Case No. D25/10

Salaries tax – refund of rent – sections 8(1), 9(1), 9(1A), 9(2), 66(1), 66(1A), 68(2D) and 68(4) of the Inland Revenue Ordinance ('IRO').

Panel: Colin Cohen (chairman), Wendy Wan Yee Ng and Young Yee Kit Jessica.

Date of hearing: 20 August 2010.
Date of decision: 27 September 2010.

The taxpayer, an employee of Company A, was eligible to obtain rental reimbursement under Company A's Rental Reimbursement Scheme. The taxpayer did not submit the relevant application and therefore Company A was not able to exercise control or to ensure that part of the taxpayer's salary was actually expended on rent. Company A did not treat the relevant Sum paid to the taxpayer as a refund of rent.

Held:

Although the Board is sympathetic to the taxpayer's position and the fact that had she completed the relevant form, she would have been entitled to obtain the benefits of the Scheme. This, however, does not entitle the Board to come to the conclusion that the assessment is incorrect or wrong. The Board has no hesitation in concluding that the Sum was not a refund of rental within the meaning of section 9(1)(a) of the IRO.

Appeal dismissed.

Case referred to:

CIR v Peter Leslie Page 5 HKTC 683

Taxpayer in absentia.
Leung To Shan for the Commissioner of Inland Revenue.

Decision:

Introduction

1. The Taxpayer wrote to the Board on 16 July 2010 and drew to our attention that she does not currently reside in Hong Kong nor will she be in Hong Kong in the near future. She resides in Toronto, Canada. She therefore asked that the Board consider hearing her appeal in her absence without an authorized representative pursuant to section 68(2D) of the Inland Revenue Ordinance ('IRO').

2. We agreed to allow her to do so.

Late appeal

3. The Determination issued by the Acting Deputy Commissioner of Inland Revenue was dated 17 March 2010 ('the Determination'). However, her notice of appeal was not received by the Clerk to the Board of Appeal until 20 April 2010.

4. However, the Inland Revenue Department ('IRD') wrote to the Taxpayer on 11 August 2010 confirming that the Determination was only delivered to the Taxpayer on 25 March 2010 and as such, took the position that they would not oppose an application for a late appeal.

5. The Board having regard to section 66(1) and section 66(1A) of the IRO was satisfied that this was a suitable case to grant an extension of time. Hence, we did so.

The issue

6. The issue that we need to decide is whether the sum of $174,000 ('the Sum') that was received by the Taxpayer from Company A, her employer for the year ended 31 March 2007 is a salary chargeable to tax pursuant to section 9(1)(a) of the IRO or a refund of rent within the meaning of section 9(1A)(a) of the IRO.

The facts

7. We accept that the Taxpayer has not challenged any of the relevant paragraphs upon which the Determination was arrived at and as such, we find them as facts. They are as follows:

> ' (1) ["The Taxpayer"] has objected to the Salaries Tax assessment for the year of assessment 2006/07 raised on her. The Taxpayer claims that part of her income was a refund of rent and should not be assessable to Salaries Tax.
>
> (2) By letter dated 10 November 2005 ["the Employment Letter"], [Company A] offered the Taxpayer an employment as Fund Analyst – Investment Communications effective no later than 3 January 2006. The Employment Letter contained, among others, the following terms:

"**Remuneration Package**

Your initial remuneration package will be HK$700,000 per annum of which a maximum of 40% will consist of rental reimbursement …

Rental Reimbursement Program

Your total actual rental reimbursement is capped at a maximum of 40% of your overall remuneration package. If your claim for rental reimbursement is less than the maximum amount specified above, or you do not have any rental expenses incurred during the relevant period, any amount not used for rental reimbursement will remain as salary."

(3) At the relevant times, [Company A] established a Rental Reimbursement Scheme ["the Scheme"] for its staff.

(4) The Policy contained, among others, the following terms:

"**Claiming Procedures**

1) All eligible employees wishing to join or remain in this scheme must complete an application form before **4 May 2006** …

The application form should be completed in full, signed and returned … A copy of the **stamped lease agreement** … must be provided with the application form in order for the application to be considered.

2) Failure to provide both a properly completed application form and a copy of the stamped lease agreement will render your application automatically invalid and you will not be eligible to join the programme for the current tax year …

…

5) On or before 7 April of the following year, participants in the program must complete a claim form. You will be required to provide original receipts in your name substantiating rent, rates and management fee expenses actually incurred by you. This is necessary in order to substantiate the payments made to you during the year so that the employer's returns can be completed.

6) The employee is responsible for ensuring that the relevant forms and documentation to substantiate the claims are submitted on a timely basis. Late submissions will not be entertained …"

(5) [Company A] filed an employer's return in respect of the Taxpayer for the year of assessment 2006/07 and reported, among others, the following income particulars:

(a)	Capacity in which employed:	Fund Analyst
(b)	Period of employment:	1.4.2006 – 31.3.2007
(c)	Particulars of income	$
	Salary	700,008
	Bonus	105,000
		805,008
(d)	Place of residence provided	No

(6) The Assessor raised on the Taxpayer the following Salaries Tax assessment for the year of assessment 2006/07:

	$
Income [Fact (5)(c)]	805,008
Less: Basic allowance	(100,000)
Net Chargeable Income	705,008
Tax Payable thereon (after tax deduction)	108,451

(7) The Taxpayer objected to the above assessment. She asserted that:

"For the 2006/07 assessment, it does not include my rental reimbursement from my employer as noted in the previous tax year 2005/06. I am including a copy of my rental receipts from my landlord … which reflects an amount of rental reimbursement of HK$43,500 for 2005/06 and HK$174,000 for 2006/07."

(8) In support of her claim, the Taxpayer supplied copies of the following documents:

(a) Rental receipts for the period from 1 January 2006 to 31 March 2007.

(b) Tenancy agreement dated 24 December 2005. The term of the tenancy was from 1 January 2006 to 30 September 2007.

(9) In response to the Assessor's enquiries, [Company A] provided the following information:

(a) To participate in the Scheme, the eligible employee was required to follow the guidelines as set out in the Policy. According to the 'Claiming Procedures' section as set out in the Policy, the eligible employee had to submit the required documents, including stamped lease agreement and original rental receipt on a timely basis.

(b) For the year of assessment 2005/06, the Taxpayer had followed the Policy procedures and submitted all the necessary documents to the Company.

(c) As set out in the Policy, the eligible employee had to submit application on an annual basis for the Company's approval by the prescribed deadline. For the year of assessment 2006/07, the Taxpayer did not submit the application nor any relevant documents to the Company. As such, the Company was not in a position to exercise control to ensure that part of the Taxpayer's salary was actually expended in the payment of rent.

(10) The Assessor drew the Taxpayer's attention to [Company A's] reply that she did not participate in the Scheme for the year of assessment 2006/07. The Assessor then invited the Taxpayer to withdraw the objection. The Taxpayer declined to withdraw and put forward the following arguments:

(a) "While my employer, [Company A], has indicated that I did not participate in the Company's Rental Reimbursement Program in 2006/07 despite my participation for the 2005/06 period, it is my belief this was an administrative misunderstanding."

(b) "In January 2006 (approximate date of hire with [Company A]), I presented my employer with a copy of my 2-year rental lease agreement … as well as supporting documentation authorizing my inclusion in the Company's Rental Reimbursement Program. It was my understanding that since I was initially applying for the 2005/06 period that my Employer would also include me in the Rental Reimbursement Program for the 2006/07 period, which is for the entire duration of my 2-year lease agreement."'

The taxpayer's submissions

8. The Taxpayer by virtue of a notice of appeal dated 12 April 2010 asserts that she misunderstood the Rental Reimbursement Programme Policy ('the Policy') of Company A.

In short, she states that due to a misunderstanding, she did not realize that she was required to apply to remain in the Rental Reimbursement Scheme ('the Scheme') each year.

9. As can be seen from the facts, it is quite clear that the Taxpayer was employed by Company A when she took up her employment, she was able to take advantage of the Scheme and she submitted all relevant documents including a stamped tenancy agreement dated 24 December 2005 which was for a 2-year period running from 1 January 2006 to 30 September 2007. Therefore, due to her misunderstanding, she did not complete any forms to allow her to remain in the Scheme for the year of assessment 2006/07. She accepts that she did not complete any application, nor did she submit the rental receipts for the year ended 31 March 2007 to Company A. She was therefore not regarded by Company A as remaining as a participant in the Scheme.

The relevant statutory provisions

10. Section 8(1) of the IRO is the basic charging section for salaries tax and provides that salaries tax shall be charged on income from employment.

11. Income from employment is defined under section 9(1). The definition is non-exhaustive and states as follows:

> '*Income from any office or employment includes -*
>
> *(a) any wages, salary, leave pay, fee, commission, bonus, gratuity, perquisite, or allowance, whether derived from the employer or others, ...*
>
> *(b) the rental value of any place of residence provided rent-free by the employer or an associated corporation;*'

12. A place of residence shall be deemed to be provided rent-free by the employer if the employer paid or refunded all the rent therefor and such payment or refund shall be deemed not to be income. Section 9(1A) stipulates the following:

> '*(a) Notwithstanding subsection (1)(a), where an employer or an associated corporation –*
>
> *(i) pays all or part of the rent payable by the employee; or*
>
> *(ii) refunds all or part of the rent paid by the employee,*
>
> *such payment or refund shall be deemed not to be income;*
>
> *(b) a place of residence in respect of which an employer or associated corporation has paid or refunded all the rent therefor shall be deemed for*

the purposes of subsection (1) to be provided rent free by the employer or associated corporation;'

13. Section 9(2) provides that the rental value of any place of residence shall be deemed to be 10% of the income as described in section 9(1)(a) of the IRO after deducting certain outgoings and expenses.

14. Section 68(4) places on the appellant the burden of proving that the assessment appealed against is excessive or incorrect.

IRD's submission

15. Ms Leung on behalf of the IRD submitted to us that the question that we need to consider is the nature of the payment of the Sum. The issue she asserts is whether the Sum is a salary or a rental refund is a question of fact. She drew to our attention the decision of CIR v Peter Leslie Page 5 HKTC 683. We accept that the real test for us to determine the true nature of the payment is for us to look at the intention of the parties at the time of the payment of the money by the employer. Mr Recorder Edward Chan SC stated as follows:

> '*7. The crucial question is what is the nature of the payment of the sum of $410,040.00. This is a question of fact. The starting point is of course the contract between the taxpayer and the employer. If by the terms of the contract, the payment was to be in the nature of rental refund, then plainly due weight must be given to the contractual provisions. However in my view, although the terms of the contract are an important and weighty factor, this is not the sole factor. This is because (a) the parties may by their conducts vary the terms of the contract; or (b) even if the conducts do not amount to a variation of the terms of the contract, the parties' conducts may be such that the payment is not made in strict accordance with the terms of the contract and so the payment may be of a nature different from what is provided for in the contract.*
>
> *18. On the facts of the present case, the majority of the Board found that the payment of $410,040.00 by the employer was rent refund. The majority took the view that "the real test was the nature of the payment itself and this in turn depends on the intention of the parties at the time they entered into the contract of employment". While I agree that the terms of the contract is a very useful starting point and is a very weighty factor in deciding the nature of the payment, I think it would be wrong to say that the terms of the contract would be the sole test. Again while I agree that the intention of the parties is the real test, the relevant point of time is the time of the payment of the money by the employer and not the point of time when the parties entered into the contract of employment.*'

Discussion

16. It is therefore clear from the documents that we have had sight of that Company A through its representative by a letter dated 9 March 2010 stated as follows:

> '…..
>
> 1. The[Company A] group has established the Rental Reimbursement Scheme ("Scheme") for years and updated policy has been/will be distributed to eligible employees from time to time. As requested, copies of the Company's Rental Reimbursement Programme Policy ("Policy") for the years 2005/06 and 2006/07 are enclosed (Appendices A and B).
>
> 2. To participate in the Scheme, the eligible employee is required to follow the guidelines as set out in the Policy. According to the "Claiming Procedures" section as set out in the Policy, the eligible employee has to submit the required documents (including stamped lease agreement and original rental receipt) on a timely basis.
>
> 3. For the year 2005/06, [the Taxpayer] had followed the Policy procedures and submitted all the necessary documents to the Company. Copies of the following 2005/06 documentary evidences are enclosed for your reference (Appendix C):
>
> - The application form completed by [the Taxpayer] in January 2006;
> - The tenancy agreement;
> - The claim form completed by [the Taxpayer] in April, 2006; and
> - The rental receipt.
>
> 4. & 5. As set out in the Policy, the eligible employee needs to submit applications on an annual basis for the Company's approval by the prescribed deadline. For the year 2006/07, [the Taxpayer] did not submit the applications nor any relevant documents to the Company. As such, the Company was not in a position to exercise control to ensure that part of [the Taxpayer]'s salary was actually expended in the payment of rent.
>
> …..'

17. Company A did not treat the Sum as a refund of rent within the meaning of section 9(1A)(a) of the IRO. Therefore, it can be seen that the Taxpayer had indeed followed the relevant procedures for the year 2005/06 but in respect of the year 2006/07, she had not submitted the relevant application and therefore Company A was not able to exercise control or to ensure that part of the Taxpayer's salary was actually expended on rent. The Taxpayer in her correspondence asserts that this was just a misunderstanding and an administrative

mistake on her behalf.

18. Although we are sympathetic to the Taxpayer's position and the fact that had she completed the relevant form, she would have been entitled to obtain the benefits of the Scheme. This, however, does not entitle us to come to the conclusion that the assessment is incorrect or wrong.

19. Therefore, having considered all matters, having reviewed very carefully all correspondence and documents and having regard to the Taxpayer's written notice of appeal, we have no hesitation in concluding that the Sum was not a refund of rental within the meaning of section 9(1)(a) of the IRO. It was therefore clearly part of the Taxpayer's emoluments which is fully assessable under section 9(1)(a) of the IRO. The Appeal is dismissed.