

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D12/92

Salaries tax – ex-gratia payment on termination of employment – whether subject to salaries tax.

Panel: William Turnbull (chairman), Charles Hui Chun Ping and Norman Leung Nai Pang.

Date of hearing: 29 April 1992.

Date of decision: 8 June 1992.

The taxpayer had been employed all his working life by one company. After working for some 40 years with the same employer, his employer closed his business. An ex-gratia sum of HK\$500,000 was paid to the taxpayer. This sum was assessed to salaries tax and the taxpayer appealed to the Board of Review. He submitted that the ex-gratia payment of HK\$500,000 was required by him to support himself and his family for the rest of his life.

Held:

Under tax law in Hong Kong ex-gratia payments made to an employee at the end of a contract of employment are subject to salaries tax unless they are made out of an approved provident fund. Accordingly the ex-gratia payment had been correctly assessed to salaries tax.

Appeal dismissed.

Amy Wong for the Commissioner of Inland Revenue.

Taxpayer in person.

Decision:

This is an appeal by a taxpayer against a salaries tax assessment for the year of assessment 1989/90. The facts of the case are quite simple and were not in dispute. They are as follows:

1. The Taxpayer spent all of his working life employed by one company with his continuous service commencing at the beginning of 1950 and ending in early 1990, a working life of some forty years in the employment of the same company.

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2. At the time of the cessation of the employment of the Taxpayer he was the treasurer of his employer.

3. Unfortunately for the Taxpayer his employer closed down his business with the result that the employment of the Taxpayer was terminated. If the employer had continued in business it would have continued to employ the Taxpayer but the Taxpayer was now too old to seek or obtain alternative employment and it is not anticipated that he will be able to obtain employment in the future.

4. In view of the long and loyal service of the Taxpayer his employer agreed to pay an ex-gratia sum of \$500,000 to the Taxpayer. Because it was an ex-gratia payment and not paid to the Taxpayer from an approved provident fund or retirement scheme the assessor assessed to salaries tax this sum of \$500,000 in the final year of employment of the Taxpayer.

5. The Taxpayer objected to the sum of \$500,000 being so assessed to salaries tax. The Commissioner by his determination dated 7 January 1992 confirmed the assessment and the Taxpayer appealed to the Board of Review. At the hearing before the Board of Review the Taxpayer appeared in person.

The Taxpayer outlined the facts which we have set out above and which were not challenged by the representative for the Commissioner. He asked the Board if in the circumstances of his case it would be possible for the Board to order that the gratuity of \$500,000 should be exempted from salaries tax. He explained that he could not obtain alternative employment and that the \$500,000 formed part of the monies which would be necessary to support him and his family for the rest of his life.

The representative of the Commissioner was not asked to make a detailed submission but confirmed to the Board that as a matter of law a payment which is not damages for breach of contract and which is not paid out of an approved provident fund or retirement scheme is subject to be assessed to salaries tax if it is paid in respect of the services provided by the Taxpayer to his employer.

The Board has total sympathy for the Taxpayer. Retirement benefits are a major subject of debate and discussion by our government, our legislators and pressure groups. There is a major debate taking place about whether or not the so-called 'sandwiched' middle class should be subject to salaries tax and whether the tax threshold should be substantially increased. Arguments are put forward that employers should be responsible and take care of their employees in their old age. It is pointed out that if statutory arrangements are not made the burden will eventually fall on the government and public revenue. It seems inconceivable in the light of all of this that our taxation law should require that when an employer goes out of business leaving behind an employee with some forty years of loyal service, and a comparatively modest ex-gratia payment of \$500,000 is made, that payment to be subject to tax only because the employer did not establish an approved provident fund or retirement scheme. Unfortunately for the Taxpayer that is the state of our law and neither the Commissioner nor this Board has any discretion in the

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matter. We are not allowed to investigate to see whether or not the payment is in fact reasonable and whether or not it would have been capable of approval if the employer had sought to establish an approved retirement scheme.

As it is clear that the payment of \$500,000 is subject to salaries tax and that we have no discretion in the matter, we have no option but to dismiss the appeal and confirm the assessment against which the Taxpayer has appealed.

We add a rider to this decision suggesting that our legislators might give this matter their urgent consideration with a view to changing the law if it is felt, as we do, that there is injustice in the system.