IN THE SUPREME COURT OF HONG KONG

HIGH COURT

(INLAND REVENUE APPEAL NO.4 OF 1996)

BETWEEN

EXTRAMONEY LIMITED Appellant

and

COMMISSIONER OF INLAND REVENUE Respondent

Coram : Hon Patrick Chan J. in Court

Date of Hearing : 19th December 1996
Date of Decision : 28th February 1997

D E C I S I O N

Upon the application of Extramoney Ltd. ("the taxpayer"), the Board of Review ("the Board") has stated a case for the determination of this court pursuant to s.69 of the *Inland Revenue Ordinance, Cap.112* ("the *Ordinance*").

The facts

The facts as agreed by the parties and found by the Board are hardly in dispute and can be summarised as follows.

The taxpayer was incorporated as a private company on 4th December 1979. At the material times it was owned by some of the subsidiary or associated companies of Carrian Holdings Ltd. ("Carrian Holdings") including Carrian Finance Ltd. ("Carrian Finance") and Carrian Realty Ltd. ("Carrian Realty"). These companies together with another subsidiary were also at all material times the directors of the taxpayer. They were

owned and/or controlled by Mr George Tan and his associate Ms Carrie Woo either through shareholdings or as directors.

On 3rd November 1981, in the absence of any profits tax return for 1980/81, the assessor estimated the assessable profits to be $500,000 with tax payable at $82,500. The taxpayer did not raise any objection to this assessment.

On 9th January 1982, the taxpayer submitted its profits tax return for the year ended 31st December 1980. The return disclosed assessable profits of $132,881,885, consisting of the following :-

(a) dividends received of $7,664,464;
(b) share dealing profits of $182,096,691;
(c) management and finance fee paid $46 million; and
(d) dividend paid $90 million.

The auditor's report was not qualified in any way and stated that the accounts "give a true and fair view" of the state of affairs of the taxpayer at 31st December 1980. The assessor accepted this return. On 15th January 1982, he assessed the additional assessable profits at $132,381,885 and tax payable at $21,843,011. No objection was raised against the additional assessment. On 13th April 1982, Carrian Holdings paid the tax plus a 5% surcharge of $1,092,150.

On 25th November 1983, joint liquidators were appointed for Carrian Holdings.

On 31st March 1987, solicitors for the taxpayer and the joint liquidators requested the assessor to correct an error or mistake in the profits tax return for the year 1980/81 pursuant to s.70A of the *Ordinance*. The basis of the tax payer's claim was that the disclosed profits in that profits tax return had been mis-stated due to the fraudulent conduct of its former director Mr Tan acting in breach of his fiduciary duty to the taxpayer. It was alleged that the taxpayer never made such profits which were fictitious and had been fraudulently and falsely declared. The tax was paid by Carrian Holdings in order to maintain the illusion.

In 1987, the taxpayer and Carrian Holdings commenced action against the auditors for negligence in High Court Action No.A8437 of 1987. In that action, it was complained that the auditors were negligent in their audit of the taxpayer's 1980/81 accounts in that they failed to qualify the accounts but declared that those accounts presented a true and fair view of the affairs of the taxpayer. The action was tried before Deputy Judge Fung Q.C. who held that the auditors were negligent but that such negligence did not cause any damage to the taxpayer and Carrian Holdings. He awarded only nominal damages.

It is not in dispute that the profits which were declared in the taxpayer's 1980/81 accounts and which were alleged to have been mis-stated, were not included in the accounts of any of the other companies within the group, and that none of these companies except Carrian Holdings had paid tax for those profits.

Apart from the above facts, the only evidence presented before the Board was a copy of the judgment in the High Court Action.

Decision of the Board

The Board took the view that the Deputy Judge in the High Court Action had expressly refrained from making any finding or decision which would be binding on the Board. He was then dealing with different issues of fact and points of law and his judgment was nothing more than evidence which could be placed before the Board for consideration. It was up to the Board to make its own findings of fact and draw its own conclusion.

The Board also found that when the 1980/81 profits tax return was filed by the taxpayer with the Commissioner for Inland Revenue, it was a deliberate decision to attribute the stated profits as being profits made by the taxpayer. It was not uncommon for the purpose of taxation to have profit transferred from one person to another. It was for the taxpayer to show that it had made an error by so attributing profits which were not made by the taxpayer to be profits so made. There could be many reasons for that but no evidence or explanation was given by the taxpayer as to why there should be such an attribution. The Board also noted that there was nothing in the documents showing how the error came about.

The Board therefore came to the conclusion that the taxpayer had failed to discharge the onus of showing that the inclusion of the profits in question was an error within the meaning of s.70A of the *Ordinance*.

The questions of law for determination

The questions of law stated for the opinion of this court are framed as follows :-

(i) whether, in view of the evidence before the Board, the decision of the board is so perverse that as a matter of law it cannot stand; and that the true and only reasonable conclusion which could be drawn from the facts contradicts the Board's decision;

(ii) whether, as a matter of law, the Board was correct in refusing to hold that the Commissioner was estopped from denying the truth of the factual matters found by the Judge in High Court

Action No.8437 of 1987 in so far as those matters bore upon the subject of the taxpayer's appeal to the Board.

Issue estoppel

I shall deal with the second question first since the answer may affect the premises upon which the first question is to be considered. The second question is in essence whether issue estoppel can operate against the Commissioner in the present case.

Counsel's arguments

Before me, counsel for the taxpayer did not seek to present any strong argument on this point, content with the criticism that the Board had wrongly rejected the evidence which was the clear findings of fact by the Deputy Judge in the High Court Action. That, of course, is a separate matter.

Counsel for the Commissioner urged me to make a ruling on this point for future guidance. He argued that by s.68(7) of the *Ordinance*, the Board of Review is not limited in the evidence it may receive or the facts it may find on the evidence. Hence issue estoppel would run contrary to the statutory scheme by which an appeal against an assessment is to be determined. He referred to s.68(3) which provides that the assessor shall attend the meetings of the Board of Review in support of the assessment. Counsel relied on authorities which held that the Crown should not be prevented from performing its public duty and cannot be estopped from exercising its power or discretion which it is its duty to exercise. In any event, he argued that the conditions for an issue estoppel in the present case were not satisfied. There was no identity of the subject matter, parties and issues in the High Court Action and the proceedings before the Board of Review. In the counterclaim made by the taxpayer in the High Court Action against the Commissioner, the court held that there was no jurisdiction to grant the relief sought by the taxpayer.

The High Court Action

It appears that in the High Court Action, the main action was between the taxpayer and Carrian Holdings as plaintiffs and the auditors as defendants. The claim was based on negligence. The auditors had lodged a counterclaim against the taxpayer, Carrian Holdings and the Attorney General representing the Commissioner of Inland Revenue. The declarations they sought in the counterclaim were, among other things, that the profits in question were mis-stated by Mr George Tan, that the assessor had made his assessment on the basis of fraudulent information, that the taxpayer and Carrian Holdings were entitled to repayment by the Inland Revenue Department of the tax already paid and that they should prosecute an appeal from such assessment to the Board of Review with due diligence.

The learned Deputy Judge held for the reasons given by him that the auditors were negligent but that the taxpayer and Carrian Holdings had failed to prove that such

negligence had caused them loss and damage and hence only nominal damages could be awarded. With regard to the counterclaim, the judge, having looked at the statutory scheme provided in the *Ordinance*, dismissed it for want of jurisdiction. There was no adjudication on the merits of the counterclaim.

In my view, the learned Deputy Judge had correctly held that there was no jurisdiction in the High Court to grant the declaratory relief sought by the auditors. As he said, the *Ordinance* has provided a very comprehensive statutory scheme with regard to assessment of profits tax, objections to assessment, appeals to the Board of Review and appeals by way of case stated to the High Court. Such procedures have to be followed step by step except as provided otherwise by the *Ordinance*.

Applicability of principles in this case

What is argued in the present case is not whether there can be an estoppel by reason of the result in the main action or the dismissal of the counterclaim, but whether the findings and rulings made by the Deputy Judge in the main action are binding on the Commissioner in the present proceedings so that the Board should follow those findings and rulings.

I think counsel for the Commissioner is right in saying that the conditions for an issue estoppel have not been satisfied in the present case. Certain conditions have to be satisfied before issue estoppel can arise.

> "The conditions for the application of the doctrine have been stated as being that :
>
> (1) the same question was decided in both proceedings;
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> (2) the judicial decision said to create the estoppel was final; and
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> (3) the parties to the judicial decision or their privies were the same persons as the parties to the proceedings in which the estoppel is raised or their privies."

(See *Halsbury's Laws of England, Vol 16*, para 977)

In the main action in the High Court Action, the parties were the taxpayer, Carrian Holdings and the auditors. The main issue was whether the auditors were negligent in the performance of their duties towards the taxpayer and Carrian Holdings. It is true that during the trial, evidence was adduced to show that the profits were not made by the taxpayer but were attributed to it in its profits tax return. However, while the Commissioner was present in the proceedings as a defendant in the counterclaim, it took no part in the main action. In other words, the parties are different. The issues are different. The conditions for issue estoppel have not been satisfied. That being the case, it is quite clear that no issue estoppel could arise before the Board.

Can the Crown ever be estopped ?

I accept that as a matter of general principle, the Crown, in this case the Commissioner of Inland Revenue, is usually not estopped from carrying out its statutory obligation. It cannot be prevented either by agreement or otherwise from discharging its duties under statute. However, I do not think it can be said that the Crown is under no circumstance subject to an estoppel. Where in a previous court proceeding in which the Crown was involved as a party and had taken active part in it, I should think that the usual principle of issue estoppel may apply as between the Crown and the party to that previous proceeding in relation to issues and/or subject matters which had been fully ventilated in that proceeding where the court had made a finding either on the facts or on the law. The purpose of the doctrine of issue estoppel is not only to save time and costs, but also to ensure finality of litigation and consistency of decisions. It is only common sense that the same parties to a proceeding, and these include the Crown, should be bound in any subsequent proceeding by a finding made by the court in the first proceeding. I do not think the Crown should be put in a better position than an ordinary litigant and be entitled to re-litigate the issues again before another court under the excuse that it is discharging a statutory duty.

Section 68(3) of the *Ordinance* provides :-

> "The assessor who made the assessment appealed against or some other person authorised by the Commissioner shall attend such meeting of the Board in support of the assessment."

This provision clearly requires the assessor to attend any hearing before the Board. It is his duty to do so. He is duty bound to assess profits tax and if his assessment is being challenged, to explain how he arrives at the assessment and if he maintains his view, to support it. However, I do not agree that such a duty to attend a hearing before the Board of Review would have the effect of allowing the assessor to canvass over the same issues or facts which had been fully and properly canvassed before another competent court in a case between the Commissioner and the taxpayer and that other competent court had already made an adjudication on those issues or facts. While he is under a statutory duty to assist the Board, I do not think such duty entitles him to abuse any adjudication process. The powers, functions and procedures of the Board are of course different. But if the issues and facts are the same, why should the Crown be better off than the taxpayer and have a second bite of the cherry? Why should the Board waste time to rehearse over the same subject matter which has already been decided by a competent court between the same parties ? Hence, at a hearing before the Board of Review, unless there are matters which come to light after the previous adjudication and which could not, with due diligence, have come to the knowledge of the parties, I am inclined to think that the Commissioner should not be allowed to re-litigate on the same issues or facts.

However, while I believe that there may be cases in which the Crown is also subject to issue estoppel, I do not think this is such a case for the reasons which I have given. In my opinion, the Board was correct in refusing to hold that the Commissioner was estopped by the findings of fact of the Deputy Judge in the main trial in the High Court Action. The judgment is, as the Board correctly held, only a piece of evidence which the Board may take into consideration.

Taxpayer's main grounds

In respect of the first question stated by the Board for the determination of this court, the taxpayer has put forward two main grounds of argument. First, the Board had a number of misconceptions of law *ex facie*. The High Court should therefore allow the appeal without inquiring into whether the facts of the case could otherwise have justified the Board's decision. Second, even if there was no misconception of law, the Board's decision was inconsistent with and contradictory to the evidence which was before the Board and hence the decision was one which a properly instructed tribunal acting judiciously could not have reached.

Facts found by the Deputy Judge

In view of the taxpayer's arguments, I should perhaps set out the findings of fact made by the Deputy Judge in the High Court Action. These findings are of relevance to the present case and had in fact been referred to by the Board in its deliberation. The more salient findings can be summarised as follows :-

(1) The appellant was a share dealing company engaged in the buying and selling of publicly quoted shares, being those of Carrian Holdings' listed subsidiary, Carrian Investment Ltd. (p.65 of the judgment);

(2) The profits in question were merely a single line journal entry in the books of the taxpayer, described as profits made by Mr Tan on behalf of the taxpayer from the sale of an unspecified number of the shares in Carrian Investment (p. 65);

(3) There was no independent supporting document verifying the underlying transactions said to have given rise to the profits (p. 66);

(4) The profit had in fact been generated by the sale and purchase shares in Carrian Investment (page 83);

(5) The documentary evidence overwhelmingly suggested that such profits were not made by the taxpayer (p. 84);

(6) Mr Tan decided to attribute the profits as having been made by the taxpayer (p. 93);

(7) Mr Lai of the auditors testified to the effect that he had asked Mr Tan and Mr Tan made certain oral representations to him to the effect that the taxpayer had made the profits. This, as the Deputy Judge held, can only be evidence of the fact that Mr Lai had raised the matter with Mr Tan but cannot be admissible evidence of the fact that the profits were or were not made by the taxpayer (pp. 103-104).

Any misconceptions of law ex facie

Counsel submitted that the Board had made a number of misconceptions of law ex facie.

Effect of Deputy Judge's findings of fact

Counsel for the taxpayer submitted that the Board was wrong in law to reject the facts found by the Deputy Judge in the High Court Action in so far as those facts bore upon the subject of the taxpayer's appeal to the Board.

With respect, I do not think that can be a valid criticism. The Board had clearly in paragraph 8.11 said that it might refer to the judgment of the Deputy Judge as evidence but no more than that. There is nothing in the reasons given by the Board to indicate that it had rejected the facts found by the Deputy Judge. It only said that the judgment was in no way binding on the Board and was one of the many pieces of evidence which the Board must carefully consider. In my view, that must be correct. As a matter of fact, the Board did refer to and rely on the findings of fact made by the Deputy Judge. This is clear in paragraph 8.17.

Materials to be looked at

Counsel submitted that the Board was wrong in law when it said that all that it had to do when considering the appellant's case in the context of s.70A of the *Ordinance* was :-

> "to look at the tax return and the audited accounts filed therewith and see whether or not for taxation purposes, there was an error." (paragraph 8.14)

With respect, I do not think that is a fair criticism either. This statement must be looked at in the context of the whole decision of the Board. It had earlier remarked that the taxpayer chose not to adduce any evidence except the judgment of the Deputy Judge. There was no other evidence including any explanation from Mr Tan or Mr Ho as to why certain profits had been attributed to be the profits of the taxpayer. It is under those circumstances that the Board said that it must look at the tax return and the audited accounts to see whether there was any error or omission. I do not think the Board

went as far as to say that in every case touching upon s.70A, the only evidence which must be looked at was the tax return and the materials submitted by the taxpayer. There are statutory provisions regarding how the Board of Review is to receive evidence in relation to such matters. It is also the decision of the Board, and its decision alone, with regard to such matters.

Any wrong interpretation of "errors or omissions"

The taxpayer's main submission is that the Board was wrong in law in giving a narrow interpretation to the words "errors or omissions" in s.70A of the *Ordinance*.

Purpose of the section

A taxpayer is under an obligation to submit an accurate tax return. The assessor is under a statutory duty to make an assessment. In doing so, the assessor is entitled to rely on the tax return and the materials submitted to him by the taxpayer. There is machinery within the *Ordinance* for the taxpayer to raise objection against the assessment and for the assessor to impose additional tax upon receipt of further information or material. Within the comprehensive scheme provided by the *Ordinance*, there should be finality. Hence s. 70.

However, s.70A of the *Ordinance* provides for an exception and allows for errors and omissions to be corrected. It confers upon the assessor a power to be exercised within six years of the tax year in question to correct the original assessment if it can be established that it :-

> "is excessive by reason of an error or omission in any return or statement submitted in respect thereof or by reason of any arithmetical error or omission in the calculation of the amount of the assessable income or profit assessed or in the amount of the tax charged."

The purpose of s.70A is to avoid possible hardship arising from mistakes made by either the taxpayer or the assessor. As the Board of Review said in IRBD No.D6/91 :-

> "Clearly there must be finality in taxation matters. That is the clear intention of s.70. The Commissioner is entitled to accept the truth of tax returns made by the taxpayers. If an individual submits a return or statement to the Commissioner which says that he is liable to tax, then it is reasonable that the Commissioner should assess the individual to tax and that should be an end of the matter.
>
> Section 70 of the Inland Revenue Ordinance states that assessments are to be final and conclusive for all purposes of the

> *Ordinance*. That is a sweeping and draconian section. It is clear that s.70A was introduced to overcome the possible hardship of s.70."

Burden on taxpayer

The burden is obviously on the taxpayer to show that the assessment was excessive by reason of an error or omission in the tax return or statement submitted by him. After all, they were his documents. Macdougall J. (as he then was) in Inland Revenue Appeal No.2 of 1985 said :-

> "If a taxpayer wishes to challenge the accuracy of his own audited statements and tax declarations made by a ... director, it is not sufficient merely to say that ... a mistake was made ... Evidence to substantiate the mistake must be given in the strongest terms."

Errors or omissions

There is no definition of "errors or omissions" in the *Ordinance*. But it is clear that not every error or omission falls within s.70A and is accepted for the purpose of this section.

Counsel for the taxpayer submitted that the Board was wrong in law to hold that a deliberate error was not a relevant error within the meaning of s.70A. It was argued that it was still an error even though it was a deliberate act unless it was prompted by improper motive. Counsel referred to the meanings of "error" in the **Oxford English Dictionary** and the cases of **Radio Pictures Ltd v. Commissioner of Inland Revenue** [1937] 22 TC 106 and **F.C.T. v. Hayden** (1944) 7 ATD 440. He argued that the evidence placed before the Deputy Judge showed that the profits in question were not made by the taxpayer but were attributed to it by Mr Tan. Since there was no finding of any fraud on the part of Mr Tan, it must follow that the inclusion of the profits in the taxpayer's accounts was an error.

This section seems to draw a distinction between two types of errors or omissions - those which are arithmetical and those which are not arithmetical. There is usually no problem in identifying the first type of errors or omissions, i.e., arithmetical errors or omissions. It is the second type which will present some difficulty since it covers a variety of situations. I think it would be unwise to attempt to give a comprehensive definition of what is or is not an error or omission which can cater for all situations. It would be easier to identify cases in which it is not.

In my view, for the purpose of s.70A, the meaning of "error" given in the **Oxford English Dictionary** (p.277) would be appropriate, that is, "something incorrectly done through ignorance or inadvertence; a mistake". I do not think that a deliberate act in the sense of a conscientious choice of one out of two or more courses which subsequently

turns out to be less than advantageous or which does not give the desired effect as previously hoped for can be regarded as an error within s.70A. It is even worse if the deliberate act is motivated by fraud or dishonesty. But the question of fraud or dishonesty need not arise.

Hence, in the context of the present case, if there is a change of opinion of the auditors or accountants in respect of the accounts, the first opinion cannot be regarded as an error or omission within the section. Similarly if there is a change of mind of the directors of the company in connection with how any part of the accounts should be made up, the previous decision will not be regarded as an error or omission. Nor is it an error or omission if it is merely a difference in the treatment of certain items in the accounts by those preparing or approving the accounts. If this were permitted, the director or officer of a company will be tempted at a later stage to try and "improve" the company's accounts or change his own decisions if this is to his advantage. This would be contrary to the spirit of the *Ordinance* that there should be finality in taxation matters. The whole statutory scheme provided in the *Ordinance* simply cannot work.

The act in this case

I accept that in some cases where it can be proved that the profits stated in the accounts of a taxpayer had in fact not been made, this may be sufficient to show that there has been an error justifying a correction in the assessment. However, each case must be considered in its own factual matrix. The present case is clearly distinguishable. Here, the evidence adduced in the trial of the High Court Action showed that the profits in question *had indeed been made* although probably not by the taxpayer and yet such profits were not shown in the accounts of any of the companies within the group but were attributed as profits made by the taxpayer. The attribution was a deliberate and conscientious decision.

From the materials before the Board, including the judgment of the Deputy Judge, I think the Board is entitled to come to the conclusion that it was the liquidators of the Carrian Holdings who, having investigated the affairs of the company and those of the taxpayer and other subsidiaries within the group, formed the opinion that the disputed profits should not have been shown as having been made by the taxpayer. In other words, the liquidators either did not agree with Mr Tan's decision or did not know why Mr Tan had decided to attribute those profits to the taxpayer. Nevertheless, it was a deliberate and conscientious decision of the persons having control of the affairs of the taxpayer and its parent and associated companies to attribute the profits to the taxpayer.

Where a taxpayer had deliberately and conscientiously made a decision to attribute a certain item, be it an item of profit or expenditure, in the tax return to be submitted to the assessor for assessment, if he subsequently changes his mind, that certainly cannot be an error within the meaning of s.70A of the *Ordinance*. In my view, the Board of Review had adopted the correct principles.

Whether the Board's decision unreasonable

Counsel for the taxpayer further submitted that the decision of the Board was one which no properly instructed board acting judiciously could have reached. It was argued that the Board was wrong to say that the only person who was in a position to give evidence to establish an error would be those who carried out the transaction. Counsel submitted that the Board had also wrongly rejected the clear findings of the Deputy Judge and taken irrelevant matters into consideration.

The burden is squarely on the taxpayer to show that there was an error falling within s.70A. The taxpayer did not see fit to adduce any evidence apart from the judgment in the High Court Action. The findings of the Deputy Judge were part of the materials placed before the Board. It cannot be said from the Decision of the Board that it had not taken those findings into consideration. In fact, it had specifically referred to some of them. Even taking all of the findings into consideration, all that could be proved before the Board was that the profits in question which were indeed made were probably not made by the taxpayer but attributed to be its profits as a result of a deliberate and conscientious decision of Mr Tan. There could be many reasons for this decision. It could be a genuine mistake. It could be a considered commercial decision. It could be part of a scheme to reduce the group' s tax liability. Mr Tan could even be wise after the event. But if it was claimed that what was done was an error, he should come out and explain what sort of mistake he had made and why he had done so.

As the Board quite rightly pointed out, it is common for a transfer of profits from one company to another or from one person to another. If a director of a number of companies has decided, deliberately and conscientiously, to transfer profits from one company to another within his group of companies, he cannot be heard to say some years later because of perhaps a tax advantage, that he should not have made that decision. He cannot be heard to say that his decision was an error or omission. That is not the intention of s.70A. In the present case, it is not disputed that there is no evidence that the profits had been shown in the accounts of any other company. I should think that even if he had come out, he might have some difficulty in offering a satisfactory explanation. In the circumstances of this case, it would, in my view, need a cogent explanation to satisfy the assessor that it was an error or omission.

In any event, in the absence of any explanation from the person who had made the decision to compile the taxpayer's accounts in the way they were, and in the absence of any evidence showing that the profits should have been attributed to any particular company within the group, I think the Board was entitled to conclude that the taxpayer had not discharged the onus of proving that there was an error within the meaning of s.70A. I would even say that that was probably the only reasonable conclusion.

Having considered all the materials before the Board, I do not think it can be said that the Board had come to a conclusion which a properly instructed Board acting judiciously could not have come to.

Conclusion

For the reasons which I have set out, the answers to the two questions stated by the Board must be no and yes respectively. The appeal must be dismissed. I make an order *nisi* that the appellant should pay the costs to the Commissioner. Finally I would like to thank both counsel for their very well-researched and well-argued submissions.

(Patrick Chan)
Judge of the High Court

Mr Gordon Fisher, inst'd by M/s Simmons & Simmons, for Appellant

Mr Robert Andrew, Crown Solicitors, for Crown/Respondent