

Case No. D19/06

Salaries tax – gratuity payment – severance payment - section 31B, 31G, 31I, 31IA, 31P and 31Q of the Employment Ordinance (‘EO’) - sections 8(1)(a) and 9(1)(a) of the Inland Revenue Ordinance (‘IRO’)

Panel: Anthony So Chun Kung (chairman), Chris Mong Chan and Edward Shen.

Date of hearing: 11 March 2006.

Date of decision: 10 May 2006.

The taxpayer’s employment (by way of a ‘rolling contract’) with the Authority was terminated on 30 September 2002 and he was paid a gratuity of HK\$185,337 (the ‘Sum’).

The taxpayer appealed and argued that he was statutorily entitled to a ‘severance pay’ of HK\$149,343 under the EO which should be tax-exempted to reduce the assessment of the Sum to HK\$35,994.

The taxpayer further argued that the Sum was in fact a discretionary or ex gratia payment upon termination and accordingly should not be taxable as employment income.

Held:

1. The label of the Sum is not conclusive. The Board has to go back to the contract of employment to examine those terms governing its payment and the circumstances and manner how the payment was made, including how it was calculated.
2. It was the Authority who terminated the taxpayer’s employment. By operation of the terms of the employment contract, the taxpayer was entitled to pro-rata gratuity. The Sum cannot be a discretionary payment.
3. The Sum cannot be a severance payment as:
 - 3.1 There was not any section 31P (of EO) written statement to the taxpayer and the taxpayer did not ask for any;
 - 3.2 There is no evidence showing computation of any severance payment to the

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taxpayer in accordance with section 31B and 31G of EO;

- 3.3 The taxpayer specifically ‘opted’ the gratuity;
- 3.4 The Authority had prior to termination paid the taxpayer total gratuities (for four successive Relevant Periods) of \$839,688.
- 3.5 The Sum was computed in the same manner as the Authority computed the taxpayer’s previous gratuities for his previous employment periods.
4. Section 31I of EO does not entitle the taxpayer to deem any gratuity payment paid under his employment contract into a statutory severance payment.
5. The Sum is a pro-rata gratuity payment relating to the taxpayer’s services with the Authority, computed and paid according to the terms of the employment of the taxpayer and hence fully chargeable to tax.

Appeal dismissed.

Cases referred to:

D151/01, IRBRD, vol 16, 101
D51/01, IRBRD, vol 16, 451
D110/03, IRBRD, vol 19, 44
D10/04, IRBRD, vol 19, 116
D13/05, IRBRD, vol 20, 298
D28/05, IRBRD, vol 20, 389
D68/05 (unreported)

Taxpayer in person.

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

Decision:

The appeal

1. This is an appeal by Mr A (‘the Taxpayer’) against the Determination of the Deputy Commissioner of Inland Revenue dated 22 November 2005 (‘the Determination’).

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2. In his Determination, the Deputy Commissioner of Inland Revenue maintained the assessment of the assessor (1) to assess the Taxpayer for the year of assessment 2002/03 on a gratuity payment of \$185,337, and (2) to reject the Taxpayer's claim for deduction of home loan interest of \$23,338.95.

3. Prior to and at the hearing, the Taxpayer confirmed withdrawing his claim for deduction of home loan interest of \$23,338.95.

4. The hearing continued on the Taxpayer's objection against the assessment raised on the gratuity payment of \$185,337.

The facts

5. By a letter of appointment signed on 23 November 1992 ('the Appointment Letter'), the Taxpayer joined Authority B (formerly Authority C) ('the Authority') as a Senior Personnel Officer on 18 January 1993.

6. The appointment was said to be under a 'rolling contract' which would continue until being terminated by two months' written notice or salary in lieu of notice. Clause 1(b) of the Appointment Letter states:

'1 Terms of Employment

...

(b) Contract Period

This will be a rolling contract of employment and will continue in effect until either (i) the date on which a new contract of employment is entered into between you and the Authority; or (ii) termination by not less than two (2) months' written notice being given by you or by the Authority to the other or (iii) immediately without notice by the payment of two (2) months salary in lieu of notice by the Authority or you to the other.'

7. Aside from salary and year-end bonus, the Taxpayer was paid a gratuity. Clause 6 of the Appointment Letter states:

'6. Gratuity

(a) Following the satisfactory completion of each successive period of 24 months of your employment under this contract (each such period being the "Relevant

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Period”), you will be paid a gratuity equal to 25% of all salary and bonus payments paid to you during the last completed Relevant Period.

- (b) In the event that your employment is terminated within any Relevant Period, you shall not be entitled to receive any gratuity which may otherwise have accrued up to the date of termination, except when the Authority terminates your employment (other than pursuant to clause 13) in which case the payment of any gratuity will be entirely at the discretion of the Authority.’

8. By a letter dated 4 April 1997 (‘the Promotion Letter’), the Taxpayer was promoted to Manager in the Human Resources and Administration Division with effect from 21 May 1997. Clause 7 of the Promotion Letter states:

‘7. Notice of Termination : Three (3) months’ written notice or three (3) months’ salary in lieu of notice.
Other terms and conditions of employment will remain unchanged.’

9. By a letter dated 30 September 2002 (‘the Termination Letter’), the Authority informed the Taxpayer that his employment with the Authority was terminated. The first two paragraphs of the Termination Letter states:

‘As a result of a recent review on the structure of Employee Services and Relationship Management Section, several changes have been introduced. You have been informed earlier that your position has been eliminated as a result. Although openings have been posted and you have been interviewed in the process, your applications have not been successful. Regrettably, we have agreed that should you be unsuccessful in securing alternative assignment within the Authority up until 30 September 2002, your service with the Authority will be brought to a close.

Pursuant to your Letter of Appointment of 23 November 1992 and Clause 7 of the Promotion Letter dated 4 April 1997, [the Authority] hereby offers you wages in lieu of three months’ notice to terminate your employment with the Authority with immediate effect. Upon termination of your employment, you will receive pro-rata gratuity payment or Severance Payment. Please note that pursuant to the Employment Ordinance, gratuity payment can be used to set off Severance Payment.’

9. The Authority filed a notification (‘IR56F’) dated 11 February 2003 under section 52(5) of the Inland Revenue Ordinance (‘the Ordinance’) showing that for the period of employment from 1 April 2002 to 1 October 2002, the Taxpayer was paid, inter alia, a ‘back pay, terminal awards and gratuities etc’ in a sum of \$260,297.

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10. In his Tax Return dated 15 June 2003 for the year of assessment 2002/03, the Taxpayer stated that a lump sum payment of \$260,297 was compensation for early termination of employment.

11. On 2 December 2003, the Assessor raised on the Taxpayer Salaries Tax assessment for the year of assessment 2002/03, inter alia, on the lump sum payment of \$260,297.

12. On 7 December 2003, the Taxpayer objected the Assessor's assessment in the following terms:

'Please note under item (of "Back pay, terminal awards and gratuities etc." in the IR56F filed by the Authority), the total amount \$260,297 is consisted of:

- an Ex-gratia payment of \$74,600 (2 months' of my basic salary of \$37,480) &
- pro-rata contract end gratuity for early termination of my employment (\$185,337)**

please note that this offset my statutory entitlement of severance pay \$149,343 i.e. $\$37480 \times \frac{2}{3} \times \text{my } 9 \text{ years \& } 257 \text{ days service with [the authority.]}$ The above should be tax-exempted and please kindly review accordingly...

13. In reply to the queries raised by the Assessor, the Authority supplied the following information and documents:

(a) The sum of \$260,297 paid to the Taxpayer upon termination of his employment was made up of an ex-gratia payment of \$74,960 and gratuity of \$185,337.

(b) A copy of the calculation of the gratuity of \$185,337 showing:

(A) Gratuity payment for the period from 18 January 2001 to 1 October 2002:

<u>Pay Period</u>	<u>Salary</u>	<u>Annual Bonus</u>	<u>Gratuity</u>
Jan-01	\$16,926.50		\$4,231.60
Feb-01	\$37,480.00		\$9,370.00
Mar-01	\$37,480.00		\$9,370.00
Apr-01	\$37,480.00		\$9,370.00
May-01	\$37,480.00		\$9,370.00
Jun-01	\$37,480.00		\$9,370.00
Jul-01	\$37,480.00		\$9,370.00

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Aug-01	\$37,480.00		\$9,370.00
Sep-01	\$37,480.00		\$9,370.00
Oct-01	\$37,480.00		\$9,370.00
Nov-01	\$37,480.00		\$9,370.00
Dec-01	\$37,480.00	\$37,480.00	\$18,740.00
Jan-02	\$37,480.00		\$9,370.00
Feb-02	\$37,480.00		\$9,370.00
Mar-02	\$37,480.00		\$9,370.00
Apr-02	\$37,480.00		\$9,370.00
May-02	\$37,480.00		\$9,370.00
Jun-02	\$37,480.00		\$9,370.00
Jul-02	\$37,480.00		\$9,370.00
Aug-02	\$37,480.00		\$9,370.00
Sep-02	\$37,480.00		\$9,370.00
Oct-02	\$1,209.00	\$28,135.70	\$7,336.20
Total	\$767,735.50	\$65,615.70	\$208,337.80
Gratuity			\$208,337.80

- (B) Employer's MPF contribution for the period of 1 December 2000 to 1 October 2003

MPF relevant income

(capped at \$20,000.00 per month) x

5% x 22 months & 1 day

\$23,000.00

(A) – (B): \$185,337.80

Remarks

- (a) Pro-rata gratuity payment equals to 25% of all salary and bonus payments from 18 January 2001 to 1 October 2002.
- (b) Employer's MPF contribution equals to 5% of all MPF relevant income (capped at \$20,000.00 per month) paid from 1 December 2000 to 1 October 2002.'

14. The Assessor accepted that the ex-gratia payment of \$74,960 was not chargeable to salaries tax, but maintained the view that the gratuity of \$185,337 should be assessable.

The issue

15. The issue in this case is whether the gratuity payment of \$185,337 ('the Sum') has been correctly assessed to tax.

The Taxpayer's case

16. The Taxpayer argues that his was a 'rolling contract' with the Authority, upon being laid redundant, he was statutorily entitled to a 'severance pay' of \$149,343 i.e. $\$37480 \times \frac{2}{3} \times 9$ years & 257 days under the Employment Ordinance ('EO'). The Taxpayer claims that such 'severance pay' should be tax-exempted to reduce the assessment of the Sum to \$35,994 (\$185,337 - \$149,343).

17. The Taxpayer argues that section 31I of the EO could not extinguish his statutory entitlement to severance pay, it only allows the employer to offset such severance pay from the Sum, but such severance pay should remain tax-exempted.

18. The Taxpayer further argues that according to clause 6(b) of his employment contract, the Sum was in fact a termination payment paid 'entirely at the discretion of the Authority'. The Sum is therefore a discretionary or ex gratia payment he received upon termination of his employment and accordingly should not be taxable as his employment income. The Taxpayer argues that the Revenue was wrong in considering such discretionary payment as gratuity payment.

The Revenue's case

19. The Revenue points out that the Taxpayer has received from the Authority prior to the termination of his employment several gratuity payments in a total sum of \$839,688.10:

<u>Date of the Tax Return filed</u>	<u>Period covered</u>	<u>Gratuities returned</u>
25-5-95	95 – 97	\$160,223
30-5-97	18-1-95 – 17-1-97	\$196,715.10
3-6-99	18-1-97 – 17-1-99	\$239,130
1-6-01	18-1-99 – 17-1-01	<u>\$243,620</u>
		<u>\$839,688.10</u>

20. The Taxpayer's entitlement to any severance payment under the EO arose at a time when he had received gratuity payments. The Revenue therefore argues that section 31I of the EO should apply to this case. The Taxpayer's statutory entitlement to any severance payment should be reduced to nil by operation of section 31I of the EO as the gratuity amount already received by the Taxpayer under his employment well exceeds the amount of his statutory entitlement.

21. The Revenue further points out that the Authority has not issued to the Taxpayer any severance payment because if it had it should have issued written statement to the Taxpayer under section 31P of the EO. The Revenue also points out that section 31IA of the EO provides for set-off of gratuity from severance payment and since the Authority has not issued any severance

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payment, there is no severance payment from which to apply set-off under section 31IA of the EO. Section 31IA of the EO therefore should not be applicable to this case.

22. Since the Authority's legal obligation in making severance payment to the Taxpayer was discharged by operation of section 31I of the EO, the Revenue therefore argues that upon termination of his employment, the Taxpayer could not have received any payment in the nature of severance payment and accordingly no tax concession could be awarded.

23. Further, the Revenue argues that the Sum was computed and paid to the Taxpayer pursuant to the terms of his contract of employment, being 25% of all salary and bonus payments paid to the Taxpayer during the period from 18 January 2001 to 1 October 2002 ('the Last Relevant Period') after deduction of the Authority's MPF contribution (see paragraph 14 above). Such pro-rata gratuity payment accordingly constitutes part of the emoluments of the Taxpayer's employment with the Authority and therefore fully assessable to tax.

Analysis and finding

24. The main focus for us is to find out the true nature of the Sum. Is the Sum a gratuity payment, a severance payment, a discretionary payment, or a mix or combination thereof, or is it some other kind of payment?

Discretionary payment?

25. The Taxpayer believes that any payment made when the Authority terminates his employment is a discretionary payment because clause 6(b) of his employment contract stipulated that '...when the Authority terminates your employment ...in which case the payment of any gratuity will be entirely at the discretion of the Authority.' According to the Taxpayer, the clause 'in which case the payment of any gratuity will be entirely at the discretion of the Authority' defines and follows 'when the Authority terminates your employment'.

26. For easy reference, we set out again the full text of clause 6(b) below:

'6(b) In the event that your employment is terminated within any Relevant Period, you shall not be entitled to receive any gratuity which may otherwise have accrued up to the date of termination, except when the Authority terminates your employment (other than pursuant to clause 13) in which case the payment of any gratuity will be entirely at the discretion of the Authority.'

27. The Taxpayer argues that if the Sum is a payment paid entirely at the discretion of the Authority, it could not be said as remunerating him for his past services and therefore he claimed that it should not be assessable as his income under employment.

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28. If the Taxpayer's interpretation is correct, it would mean that the Authority could rely on clause 6(b) to avoid paying gratuity which may otherwise have accrued by terminating Taxpayer's employment any time before he could have completed one Relevant Period. We find it difficult to believe that while signing off clause 6(b) of the Appointment Letter on 23 November 1992 the Taxpayer did really intend clause 6(b) of the Appointment Letter to afford the Authority such a right.

29. Clause 6(b) should be interpreted under the context of the entire clause 6 which touches and concerns 'gratuity'. Clause 6(a) sets out 25% gratuity as Taxpayer's emolument payable to the Taxpayer every Relevant Period of 24 months. Clause 6(b) sets out how to compute gratuity if the Taxpayer cannot complete a Relevant Period, one way is by usual pro rata basis, the other is at the discretion of the Authority.

30. We are of the view that the clause 'in which case the payment of any gratuity will be entirely at the discretion of the Authority' defines and explains 'In the event...you shall not be entitled to receive any gratuity which may otherwise have accrued up to the date of termination...', setting out the simple logic that if ever the Taxpayer shall not be entitled to pro rata gratuity earned and accrued, then payment of gratuity will be at the discretion of the Authority; on the other hand if the Taxpayer shall be entitled to pro rata gratuity, payment of gratuity will not be at the Authority's discretion.

31. As to when the Taxpayer shall be entitled to pro rata gratuity earned and accrued and when he shall not be entitled, we are of the view that according to clause 6(b), the Taxpayer shall not be entitled to pro rata gratuity if his employment is terminated before completion of one Relevant Period, for example if the Taxpayer resigns, in which case any payment of gratuity will be entirely at the Authority's discretion. But it could not be right for the Authority to have discretion on gratuity already earned and accrued by the Taxpayer if it is the Authority who terminates the employment, accordingly, clause 6(b) excludes and except non-entitlement to pro rata gratuity to a situation where it is the Authority who terminates the employment. This means if it is the Authority who terminates the employment, the Taxpayer shall still be entitled to a pro-rata gratuity, other than if the Authority's termination is pursuant to clause 13 which are for causes of summary dismissal. Under clause 6(b), the Authority can have discretion over gratuity payment only for cases where the employment was not terminated by the Authority, not the other way round as argued by the Taxpayer.

32. In this case, it was the Authority who terminated Taxpayer's employment. The Taxpayer was entitled to pro rata gratuity under clause 6(b).

33. We believe the Authority has interpreted clause 6(b) in manner like us. It computed the Sum as 25% of the Taxpayer's salary and bonus as accrued up to the date of termination. Under such circumstance, the Sum cannot be a discretionary payment paid at the discretion of the Authority.

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Severance payment or gratuity payment, or a mixture of both?

34. The Revenue points out that under section 31P of the EO, the Authority must give to the Taxpayer as employee *'a written statement indicating how the amount of the (severance) payment has been calculated'*.

35. Section 31P of the EO provides:

'(1) On making any severance payment, otherwise than in pursuance of a decision of the Minor Employment Claims Adjudication Board or Labour Tribunal which specifies the amount of the payment to be made, the employer shall give to the employee a written statement indicating how the amount of the payment has been calculated.

(2) ...

(3) Without prejudice to any proceedings for an offence under subsection (2)(a), if an employer fails to comply with the requirements of subsection (1), the employee may by notice in writing to the employer require the employer to give to the employee a written statement complying with those requirements within such period (not being less than 1 week beginning with the day on which the notice was given) as may be specified in the notice.'

36. The Authority has not given section 31P written statement to the Taxpayer and the Taxpayer has not required the employer to do so. There is no evidence showing that the Authority has made any computation of severance payment to the Taxpayer.

37. Further, the Taxpayer fails to show to us that the statutory severance pay of \$149,343 i.e. $\$37,480 \times \frac{2}{3} \times 9$ years & 257 days which he claims for tax exemption was in fact computed pursuant to the provision of sections 31B and 31G of the EO.

38. Section 31B(1) of the EO provides:

'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) is laid off within the meaning of section 31E

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

39. Section 31(G) of the EO provides:

'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, whichever is less;*
- (b) in any other case, 18 days' wages based on any 18 days chosen by the employee and occurring during his last 30 normal working days, or two-thirds of \$22,500, whichever is less;*

for every year ... of employment under a continuous contract by his employer subject in all cases to a maximum payment not exceeding, where the relevant dates occurs in a period specified in column 1 of table A in the Seventh Schedule, the amount specified in column 2 of that table opposite to the period'.

40. The formula provided under section 31(G)(1)(a) of the EO works on 'two-thirds of his last full month's wages, or two-thirds of \$22,500, whichever is less'; the formula of the Taxpayer (\$149,343 i.e. \$37,480 x 2/3 x 9 years & 257 days) on the contrary works on the higher instead of the less between two-thirds of his last full month's wages and two-thirds of \$22,500.

41. Further, the Sum could not be severance pay because the Taxpayer specifically 'opted' the gratuity. In his letter dated 19 December 2005 to the Clerk to the Board of Review, the Taxpayer wrote:

'...Upon the establishment of [the Authority] Retirement Benefit Scheme, all staff on rolling contracts had options to join the Retirement Benefits Scheme or stayed with the "gratuity payment". The (Taxpayer), for personal financial reasons, opted the gratuity payment. Please note such option/decision has had no bearing nor had changed the nature of continuous employment of the concerned staff within the Authority...'

42. Indeed, the Taxpayer at the hearing accepted that according to the computation done by the Authority, the Sum was a pro-rata gratuity payment computed at 25% of his salary and bonus of the Last Relevant Period, in same manner as the Authority computed his previous gratuities for his previous employment periods. Under such circumstance, the Sum cannot be a severance payment.

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43. The Taxpayer however argues that such gratuity payment he 'opted', or part thereof, was in fact his statutory severance payment by way of set-off under the EO.

44. The Taxpayer refers us to the Termination Letter wherein the Authority wrote, 'Please note that pursuant to the Employment Ordinance, gratuity payment can be used to set off Severance Payment'. He argues that his statutory severance payment has already been used up in setting off under section 31I of the EO by the Authority, such part of the gratuity so set off should therefore be deemed as severance payment so as to entitle him to enjoy the Revenue's concession thereon. For easy reference, we shall refer to his above argument as the Taxpayer's 'set-off' contention.

45. The sections of the EO which may be relevant to the Taxpayer's 'set-off' contention are 31I and 31IA:

(a) Section 31I of the EO provides:

'If an employee becomes entitled to payment of the 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 one or more relevant occupational retirement scheme benefits have been paid to the employee; or

(b) a relevant mandatory provident fund scheme benefit is being held in a mandatory provident fund scheme in respect of the employee,

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

(b) Section 31IA(1) of the EO provides:

'(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, or to payment of a relevant occupational retirement scheme benefit; or

(b) a relevant mandatory provident fund scheme benefit is being held in a mandatory provident fund scheme in respect of the employee,

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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.'

46. The Taxpayer however has not explained to us why under section 31I of the EO he should be entitled to a severance pay of \$149,343 when the Authority had prior to that paid him a total of \$839,688 of gratuities payment.

47. Even if we accept that he was entitled to a severance pay of \$149,343 under the EO despite he had prior to that received a total of \$839,688 of gratuities payment, the Taxpayer still fails to explain why such severance pay should not be fully set-off and reduced to zero under section 31I of the EO against the final pro rata gratuity payment of \$185,337.80 which he received from the Authority upon termination of his employment.

48. There are long line of authorities explaining the application of section 31I, including those cited by the Revenue, Case Nos D151/00, IRBRD, vol 16, 101, D51/01, IRBRD, vol 16, 451, D110/03, IRBRD, vol 19, 44, D10/04, IRBRD, vol 19, 116, D13/05, IRBRD, vol 20, 298, D28/05, IRBRD, vol 20, 389, D68/05 [unreported]. None could be said to support the 'set-off' contention of the Taxpayer.

49. For instance, the Board in Case No D51/01 at paragraphs 30 and 32 of its decision stated:

'First, although section 31IA seems to be the other side of the coin of section 31I, basically they are provisions in the EO which regulate the relationship between an employer and an employee and are made to ensure that an employer is not obliged to make double payment for the same thing. At the end of the day one still has to look into the true nature of the payment...

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We appreciate that Mr Wu places a lot of reliance on the concessions made by the Commissioner at the hearing, especially the concession in paragraph 24 of the written submission of his representative. Read in its context, we take the view, however, that that concession was to the effect only that the Taxpayer would have been entitled to severance payment on completion of his extended employment on 31 January 1998 but for the operation section 31I of the EO. It therefore is of no assistance to the Taxpayer.'

50. Further, the Board in Case No D110/03 at paragraphs 13 of its decision stated:

'The Board presiding in Case No. D151/00 IRBRD vol 16 101 opines that the EO does not bind the Government. The Board also opines that, even if the EO binds the Government, looking at the terms of the contract of the case, undoubtedly gratuity was part of the remuneration, and was not severance payment or long service payment under the EO. Furthermore, the provision in section 31I of the EO about offsetting severance payment from gratuity is to reduce the severance payment payable by the employer (until reduced to nil), such provision could not change gratuity into severance payment.'

The original Chinese text is as follows:

'在D151/00 IRBRD vol 16 101一案中，審理該案的上訴委員會認為[僱傭條例]對政府不具約束力。上訴委員會並認為，則使《僱傭條例》對政府具約束力，在該案中，? 觀合約條文，毫無疑問地約滿酬金乃酬金的一部份，而並不是《僱傭條例》下所指的遣散費或長期服務金。此外，《僱傭條例》第31I條內有關以酬金抵銷遣散費的規定只是令僱主應付的遣散費減少（甚至完全減免），該條例並不能令酬金變為遣散費。'

51. Section 31I of the EO only allows an employer to avoid double payment by reducing severance payment for the total amount of all of the gratuity and benefits to the extent that they relate to the employee's years of service for which the severance payment is payable. It does not entitle an employee (the Taxpayer in this case) to consider or to deem for tax purposes any part of what otherwise would be a gratuity payment paid under an employment contract as a statutory severance payment. Plainly, we find no such deeming entitlement written in section 31I of the EO and we have no jurisdiction to read such deeming entitlement into it.

52. The Taxpayer's 'set-off' contention is a result of his misinterpretation of sections 31I of the EO. The Taxpayer is wrong in construing section 31I of the EO as entitling him to deem a gratuity payment as a severance payment.

53. In paragraph (iii) of his written submission the Taxpayer suggests that different tax implication could be achieved by the way how the Authority presented 'gratuity and offset of severance pay' to IRD. The Taxpayer seems to believe that the nature of a payment depends on the way or manner how the employer has presented or labeled it. He is again wrong in so believing.

54. The way how the Authority would present or label the Sum to the Revenue is not conclusive. We have to go back to the contract of employment to examine those terms governing its payment and the circumstances and manner how the payment was made, including how the payment was calculated. Above all, we have to examine the relevant taxing provisions in the IRO to consider whether the payment is chargeable to tax, if so, under which provisions.

55. The Board in Case No D151/00 at paragraph 34 of its decision stated:

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'It is settled law that labels such as 'gratuity' or 'severance payment' are not conclusive. 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. See decisions of the Board in D90/96 IRBRD, vol 11, 727 and D24/97, IRBRD, vol 12, 195.'

55. The Board in Case No D80/00 at paragraph 9 of its decision stated:

'In D24/88, ... the Board attached significance to the way in which the sum of \$53,333 was arrived at, and found that it was paid by reference to the Taxpayer's service with a previous employer and the payment was made in discharge of the personal obligation of a director of the employer to the employee. It was therefore not a payment for services and not taxable. The case illustrates the point that where it is possible to ascertain how the payment in question was calculated, it can help in identifying the nature of the payment.'

57. The relevant taxing provisions in this case are sections 8 and 9 of the IRO:

(i) Section 8(1)(a) of the IRO provides:

'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;...'

(ii) Section 9(1)(a) of the IRO provides:

'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...'

58. After carefully examining the Appointment Letter, the Promotion Letter, the Termination Letter, relevant tax returns filed by the Taxpayer and the Authority respectively, the payment computation done by the Authority, the replies sent to the Revenue by the Authority and the Taxpayer respectively, we find that the Sum of \$185,337.80 is a pro-rata gratuity payment relating to the Taxpayer's services during his Last Relevant period of employment with the Authority. It was computed and paid according to the terms of the employment of the Taxpayer. It

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constitutes the emoluments of the Taxpayer's employment with the Authority. The Sum is therefore fully chargeable to tax under sections 8(1)(a) and 9(1)(a) of the IRO.

Other side issues

59. First, we have not dealt with section 31IA of the EO in this case. This is because the Sum in question is a gratuity and not a severance payment, section 31IA which provides for set off of gratuity from severance payment is therefore not applicable.

60. Second, the Taxpayer in his written submission suggested that the Revenue had preferred 'Retirement Benefits Scheme' over 'gratuity payment' by allowing differential tax treatment in favour of leavers under Retirement Benefits terms. He felt aggrieved in having to pay tax on gratuity whereas his other colleagues who elected retirement benefits were tax exempted. This is a misunderstanding on the part of the Taxpayer. The Revenue has not preferred one scheme over another. The Revenue is simply executing the law as it has been statutorily provided for. Section 8(2)(cc) of the IRO states:

'8 (2) In computing the income of any person for the purposes of subsection (1) there shall be excluded the following-

*.
(cc) subject to subsections (4) and (5)-*

(i) any sum (not being a pension) withdrawn from a recognized occupational retirement scheme on retirement, death, incapacity or termination of service; and

(ii) a sum equal to so much of the accrued benefit received from the approved trustee of a mandatory provident fund scheme on retirement, death, incapacity, termination of service, or taken to have been received from the approved trustee of such a scheme as provided by subsection (9), as is attributable to voluntary contributions paid to the scheme by an employer;'

61. Section 8(2)(cc) of the IRO was all along there and the Taxpayer did have a choice to take tax advantage of it by electing the Retirement Benefit Scheme. For personal financial reasons however he elected gratuity payment instead. He has chosen gratuity payment as his remuneration package on his own volition for his own personal reasons, and this is exactly what the Authority has paid him upon his leaving his employment. The Taxpayer has not been prejudiced or differentially treated as he might wish to believe. It is due to his own management of his affairs that he has turned away Retirement Benefit Scheme and has 'opted' for gratuity which subjects him to tax.

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62. It is long established law that a taxpayer could in organizing his tax affairs take full advantage of all benefits afforded under the tax statutes and for that purpose he would be entitled to seek advice and assistance from other people including tax professionals. With or without outside advice and assistance, if he has organized his tax affairs in a way which he later feels aggrieved, he has himself to blame and not the system.

63. The Board in Case No D10/04 at paragraph 5 of its decision stated:

'The difficulties with this branch of the law stems from the Revenue's concession in not taxing severance payments paid pursuant to the statutory obligation as imposed by the EO. Taxpayers had frequently transposed such concession to a situation where the payment in question was made pursuant to the provisions of a contract of employment.'

64. The Taxpayer in this case misconceived his appeal by transposing the Revenue's concession in not taxing severance payments to treating the gratuity payments he received under his contract of employment as severance payment.

Conclusion

65. Section 68(4) of the IRO provides that:

'The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.'

For reasons stated above, we find that the Taxpayer has failed to discharge his onus.

66. In the result, we dismiss the Appellant's appeal and confirm the assessment.