1984 March 17

[DEMETRIADES, J.]

IN THE MATTER OF ARTICLE 146 OF THE CONSTITUTION

PETROS DEMETRIOU AND ANOTHER,
Applicants,

v.

THE REPUBLIC OF CYPRUS, THROUGH
1. THE MINISTER OF FINANCE,
2. THE COMMISSIONER OF INCOME TAX,
Respondents.

(*Cases Nos.* 390/78, 400/78).

Income Tax—Cyprus Telecommunications Authority—Dismissal of employees "for having successfully completed their career" at a time when they had a number of years ahead for service—Regulations 9(7)(d), (15) *of the General Regulations of Personnel of the Authority—Compensation paid on account of such dismissal under regulation* 20(1)(*f*) *not a payment in respect of their employment but one in respect of the termination of their employment and is compensation for loss of office—Not liable to income tax—Section* 8(*g*) *of the Income Tax Laws,* 1961 - 1978.

Both applicants were "compulsorily dismissed" from the service of the Cyprus Telecommunications Authority ("the Authority") in accordance with the Authority's General Regulations* of Personnel after they were found that they had "completed their career successfully". Following their dismissal they were paid compensation under the provisions of regulation 20(1)(f) which provides that such compensation cannot exceed the amount of the salary which the officer would have received if he continued his service until the completion of the normal age of his retirement. The respondent Commissioner decided that

* The relevant provisions are regulation 9(7)(d), (15) and 20(1)(f) which are quoted at pp. 435–437 post.

this compensation was taxable and upon a recourse by the applicants against this decision the issue that turned for consideration was whether the lump sum received by each applicant was one falling within the provisions of section 8(g)* of the Income Tax Laws, 1961-1978, i.e. whether it was received by way of retiring gratuity or whether the payment was made to them in respect of their employment, in which case the sum concerned was liable to income tax.

Held, that although the Personnel Regulations of the Authority speak about "dismissal of an employee for having successfully completed his career", one cannot lose sight of the fact that both applicants had a number of years ahead for service in the employment of the Authority; that the relevant regulation is headed "Dismissal"; and that had they refused to accept the decision of the Promotion Board, they would, in any event, be dismissed in a couple of years as "stagnant"; that, therefore, the compensation which they received by virtue of the provisions of regulation 20(1)(f) is not a payment in respect of their employment because they had ceased to hold office, but is one in respect of the termination of their employment and is compensation for loss of office and, therefore, not liable to income tax; accordingly the sub judice decision must be annulled.

Sub judice decision annulled.

Cases referred to:

Coussoumides v. Republic (1966) 3 C.L.R. 1;

Chibbett v. Joseph Robinson and Sons, 9 T.C. 48 at pp. 60, 61;

Comptroller-General of Inland Revenue v. Knight [1972] 3 W.L.R. 594 at p. 598;

Heywood v. Comptroller-General of Inland Revenue [1975] A.C. 229;

Jennings v. Kinder (Inspector of Taxes), Hochstrasser (Inspector of Taxes) v. Mayes [1958] 1 All E.R. 369;

Hochstrasser (Inspector of Taxes) v. Mayes [1959] 3 All E.R. 817 at p. 821.

Recourses.

Recourses against the decision of the respondents whereby it was decided that the lump sum received by the applicants

* Section 8(g) is quoted at p. 438 post.

from their employers, the Cyprus Telecommunications Authority on their retirement is liable to income tax.

E. Efstathiou with *C. Loizou*, for applicant in Case No. 390/78.

C. Hadjiloannou, for applicant in Case No. 400/78.

A. Evangelou, Senior Counsel of the Republic, for the respondents.

Cur. adv. vult.

DEMETRIADES J. read the following judgment. The issue that poses for decision in these two consolidated recourses is whether the lump sum which was payable to the applicants by their employers, the Cyprus Telecommunications Authority, hereinafter referred to as "the Authority", on their retirement from service for having "successfully completed their career", is liable to income tax, as was decided by the Commissioner of Income Tax, hereinafter referred to as "the Commissioner".

Both applicants, by their respective recourses, challenge the aforesaid decision of the Commissioner and pray for a declaration that it is null and void and of no effect in that it was taken in contravention of the basic provisions of the relevant Law, the Constitution and/or in abuse of power.

The applicant in Recourse No. 390/78 bases his complaint on the following grounds of law:

(a) The decision of the respondents was based on a misconception of facts and/or on misconcepted criteria.

(b) The decision of the respondents is the product of a misconception as to the Law and/or of a wrong application of the Income Tax legislation in force.

(c) The decision of the respondents was reached in abuse and/or in excess of power.

(d) Generally the decision of the respondents was not at all and/or duly reasoned.

The applicant in Recourse No. 400/78 relies on the following grounds of law:

(a) The sum collected by him, subject matter of this re-

course, "is a sum received by way of retiring gratuity" and as such is excepted from taxation.

(b) The interpretation given by the Commissioner of Income Tax that the payment of the said sum "is for services and profits of office which are treated as deferred emoluments" is erroneous, and

(c) The lump sum payment made to applicant was paid in consideration of the release of the employers obligations under the service agreement.

Although the duties carried out by the applicants and the amount received by them as lump sum on the termination of their employment were different, I do not propose to deal with them as these facts are immaterial for the outcome of the present cases.

Both applicants were "compulsorily dismissed" in accordance with the Authority's General Regulations of Personnel after they were found that they had "completed their career successfully." The relevant provisions of the General Regulations of Personnel of the Authority, by virtue of which the two applicants were "compulsorily dismissed from service" are regulation 9(7)(d), (15) and regulation 20(1)(f), which read:-

"ΑΡΘΡΟΝ 9

7. Τὸ Συμβούλιον προσωπικοῦ, κρῖνον πρὸς προαγωγὴν, καταρτίζει πίνακας κατὰ βαθμὸν:

δ) Τῶν εὐδοκίμως περατωσάντων τὴν σταδιοδρομίαν των.

Οὐχ ἧττον οὐδεὶς δύναται νὰ περιληφθῆ εἰς τοὺς πίνακας τούτους ἐὰν δὲν συνεπλήρωσε 25ετῆ ὑπηρεσίαν, προκειμένου περὶ ἀρρένων Τομεαρχῶν καὶ Ὑποτομεαρχῶν, ἢ 20ετῆ τοιαύτην, προκειμένου περὶ θηλέων, ἢ 20ετῆ ὑπηρεσίαν, προκειμένου περὶ ἀρρένων τῶν διοφόρων ἄλλων κατηγοριῶν, καὶ 15ετῆ τοιαύτην προκειμένου περὶ θήλεος Προσωπικοῦ.

Νοεῖται ὅτι αἱ διατάξεις περὶ εὐδοκίμου ἀφυπηρετήσεως δι' ἅπαντας τοὺς βαθμοὺς τοῦ Προσωπικοῦ ἐφαρμόζονται μόνον εἰς περιπτώσεις ἀμοιβαίας συγκαταθέσεως (Ἀρχῆς καὶ Ὑπαλλήλων).

15. Οἱ κριθέντες ὡς εὐδοκίμως περατώσαντες τὴν σταδιοδρομίαν των ἀπολύονται ὑποχρεωτικῶς τῆς ὑπηρεσίας, συμφώνως πρὸς τὴν ἐν ἄρθρῳ 20 παράγραφος 1 στ. τοῦ παρόντος Κανονισμοῦ διάταξιν.

ΑΡΘΡΟΝ 20

1. Τὸ μόνιμον καὶ τακτικὸν προσωπικὸν ἀπολύεται:-

.....

στ. Κατ' ἐφαρμογὴν τῆς ἐν ἄρθρῳ 9 παράγραφος 15 τοῦ παρόντος Κανονισμοῦ διατάξεως, ἐὰν κριθῇ ὡς εὐδοκίμως περατῶσαν τὴν σταδιοδρομίαν του.

Τὸ οὕτως ἀπολυόμενον προσωπικὸν λαμβάνει ὡς ἀποζημίωσιν τόσους μηνιαίους μισθοὺς (Μισθὸς=Βασικὸς καὶ Τιμαριθμικὸν Ἐπίδομα) ὅσα τὰ πραγματικὰ ἔτη ὑπηρεσίας του. Εἰς πᾶσαν περίπτωσιν οἱ μηνιαῖοι οὗτοι μισθοὶ εἶναι οἱ ἀντιστοιχοῦντες εἰς τὴν ἀνωτάτην μισθολογικὴν βαθμῖδα τῆς μισθολογικῆς κλίμακος ἣν ἠκολούθει τὸ προσωπικὸν τοῦτο πρὸ τῆς ἀπολύσεως του, ἐν πάσῃ δὲ περιπτώσει ἡ ἀποζημίωσις αὕτη δὲν δύναται νὰ ὑπερβαίνῃ τὸ ποσὸν τῆς μισθοδοσίας του τὴν ὁποίαν θὰ ἐλάμβανε ἐὰν ἐσυνέχιζε τὴν ὑπηρεσίαν του μέχρι τῆς συμπληρώσεως τοῦ κανονικοῦ διὰ τὴν ἀφυπηρέτησιν ὁρίου ἡλικίας του".

("REGULATION 9

7. The Board of Personnel in considering for promotion prepares grading lists of:

.....

d) Those who have completed their career successfully. Nevertheless no-one can be included in these lists if he had not completed 25 years of service, in the case of male Section Head and Sub-Section Heads (Τομεαρχῶν καὶ Ὑποτομεαρχῶν) or 20 years of service, in the case of females, or 20 years service, in the case of males of various other classes, and 15 years service in the case of female Personnel.

Provided that the provisions for successful retirement for all classes of Personnel apply only in cases of mutual consent (Authority and Employees).

.....

15. Those found to have successfully completed their

career are dismissed compulsorily from the service in accor dance with the provision of paragraph 1(f) of regulation 2(of the present Regulation.

REGULATION 20

1. The permanent and ordinary personnel is dismissed:-

.....

(f) On the application of the provision of paragraph 1 of regulation 9 of the present Regulation if he is found t have successfully completed his career.

The personnel so dismissed receives as compensation s many monthly salaries (Salary - Basic and Cost of Livin Allowance) as his exact years of service. In every case suc monthly salaries are the corresponding to the highest salar point of the salary scale in which such personnel was place before its dismissal, but in any case such compensatio cannot exceed the amount of the salary which he would hav received if he continued his service until the completion c the normal age of his retirement.")

According to the evidence of Mr. N. Markides, the officer i charge of the Personnel Department of the Authority, the appl cant in Recourse No. 390/78 had limited chances of promotio as he was incapaciteated after an accident he had in the cours of his employment and, further, because of his inefficiency in th service. As regards the applicant in Recourse No. 400/78, h stated that though he was recommended by the Promotio Board for promotion, the Director-General did not agree witl the recommendation and as other employees were to be promote instead of this applicant, he was included by them in the list o employees "who had successfully completed their career"

Mr. Markides said that before both applicants were include in the list, he approached both of them, informed them of th intention of the Promotions Board and that both applicant agreed to be dismissed as having successfully completed thei career with the Authority.

This witness further said that as neither of the two applicant had any prospect of promotion, they would, after a further servi ce of two years, be dismissed as "stagnant".

The issue that turns for decision in the present two recourses is whether the lump sum received by each applicant is one falling within the provisions of section 8(g) of the Income Tax Laws, 1961 - 1978, i.e. whether it was received by way of retiring gratuity or whether the payment was made to them in respect of their employment, in which case the sum concerned is liable to income tax.

Section 8(g) reads as follows:-

"8. There shall be exempted from the tax -

.....

(g) any lump sum received by way of retiring gratuity, commutation of pension, death gratuity or as consolidated compensation for death or injuries.

....."

Counsel for the applicants argued that the payment made to the applicants was by way of retiring gratuity, whilst counsel for the respondent submitted that it was a payment made in respect of employment.

Counsel for the respondent, in support of his argument, relied on the case of *Coussoumides v. The Republic*, (1966) 3 C.L.R. 1, in which Triantafyllides J., as he then was, in delivering his judgment decided that a gratuity paid to the applicant was not received by way of retiring gratuity and, therefore, it was taxable. However, that case must be distinquished from the present cases. Coussoumides had been employed by a company as a chemist under an agreement which contained no provision at all for any gratuity or bonus payable to him on the determination of his employment and before the expiration of the term of the period of service provided in the said agreement, he decided to leave his employment in order to take up work somewhere else and requested the Managing Director of his employers to release him from his obligations under the agreement. The Board of Directors of his employers agreed to release him from his obligations and decided to give him a gratuity for his services with them.

In the present cases the applicants, with their consent, were put on the list of employees who had successfully completed their career, in which case they were, under regulation 20(1)(f) of the relevant Regulations, entitled to compensation which was

calculated in accordance with the provisions of the said regulation.

In the case of *Chibbett v. Joseph Robinson & Sons,* 9 T.C. 48, in which the same issues that arise in these two recourses were decided, Rowlatt J., in delivering his judgment, had this to say (at pp. 60, 61):-

"I think everybody is agreed, and has been agreed for a long time, that in cases of this kind the circumstance that the payment in question is a voluntary one does not matter. As Sir Richard Henn Collins said, you must not look at the point of view of the person who pays and see whether he is compellable to pay or not; you have to look at the point of view of the person who receives, to see whether he receives it in respect of his services, if it is a question of an office, and in respect of his trade, if it is a question of trade, and so on. You have to look at his point of view to see whether he receives it in respect of those considerations. That is perfectly true. But when you look at that question from what is described as the point of view of the recipient, that sends you back again, looking, for that purpose, to the point of view of the payer: not from the point of view of compellability or liability, but from the point of view of a person inquiring what is this payment for; and you have to see whether the maker of the payment makes it for the services and the receiver receives it for the services.

.....

If it was a payment in respect of the termination of their employment I do not think that is taxable. I do not think that is taxable as a profit. It seems to me that a payment to make up for the cessation for the future of annual taxable profits is not itself an annual profit at all. I do not know whether it has arisen or been discussed, and perhaps the less I say about it the better, but I should not have thought that either damages for wrongful dismissal or a payment in lieu of notice, at any rate if it was for a longish period - I will not say a payment in lieu of notice. I will say a voluntary payment in respect of breaking an agreement which had some time to run - would be taxable profits. But at any rate it does seem to me that compensation for loss of an employment which need not continue, but which was likely

to continue, is not an annual profit within the scope of the Income Tax at all."

The judgment of Rowlatt J., above, was approved by the Privy Council in the case of *Comptroller-General of Inland Revenue v. Knight,* [1972] 3 W.L.R. 594, the headnote of the report of which reads as follows:-

"The taxpayer was employed by a company as a surveyor on a service agreement which provided for determination by either party on three months' notice. In November 1965, the board of directors of the company passed a resolution that he be declared redundant as from December 1965 and be given redundancy pay at the rate of one month's salary for every year's service. The taxpayer accepted that. The Comptroller-General of Inland Revenue contended that the amount of the redundancy payment was a gratuity paid or granted in respect of his employment and therefore assessable to tax as income under section 10(1)(b) of the Income Tax Ordinance No. 48 of 1947, and made an assessment accordingly. The taxpayer appealed to the Special Commissioners of Income Tax contending that the payment was made in consideration of the abrogation of a contract of employment and was not taxable. The Special Commissioners dismissed the taxpayer's appeal but their decision was reversed by the High Court of Malaysia whose decision was affirmed by the Federal Court of Malaysia."

The Comptroller-General appealed to the Privy Council against the decision of the Federal Court of Malaysia. The issues that the Privy Council had been asked to give their advice on were the same as the questions called for decision in the present recourses. As section 8(g) of our Income Tax Laws, section 10(2)(a) of the Malaysian Income Tax Ordinance No.48 of 1947, on which the Privy Council was called upon to decide, expressly referred to "gratuities".

Lord Wilberforce in delivering the judgment in the *Knight's* case, supra, had this to say (at p. 598):-

"The question, under section 10(2)(a) of the Ordinance, is whether the money was paid 'in respect of the employment'. If the fact is that it was paid in respect of the loss of the employment, it does not come within the taxing words.

Their Lordships find support for this in the English case of *Chibbett v. Joseph Robinson & Sons* [1924] 9 T.C. 48 where a sum of £50,000 was granted by a company in voluntary liquidation to a firm of ship managers as compensation for loss of office. Although there was no specific agreement or bargain that the payment should be made as consideration for abrogating the employment, the payment was held not to be taxable. This case was later considered in *Hunter v. Dewhurst* [1932] 16 T.C. 605, and although Lord Macmillan, in the House of Lords, found some of the words used by Rowlatt J. too widely expressed, the actual decision seems not to have been disapproved. Their Lordships consider it a right decision in law.

.....

Section 10(2)(a) certainly refers expressly to gratuities. But it remains the case that, in order to be taxable, a gratuity must be paid in respect of the employment - many gratuities are so paid such as 'tips' and these no doubt are taxable. If the gratuity is not so paid, but is paid in respect of the termination of his employment, it is not taxable."

The judgment in the *Knight's* case, supra, was applied by the Privy Council on appeal from the Federal Court of Malaysia, in *Heywood v. Comptroller-General of Inland Recenue,* [1975] A.C. 229.

What is a profit arising from a taxpayer's employment has been clearly defined by Upjohn J. in delivering his judgment in the case of *Jennings v. Kinder* (*Inspector of Taxes*), *Hochstrasser* (*Inspector of Taxes*) *v. Mayes,* [1958] 1 All E.R. 369. His dictum that "..... to be a profit arising from employment, the payment must be made in reference to the service the employee renders by virtue of his office, and it must be something in the nature of a reward for services past, present or future", was cited with approval by Viscount Simonds when the *Hochstrasser* case, supra, came before the House of Lords (see *Hochstrasser* (*Inspector of Taxes*) v. *Mayes,* [1959] 3 All E.R. 817, 821) despite the fact that His Lordship had reservations as to the use of the word "past".

In the present cases, although the Personnel Regulations of the Authority speak about "dismissal of an employee for having

successfully completed his career", one cannot lose sight of the fact that both applicants had a number of years ahead for service in the employment of the Authority; that the relevant regulation is headed "Dismissal", and that had they refused to accept the decision of the Promotion Board, they would, in any event, be dismissed in a couple of years as "stagnant".

It is my view, therefore, that the compensation which they received by virtue of the provisions of regulation 20(1)(f) is not a payment in respect of their employment because they had ceased to hold office, but is one in respect of the termination of their employment and is compensation for loss of office and, therefore, not liable to income tax.

In the light of my above findings, the sub judice decisions are declared null and void and of no legal effect, but in the circumstances of the cases and, in particular, in view of the novelty of the issues raised in the present recourses, I make no order as to costs.

Sub judice decisions annulled. No order as to costs.