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Commissioner of Inland Revenue,
G.P.O. Box 132, HONG KONG.

來函編號：
Your Ref.: CB2/SC/16
來函請敘明本局檔案號碼
IN ANY COMMUNICATION PLEASE QUOTE OUR FILE NO.

本局檔案號碼：
Our File No.: DAD(CR)197/1046C

Ms Josephine SO
Clerk to Select Committee
Legislative Council
Legislative Council Complex
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Central, Hong Kong

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By post and by fax
(Fax No. : 2509 9055)

Dear Ms SO,

Select Committee to Inquire into Matters about the Agreement between Mr LEUNG Chun-ying and the Australian firm UGL Limited

I refer to your letter of 14 November 2017 and provide below the requested general information.

The Inland Revenue Department ("IRD") is responsible for administering, among others, the Inland Revenue Ordinance ("IRO"). In deciding whether a certain payment is chargeable to tax under the IRO, the task of the IRD is to apply the law, including statutory provisions and principles established in case law, to the facts of the case in question. No issue of policy is involved here.

In your letter of 14 November 2017, you referred to a situation where a payment is received by a Hong Kong resident from (a) his employer or former employer and (b) a non-employer entity, pursuant to a contract or other forms of arrangement imposing restrictive covenants that seek to, for example, prohibit the person from having any business dealings in competition with his former employer, or prohibit the person from soliciting employees of his former employer; and where the Hong Kong resident is required under the contract (or other forms of arrangement) to provide assistance in the promotion of the former employer regardless of whether assistance has in fact been rendered. In this connection, I consider the relevant taxation principles include the following:

(1) Section 8(1) of the IRO imposes the charge to salaries tax upon every person in respect of income arising in or derived from Hong Kong from any office or employment of profit and any pension. The charge makes no distinction between a Hong Kong resident and a non-Hong Kong resident.

(2) No general rules are given in the IRO for determining whether income "arises in or is derived from Hong Kong". It has long been accepted that it is necessary to establish the place where the employment, the source of income, is located. The IRD has accepted that in the great majority of the cases, the question of Hong Kong or non-Hong Kong employment can be resolved by considering three factors, namely, (a) where the contract of employment was negotiated and entered into, and is enforceable, (b) residence of the employer, and (c) place of payment of remuneration. Departmental Interpretation & Practice Notes No. 10 (Revised) "The Charge to Salaries Tax" sets out IRD's view and practice in determining source of employment and is available at http://www.ird.gov.hk/eng/pdf/e_dipn10.pdf.

(3) Section 9(1)(a) of the IRO defines income from an office or employment to include wages, salary, leave pay, fee, commission, bonus, gratuity, perquisite, or allowance, whether derived from the employer or others. A sum received by a taxpayer from a person other than his employer can be taxable provided that it is an income from his employment.

(4) For a payment to be chargeable to salaries tax, it is not sufficient to say that the employee would not have received the sum in question if he had not been an employee[1].

(5) Chargeable income is not confined to income earned in the course of employment but also embraces payments made in return for acting as or being an employee, or as a reward for past services or as an inducement to enter into employment and provide future services[2].

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[1] Fuchs v. CIR (2011) 14 HKCFAR 74, para. 16, quoting Hochstrasser (Inspector of Taxes) v Mayes [1960] AC 376.

[2] Ibid, para. 17.

(6) The applicable test is whether the payment in question is "from employment"[3].

(7) Where the payment is not made pursuant to any entitlement under the employment contract but is made in consideration of the employee agreeing to surrender or forgo his pre-existing contractual rights, it might not be taxable[4].

(8) In general, a payment made for post-employment restrictive covenants is not chargeable to salaries tax[5]. Where there are terms in the contract or arrangement other than the giving of the restrictive covenants, it is essentially a question of fact whether the payment is entirely attributable to the giving of the restrictive covenants or the payment is partly made for something else[6]. In the case of the latter, it is necessary to decide whether that part of the payment that is made for something else is "income from employment".

I wish to emphasise that the taxation principles set out above are general principles only and whether a payment is income from employment and thus taxable can only be determined upon consideration of all the relevant facts and circumstances.

I hope the above is helpful to the Select Committee.

Yours sincerely,

(WONG Kuen-fai)
Commissioner of Inland Revenue

c.c. Hon Paul TSE Wai-chun, JP (Chairman)

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[3] Ibid, para. 18.
[4] Ibid, para. 22 and headnote.
[5] *Beak v Robson* [1943] 1 All ER 46, applied in *CIR v Yung Tse Kwong* [2004] 3 HKLRD 192.
[6] *CIR v Yung Tse Kwong* [2004] 3 HKLRD 192, paras 11 – 20.