant and Figure stated in Separation Agreement I

85. Regarding the discrepancy between the amount stated in Separation Agreement I, which was $2,514,515.21, and the actual amount received from the Company, that is $2,376,515.21, the Appellant explained that the compensation of $2,514,515.21 stated in Separation Agreement I was the amount that both parties had discussed and agreed upon. This agreed amount included compensation of $138,000 for the earlier return of the company car. However, the Appellant and the Company later agreed that the Appellant would forgo the $138,000 compensation and continue using the company car. As a result, the actual payment the Appellant received was less than the $2,514,515.21 stated in Separation Agreement I, due to the Appellant forfeiting the $138,000 car compensation.

86. As previously noted, the Board finds that the Appellant's departure of the Company is classified as a termination without cause. Consequently, in accordance with Clause 14.2 of the Employment Agreement, the Company is obliged to provide base salary, housing allowance, car allowance, and medical insurance to the Appellant. The Board accepted the Appellant's contention that, although the agreed amount of $2,514,515.21 included compensation for the car allowance, subsequent negotiations resulted in the Appellant agreeing to forgo the $138,000 car allowance in exchange for the continued use of the company car. Therefore, while the Company compensated the Appellant in accordance with Clause 14.2, Sum-OP now reflects only three months of base salary and three months of housing allowance, as the car allowance was not included in the Sum-OP due to the Appellant's continued use of the company car.

Compensation Paid to Appellant Prior to Receiving the Duly Signed Separation Agreement

87. According to the Company's record and explanation, the Appellant was paid a total of $2,376,515.21 before the Company received a duly signed and executed separation agreement from the Appellant because the Employment Ordinance requires that employees be paid within seven days following the end of the wage period. The Appellant also confirmed in his testimony that he received this payment prior to signing the separation agreement.

88. The Board finds that this arrangement does not support the Appellant's claim that the payment was made as consideration for signing the separation agreement, particularly since the Company never received a signed version. Instead, it reinforces the

Company's position that the payment was made in accordance with legal obligations then existing.

Discrepancy in the Appellant's case regarding the three versions of Separation Agreements

89. The Board observes significant inconsistencies in the Appellant's case concerning the three versions of the separation agreement[27]. The Appellant claims that the final amount agreed upon with the Company was $2,514,515.21, which contradicts his earlier submissions to both the Assessor and the Board.

90. Previously, he indicated, in an email to the Assessor dated 8 January 2018, and in a letter to the Assessor on 21 September 2018, that he chose not to sign Separation Agreement I due to concerns about increased legal and tax liabilities. However, he later alleged that he discovered a signed copy of the separation agreement (ie Separation Agreement III) on 3 June 2023. Furthermore, despite expressing feelings of being unfairly treated and considering legal action, he ultimately confirmed in his Opening Statement that he signed Separation Agreement III and that it was honoured.

91. Additionally, during his testimony, he mentioned that Separation Agreement III, which specified the amount of $2,511,462.03, is duly recognized by both parties. The Board finds that these contradictions raise serious questions over the reliability of the Appellant's statements.

92. Nevertheless, whether the agreed amount should be $2,511,462.03 or $2,514,515.21, on its own, does not impact the issue in the current appeal, as the Appellant confirmed in his testimony that the differences arise from 0.36 days of unused outstanding annual leave, which is unrelated to the Sums.

True Purposes of the Sums

93. The Board should consider each of the payments that constitute the Sums individually for determining the respective purposes of these payments and for answering the question of whether, in substance, they were 'income from employment' or for 'something else'.

94. Based on our analysis below, the Board's answer to the question is that the Sums were income from employment and are taxable.

95. On the Appellant's own case, the separation agreements[28] which were provided to him by the Company each had a 'Final Salary Payment Breakdown' attached. The 'Final Salary Payment Breakdown' describes the payments made. The PILON, referred to as 'three months' notice payment' in the Final Salary Payment Breakdown, was paid by the Company pursuant to Clause 14.1 of the Employment Agreement to effect termination by providing a payment in lieu of notice. While it is not disputed that the termination was

[27] *ibid*.
[28] *ibid*.

effected without three months' notice, the Company is contractually obliged to honour such terms. The Appellant failed to discharge his burden of adducing evidence to prove otherwise. Therefore, the Board agrees with the Determination that if PILON were not a payment in lieu of notice, the Company would not have fulfilled its contractual obligation to terminate the employment without providing the requisite notice.

96. The Sum-OP, referred to as 'Other Payment' in the Final Salary Payment Breakdown, amounted to three months of the Appellant's salary and housing allowance[29]. In response to the Assessor's query, the Company explained that such payment was in accordance with Clause 14.2 of the Employment Agreement. Whilst it was agreed that the termination of employment could be described as termination by mutual consent, it did not change the true nature underlying the termination. The compensation payment therefore comes within the scope of Clause 14.2 of the Employment Agreement. The Appellant failed to provide evidence to prove otherwise, and thus the Board agrees with the Determination on the true purpose of the Sum-OP.

97. The Sum-YEB, which is described as 'Year End Bonus' in the Final Salary Payment Breakdown, was explained to be a pro-rated guaranteed 13th-month salary payable to the Appellant. As previously mentioned, the burden of proof rests with the Appellant in this matter. He failed to provide any particulars or adduce evidence to contest this.

98. Consequently, the Board is of the view that there is insufficient evidence adduced by the Appellant to conclude that the PILON, Sum-OP and Sum-YEB should not be classified as taxable salaries under the Ordinance.

I. Board's views on Appellant's Grounds of Appeal

99. In the Board's view, the first seven grounds of the Appellant's grounds of appeal are his own interpretation of the facts or analysis based on which the tax assessment was made. They are without merits and do not provide sufficient basis for overturning the findings of the Determination.

100. As regards the eighth ground, the Board considers that concerns raised regarding the $138,000 do not affect the substance of the Sums at issue in the appeal.

J. Conclusion

101. By reasons of the above, this Board determines that the Appellant has failed to discharge his burden of proof under section 68(4) of the Ordinance to show that the Salaries Tax Assessment for the year of assessment 2016/17 imposed on him was excessive or incorrect.

102. The Appellant's appeal is dismissed.

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[29] The car allowance covered by Clause 14.2 was provided to the Appellant as a benefit in kind by allowing him to have continued use of the car.

103. The Deputy Commissioner of Inland Revenue's Determination that the salaries tax payable being $562,664 for the year of assessment 2016/17 is affirmed.

104. Pursuant to section 68(9) of the Ordinance, the Appellant is ordered to pay costs of the Board at the sum of $20,000.