

Case No. D68/05

Salaries tax – whether gratuity or long service payment – sections 8, 9 and 68 of the Inland Revenue Ordinance ('IRO') – sections 31B, 31G, 31I, 31IA, 31R, 31V, 31Y and 31YAA of the Employment Ordinance.

Panel: Anna Chow Suk Han (chairman), David Li Ka Fai and Daisy Tong Yeung Wai Lan.

Date of hearing: 29 September 2005.

Date of decision: 10 January 2006.

By an appointment letter dated 22 May 1997 Company B offered and the taxpayer accepted employment for a term of two years commencing from 15 May 1997 (the Agreement). The letter contained, inter alia, a term stating that 'Costs borne by the Company, such as severance pay and long service pay, will be deducted from the gratuity'. By a letter dated 22 February 2002 (the Renewal Agreement) Company B renewed the Agreement for a term of one year commencing from 1 April 2002. By a letter dated 3 March 2003, Company B extended the Renewal Agreement for one year to 31 March 2004. At the relevant times, the terms and conditions of employment governing the taxpayer's entitlement to gratuity during the extension periods remained the same as those stipulated in the Agreement.

Upon completion of the Renewal Agreement on 31 March 2004, the taxpayer ceased employment with Company B. As a result, Company B filed a notification in respect of the taxpayer, showing that the taxpayer was paid during the period from 1 April 2003 to 31 March 2004, inter alia, salary of \$1,053,120 and gratuities of \$251,280 (the Sum). In response to the Assessor's enquires, Company B informed the assessor that during the period of the taxpayer's employment from 1 April 2003 to 31 March 2004, the taxpayer was paid a net sum of \$251,280 being gratuity of \$263,280 at 25% of the salary, less \$12,000 which represented the employer's contributions to the MPF and that severance payment and/or long service payment had not been paid to the taxpayer as circumstances giving rise to severance payment and/or long service payment did not occur.

The assessor did not accept the taxpayer's claim for exclusion of the Sum and raised on the taxpayer the 2003/04 salaries tax assessment including the Sum as taxable income. The taxpayer objected to the assessment.

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

The taxpayer's case was that the gratuity included the severance payment due to him in accordance with section 31IA of the Employment Ordinance (EO) and his service with Company B was from 15 May 1992 to 31 March 2004.

The Revenue's case was that the Sum was neither a long service payment nor a severance payment. It was a gratuity paid to the taxpayer upon completion of the service period and was sourced from his employment and is thus taxable under sections 8(1)(a) and 9(1)(a) of the IRO. Section 31I or 31Y of the EO, but not section 31IA or 313YAA are applicable. It was a mere assertion on the part of the taxpayer that the gratuity included severance payment as provided under section 31IA of the EO. The Revenue contended that Company B was the agent acting on behalf of the Hong Kong Government under the two employment contracts dated 15 May 1992 and 15 November 1994 and that the taxpayer only worked for Company B for the period from 15 May 1997 to 31 March 2004.

Held:

1. Both agreements dated 15 May 1992 and 15 November 1994 described that Company B was acting as agents for the Hong Kong Government. On the other hand, the Agreement clearly stated that the taxpayer was employed by Company B. Thus the Board finds that the taxpayer's employment with Company B commenced on 15 May 1997 and not 15 May 1992 as claimed by the taxpayer. Consequently, if the taxpayer were entitled to a severance payment or a long service payment under the EO from Company B he would have been entitled to them as from 15 May 1997. If they were payable, they would have been calculated in accordance with the provisions of section 31G and section 31V of the EO. In the present case, since the taxpayer had worked for Company B for a continuous period of five years, he would have been entitled to a long service payment upon termination of his employment with Company B. Since the Board has no evidence as to whether or not the taxpayer was in fact redundant, the Board will treat the taxpayer's entitlement under the circumstances as a long service payment.
2. It is well settled law that the label to put a payment such as 'a gratuity' or 'a severance payment' is not conclusive of the nature of the payment. One must look at the terms of the contract and the character of a payment made under it in order to determine the true nature of such payment. Having considered the Agreement and the Renewal Agreement, the Board finds that the Sum paid to the taxpayer upon completion of the Renewal Agreement consisted of two natures, firstly, a long service payment and secondly a gratuity equal to 25% of the total basic salary less the MPF contribution and the amount of the long service payment. The Board takes this view because of the condition in the Renewal Agreement which is a term

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

agreed between the parties and it is clearly stated therein that costs such as severance pay and long service pay will be deducted from the gratuity. That being the case, when a severance payment or a long service payment is due to the taxpayer, Company B must pay to the taxpayer firstly the severance payment or the long service payment and then the gratuity. Those payments cannot be reduced by the gratuity payable to the taxpayer. On the other hand, because of the said condition, when a long service payment or a severance payment is payable to the taxpayer, such payment must come before the payment of the gratuity. In the present case, Company B made one payment to the taxpayer. It is a logical inference that the long service payment was made prior to or simultaneously with the payment of the gratuity due to the taxpayer. The Board finds that Company B's obligation to make a severance payment or a long service payment to the taxpayer cannot be affected by the view it held of the matter nor the character of the payment can be altered by the label it put to it. For the foresaid reasons the Board finds that under the terms of the Renewal Agreement Company B was obliged to make a long service payment to the taxpayer and to deduct the same from the gratuity payable.

3. It is a declared policy and an established practice of the Revenue that no salaries tax will be assessed and demanded on severance payment and long service payments made in accordance with the EO. In the present case, the Board has decided on the facts that section 31YAA of the EO applies and not section 31Y and as a result, the taxpayer is able to enjoy the tax benefit accorded to him by the Revenue's aforesaid policy and practice. However had it not been for the provision that 'costs borne by the company, such as severance pay and long service pay, will be deducted from the gratuity' which renders section 31Y not applicable, the taxpayer would have been liable to pay salaries tax on the part of the gratuity equal to the amount of long service payment to which he was entitled under the law. Clearly the purpose of section 31I, 31IA, section 31Y and section 31YAA is to ensure that an employer is not obliged to pay twice for the same nature of payment. Section 31I is to compliment section 31IA and section 31Y to compliment section 31YAA. Surely, they are not meant to exempt tax liability on severance payments and long service payments under the law in some situations and not in the others. However, as it is, application of sections 31I and 31Y produces a different result from that of application of sections 31IA and 31YAA, for entitlement of severance payments and long service payments under the law. No doubt, these results are not only undesirable but are also unfair to those taxpayers who would otherwise be able to enjoy tax exemption on the severance payments and long service payments to which they are entitled under the law. Thus, the Board feels that it ought to raise the question as to whether the Revenue should see fit to extend its aforesaid declared policy and established practice to situations where section 31I and section 31Y of the EO apply.

Appeal allowed.

Cases referred to:

D151/00, IRBRD, vol 16, 101

D51/01, IRBRD, vol 16, 451

D81/01, IRBRD, vol 16, 671

D110/03, IRBRD, vol 19, 44

D10/04, IRBRD, vol 19, 116

D28/05, IRBRD, vol 20, 389

Taxpayer in person.

Lai Wing Man and Chan Wai Yee for the Commissioner of Inland Revenue.

Decision:

The appeal

1. This is an appeal by Mr A ('the Taxpayer') against the salaries tax assessment for the year of assessment 2003/04 raised on him. The Taxpayer claims that the sum of \$251,280 paid to him was his severance payment and long service payment and should be exempt from salaries tax.

The facts

2. By an appointment letter dated 22 May 1997 ('the Agreement'), Company B offered, and the Taxpayer accepted, employment as Senior Resident Engineer for a term of two years commencing from 15 May 1997. The letter contained, inter alia, the following terms and conditions:

‘ 8. You will be entitled to a gratuity of 25% of basic salary earnings payable at the end of 2 years on completion of satisfactory service. Costs borne by the Company, such as severance pay and long service pay, will be deducted from the gratuity. You will not be entitled to a gratuity in the event of resignation or dismissal for unsatisfactory service.’

3. (a) By a letter dated 15 April 1999, Company B extended the Agreement for another two years to 14 May 2001.

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

- (b) By a letter dated 14 May 2001, Company B extended the Agreement for a further period to 31 March 2002.

At the relevant times, the terms and conditions of employment governing the Taxpayer's entitlement to gratuity during the extension periods remained the same as those stipulated in the Agreement.

4. By a letter dated 22 February 2002 (the Renewal Agreement') Company B renewed the Agreement for a term of one year commencing from 1st April 2002. The letter contained, inter alia, the following terms and conditions:

- ' 10. On completion of satisfactory service, you will receive a gratuity for the period of service on the [project C]. The gratuity payable will be the sum which, when added to the Company's contribution to MPF Scheme, equals to 25% of the total basic salary drawn during your service period on the [project C].

Costs borne by the Company, such as severance pay and long service pay, will be deducted from the gratuity. You will not be entitled to a gratuity in the event of resignation or dismissal for unsatisfactory service.'

5. By a letter dated 3 March 2003, Company B extended the Renewal Agreement for one year to 31 March 2004.

6. Upon completion of the Renewal Agreement on 31 March 2004, the Taxpayer ceased employment with Company B. As a result, Company B filed a notification in respect of the Taxpayer, showing that the Taxpayer was paid during the period from 1 April 2003 to 31 March 2004, salary of \$1,053,120, back pay, terminal awards and gratuities of \$251,280 ('the Sum') and housing allowance of \$211,488.

7. The Taxpayer declared the same amount of income but claimed that the Sum should be excluded from assessment on the ground that it was a severance payment and long service payment.

8. In response to the Assessor's enquires, Company B informed the assessor that inter alia, during the period of the Taxpayer's employment from 1 April 2003 to 31 March 2004, the Taxpayer was paid a net sum of \$251,280 being gratuity of \$263,280 at 25% of the salary, less \$12,000 which represented the employer's contributions to the mandatory provident fund and that severance payment and/or long service payment had not been paid to the Taxpayer as circumstances giving rise to severance payment and/or long service payment did not occur.

9. The assessor did not accept the Taxpayer's claim for exclusion of the Sum and raised on the Taxpayer the 2003/04 salaries tax assessment including the Sum as taxable income. The Taxpayer objected against the assessment. By his determination of 30 June 2005, the Deputy

Commissioner confirmed the assessment. Consequently, the Taxpayer filed a notice of appeal against the determination.

The Taxpayer's case

10. The Taxpayer's reasons for his appeal are as follows:

- (a) The gratuity included the severance payment due to him in accordance with section 31IA of the Employment Ordinance ('the EO'). Labour Department had provided a written clarification on a similar case that 'if an employee is entitled to gratuities for all the years of service in respect of which a severance payment is payable, such gratuities shall be reduced by the severance payment paid to him'. Item 10 of his service contract stated that costs borne by the company, such as severance pay and long service pay will be deducted from the gratuity.
- (b) His service with Company B was $11 \times 10.5/12$ years from 15 May 1992 to 31 March 2004 instead of $6 \times 321/365$ years.

The Revenue's case

11. The Sum was neither a long service payment nor a severance payment. It was a gratuity paid to the Taxpayer upon completion of the service period and was sourced from his employment and is thus taxable under sections 8(1)(a) and 9(1)(a) of the Inland Revenue Ordinance. As advised by Company B, the Sum was calculated solely as gratuity and by reference to 25% of the Taxpayer's salary in accordance with the Renewal Agreement. There is no evidence to show that Company B contemplated anything other than to pay the Taxpayer precisely what was due to him as gratuity under the Renewal Agreement. And Company B has unequivocally confirmed that no severance payment and/or long service payment was made to the Taxpayer.

12. Section 31I or 31Y of the EO, but not section 31IA or 31YAA, are applicable to this case. The Taxpayer ceased to be employed by Company B on 1 April 2004. Only then he was entitled to a severance payment or a long service payment calculated in accordance with the length of his service of employment. Since the Taxpayer prior to that date was paid a gratuity pursuant to his employment contract, the circumstances of this case come under section 31I or 31Y of the EO. On the other hand, there is no evidence to show that the Taxpayer did receive any severance payment or long service payment as provided by the EO out of the gratuity received by him. Thus section 31IA or 31YAA does not apply. This conclusion accords with the decisions of the Board of Review including D151/00, IRBRD, vol 16, 101, D51/01, IRBRD, vol 16, 451, D81/01, IRBRD, vol 16, 671, D110/03, IRBRD, vol 19, 44, D10/04, IRBRD, vol 19, 116 and D28/05, IRBRD, vol 20, 389. Even if the Taxpayer was entitled to a severance payment or a long service payment, such payment should only come to \$103,196, being calculated in accordance with the

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

provisions of section 31G or section 31V of the EO ($\$22,500.00 \times \frac{2}{3} \times 6 \frac{321}{365}$ years). However, by reason of section 31I or 31Y any entitlement of the Taxpayer to a severance payment or a long service payment under the Employment Ordinance would have been reduced to nil because of the gratuities of \$1,698,663 he received under the Agreement and the Renewal Agreement. It should be noted that section 31I or 31Y of the EO does not deem all or any part of a gratuity to be severance payment or long service payment.

13. It is a mere assertion on the part of the Taxpayer that the gratuity included severance payment as provided under section 31IA of the EO. There is no evidence to show that there was any agreement between Company B and the Taxpayer on the payment of a severance payment or a long service payment as a result of which the severance payment or the long service payment was deducted from the gratuity. It is very clear from the response of Company B that Company B did not pay any severance payment or long service payment to the Taxpayer.

14. As to the Taxpayer's assertion that his length of service with Company B was 11 10.5/12 years, Company B was the agent acting on behalf of the Hong Kong Government under the two employment contracts dated 15 May 1992 and 15 November 1994. The Taxpayer were under the employment of the Hong Kong Government from 15 May 1992 to 14 May 1997 and the Employment Ordinance does not bind the Hong Kong Government. Even if the Taxpayer were deemed to be the employee of Company B as from 15 May 1992, since the Taxpayer had already received a gratuity of \$899,415 during that period of service, by reason of section 31I or 31Y of the EO, the severance payment or long service payment would have been reduced to nil.

Statutory provisions

15. Inland Revenue Ordinance

8. Charge of salaries tax

(1) *Salaries tax shall, subject to the provisions of this Ordinance, be charged for each year of assessment on every person in respect of his income arising in or derived from Hong Kong from the following sources:-*

(a) *any office or employment of profit; and*

(b) *any pension.*

9. Definition of income from employment

(1) *Income from any office or employment includes:-*

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

- (a) *any wages, salary, leave pay, fee, commission, bonus, gratuity, perquisite, or allowance, whether derived from the employer or others*

68. Hearing and disposal of appeals to the Board of Review

- (4) *The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.*

16. Employment Ordinance

31B. *General provisions as to right to severance payment*

- (1) *Where an employee who has been employed under a continuous contract for a period of not less than 24 months ending with the relevant date:-*

- (a) *is dismissed by his employer by reason of redundancy; or*
- (b)

.... the employer shall be liable to pay to the employee a severance payment calculated in accordance with section 31G.

31G. *Amount of severance payment*

- (1) *Subject to this Part, the amount of a severance payment to which an employee is entitled in any case shall be calculated by allowing:-*

- (a) *in the case of a monthly rated employee, two-thirds of his last full month's wages, or two-thirds of \$22,500.00 which ever is less; and*

....

31H. *Severance payment to be reduced by amount of gratuities and benefits in certain cases*

If an employee becomes entitled to payment of a severance payment under this Part and:-

- (a) *because of the operation of the employee's contract of employment, one or more gratuities based on length of service or*

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

one or more relevant occupational retirement scheme benefits have been paid to the employee; or

(b)

the severance payment is to be reduced by the total amount of all of the gratuities and benefits to or in respect of the employee to the extent that they relate to the employee's years of service for which the severance payment is payable.

31IA. Gratuity or benefit to be reduced by amount of severance payment in certain cases

(1) *If:-*

(a) *because of the operation of the employee's contract of employment, an employee has become entitled to payment of a gratuity based on length of service,*

(b)

and the employee has been paid a severance payment under this Part, the gratuity or benefit is, to the extent that it is attributable to the same years of service as those for which the severance payment is payable, to be reduced by the whole amount of the severance payment. 31R. General provisions as to employee's right to long service payment

31R. General provisions as to employee's right to long service payment

(1) *Where an employee who has been employed under a continuous contract:-*

(a) *for not less than 5 years of service at the relevant date:-*

(i) *is dismissed and his employer is not liable to pay him a severance payment by reason thereof; or*

(ii)

(b)

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

.... the employer shall pay to the employee a long service payment calculated in accordance with section 31V(1).

31V. Amount of long service payment

(1) Subject to this Part, the amount of a long service payment payable under section 31R(1) or 31RA(1) shall be calculated by allowing:-

(a) in the case of monthly rated employee, two-thirds of his last full month's wages, or two-thirds of \$22,500.00, whichever is less; and

....

31Y. Long service payment to be reduced by amount of gratuities and benefits in certain cases

If an employee becomes entitled to payment of a long service payment under this Part and:-

(a) because of the operation of the employee's contract of employment, one or more gratuities based on length of service or one or more relevant occupational retirement scheme benefits have been paid to the employee; or

(b)

the long service payment is to be reduced by the total amount of all of the gratuities and benefits to or in respect of the employee to the extent that they relate to the employee's years of service for which the long service payment is payable.

31YAA. Gratuity or benefit to be reduced by amount of long service payment in certain cases

(1) If:-

(a) because of the operation of the employee's contract of employment, an employee has become entitled to payment of a gratuity based on length of service

(b)

and the employee has been paid a long service payment under this Part, the gratuity or benefit is, to the extent that it is attributable to the same years of service as those for which the long service payment is payable, to be reduced by the whole of the long service payment.

The issue

17. There are two issues to be decided by the Board:
1. whether or not the Sum is the Taxpayer's taxable income; and
 2. whether the Taxpayer's employment with Company B commenced on 15 May 1992 or on 15 May 1997.

Our decision

18. Before we deal with the main issue as to whether the Sum is the Taxpayer's taxable income, we will first deal with the secondary issue as to whether the Taxpayer was employed by Company B as from 15 May 1992.

19. The Taxpayer contends that he had been employed by Company B since 15 May 1992 and thus he was entitled to a severance payment and a long service payment for the period from 15 May 1992 to 31 March 2004, being 11 10.5/12 years. However, the Revenue contends that the Taxpayer only worked for Company B for the period from 15 May 1997 to 31 March 2004 being 6 321/365 years.

20. Apart from the Agreement, the extension letters of 15 April 1999 and 14 May 2001 and the Renewal Agreement, the Revenue has also produced to us two agreements dated 15 May 1992 and 15 November 1994 respectively. Both of these agreements described that Company B was acting as agents for the Government of Hong Kong. Both agreements said that the Hong Kong Government agreed to employ the Taxpayer. On the other hand, the Agreement clearly stated that the Taxpayer was employed by Company B. Thus, we find that the Taxpayer's employment with Company B commenced on 15 May 1997 and not 15 May 1992 as claimed by the Taxpayer. Furthermore, by his letter to the Inland Revenue Department of 12 November 1999 on his objection to the salaries tax assessment for year of assessment 1997/98, the Taxpayer informed the department and directly acknowledged the fact that he was employed by Company B from 15 May 1997 and that he was employed by the Hong Kong Government prior to that date. Hence we have no doubt that the Taxpayer's employment with Company B only commenced on 15 May 1997 and not 15 May 1992. Consequently, if the Taxpayer was entitled to a severance payment or a long service payment under the EO from Company B he would have been entitled to them as from 15 May 1997 and not 15 May 1992. If they were payable, they

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

would have been calculated in accordance with the provisions of section 31G and section 31V of the EO. An employee's rights to a severance payment and a long service payment are governed by section 31B and section 31R of the EO. By virtue of section 31R, where an employee who has been employed under a continuous contract for not less than five years of service is dismissed and his employer is not liable to pay him a severance payment by reason thereof, the employer shall pay the employee a long service payment calculated in accordance with section 31V(1). The effect of this provision is that an employer is only liable to pay an employee who has been employed under a continuous contract for not less than five years, a long service payment if the employee is not at the same time entitled to a severance payment for his dismissal. In another word, the employer is not required to pay twice the amount. Thus, in the present case, since the Taxpayer had worked for Company B for a continuous period of five years, he would have been entitled to a long service payment upon termination of his employment with Company B. The Taxpayer claims that he was in fact dismissed because the position held by him in Company B no longer existed after his contract ended. For practical purposes, it matters not whether he was dismissed or not because even if he was entitled to both a long service payment and a severance payment, he would only be paid one and the same amount under the EO. Since we have no evidence as to whether or not the Taxpayer was in fact redundant, we will treat the Taxpayer's entitlement under the circumstances as a long service payment.

21. Having disposed of the secondary issue, we now come to deal with the main issue.
22. It is well settled law that the label to put a payment such as 'a gratuity' or 'a severance payment' is not conclusive of the nature of the payment. One must look at the terms of the contract and the character of a payment made under it in order to determine the true nature of such payment.
23. Having considered the Agreement and the Renewal Agreement, we find that the Sum paid to the Taxpayer upon completion of the Renewal Agreement consisted of two natures firstly, a long service payment and secondly a gratuity equal to 25 % of the total basic salary less the MPF contribution and the amount of the long service payment. We take this view because of the following condition in the Renewal Agreement:
 - ' 10. On completion of satisfactory service, you will receive a gratuity for the period of service on the [project C]. The gratuity payable will be the sum which, when added to the Company's contribution to MPF Scheme, equals to 25% of the total basic salary drawn during your service period on the [project C].

Costs borne by the Company, such as severance pay and long service pay, will be deducted from the gratuity. You will not be entitled to a gratuity in the event of resignation or dismissal for unsatisfactory service.'

This condition is a term agreed between the parties and it is clearly stated therein that costs such as severance pay and long service pay will be deducted from the gratuity. This provision does not exonerate Company B from its obligation

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

to make payment of severance payment and long service payment even when a gratuity is payable and it also stipulates that such payment will be deducted from the gratuity. That being the case, when a severance payment or a long service payment is due to the Taxpayer, Company B must pay to the Taxpayer firstly the severance payment or the long service payment and then the gratuity. Thus presently notwithstanding the fact that Company B labeled the entire the Sum as gratuity, whether inadvertently or otherwise, the Sum must consist of, firstly the long service payment to which the Taxpayer was entitled and secondly, the gratuity equal to 25% of the salary drawn, less the MPF contribution and the amount of long service payment due to the Taxpayer. In law, the nature of the payment cannot be altered by the label put to it by Company B. The Revenue contends that if a severance payment or a long service payment is payable to the Taxpayer, section 31I or section 31Y of the EO should apply. However, we are of the view that by operation of the said condition, we need not seek assistance from the EO for determination of the Taxpayer's entitlements. If we are wrong on this and we need to seek assistance from the EO, we take the view that section 31I or section 31Y does not apply. Section 31I and section 31Y respectively provide that if an employee becomes entitled to payment of a severance payment or a long service payment and because of the operation of the employer's contract, he is also entitled to a gratuity, the severance payment or the long service payment is to be reduced by the gratuity. In the present case, because the said condition provides that Company B shall bear the costs of the severance payment or the long service payment which shall be deducted from the gratuity, those payments cannot be reduced by the gratuity payable to the Taxpayer. On the other hand, because of the said condition, when a long service payment or a severance payment is payable to the Taxpayer, such payment must come before the payment of the gratuity. Taking a different order of payment would not be possible because unless the amount of severance payment or long service payment was calculated and/or paid, the balance of the gratuity due to the Taxpayer, cannot be ascertained. In the present case, Company B made one payment to the Taxpayer. It is a logical inference that the long service payment was made prior to or simultaneously with the payment of the gratuity due to the Taxpayer. Making the gratuity payment before the long service payment would not be possible. Consequently, if we need to seek assistance from the EO, the Taxpayer's case should fall within section 31YAA instead of section 31Y of the EO. In reaching this view, we are well aware of the contents of the letter from Company B to the Commissioner of 1 April 2005 when it informed the Commissioner that the Taxpayer was entitled to a severance payment and/or a long service payment in accordance with the EO and the company had not made such payment to the Taxpayer being that the circumstances giving rise to such payment did not occur and no payment had been deducted from the gratuity of \$251,280. In this letter, Company B admitted that the Taxpayer was entitled to a severance payment and/or a long service payment in accordance with the EO, but at the same time it stated that circumstances giving rise to a severance payment and/or a long service payment did not occur. With regard to this statement, we have evidence before us that circumstances giving rise to a long service payment did occur because the Taxpayer had worked for Company B for at least five years although there is no evidence to show that circumstances giving rise to a severance payment did occur. We find that Company B's obligation to make a severance payment or a long service payment to the Taxpayer cannot be affected by the view it held of the matter nor the character of the payment can be altered by the label it put to it. We find that this case is distinguishable from the other cases quoted by the Revenue. In those cases, the term and agreement that the costs of severance payment and long service payment borne by the employer shall be deducted from the gratuity, was absent.

24. For the aforesaid reasons we find that under the terms of the Renewal Agreement Company B was obliged to make a long service payment to the Taxpayer and to deduct the same from the gratuity payable. However, since the period of employment of the Taxpayer commenced

(2005-06) VOLUME 20 INLAND REVENUE BOARD OF REVIEW DECISIONS

on 15 May 1997, by virtue of section 31V of the EO, the amount of long service payment due to the Taxpayer, would be \$103,196 being $(\$22,500 \times 2/3 \times 6 \frac{321}{365} \text{ years})$. Consequently, the salaries tax assessment of the Taxpayer for the year of assessment 2003/04 should be reduced by the same amount of \$103,196.

25. It is a declared policy and an established practice of the Revenue that no salaries tax will be assessed and demanded on severance payments and long service payments made in accordance with the EO. In the present case, we have decided on the facts that section 31YAA of the EO applies and not section 31Y and as a result, the Taxpayer is able to enjoy the tax benefit accorded to him by the Revenue's aforesaid policy and practice. However, had it not been the provision that 'costs borne by the company, such as severance pay and long service pay, will be deducted from the gratuity' which renders section 31Y not applicable, the Taxpayer would have been liable to pay salaries tax on the part of the gratuity equal to the amount of long service payment to which he was entitled under the law. Clearly the purpose of sections 31I, 31IA, section 31Y and section 31YAA is to ensure that an employer is not obliged to pay twice for the same nature of payment. Section 31I is to compliment section 31IA and section 31Y to compliment section 31YAA. Surely, they are not meant to exempt tax liability on severance payments and long service payments under the law in some situations and not in the others. However, as it is, application of sections 31I and 31Y produces a different result from that of application of sections 31IA and 31YAA, for entitlement of severance payments and long service payments under the law. It appears to us that in some cases whether sections 31I and 31Y or sections 31IA and 31YAA should apply, will depend on the employers' treatments of the payments to their employees. If the employers treat the entire payments to the employees as gratuities even if those employees are at the same time entitled to severance payments or long service payments under the law, those employees will then be deprived of the tax exemption granted to taxpayers under the aforesaid declared policy. No doubt, these results are not only undesirable but are also unfair to those taxpayers who would otherwise be able to enjoy tax exemption on the severance payments and long service payments to which they are entitled under the law. Thus, we feel that we ought to raise the question as to whether the Revenue should see fit to extend its aforesaid declared policy and established practice to situations where section 31I and section 31Y of the EO apply.