

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. BR 80/76

Board of Review:

L. J. D'Almada Remedios, *Chairman*, D. Barrett, W. I. Cheung, & Lawrence H. L. Fung, *Members*.

14th March 1978.

Additional tax – failure to disclose profits derived from sale of land – taxpayer's honest belief that sale was not trading transaction – reliance on professional advice – whether taxpayer liable to a penalty assessment under section 82A of the Inland Revenue Ordinance – whether there was reasonable excuse.

The appellant failed to include profits derived from selling two pieces of land in the New Territories in his tax returns and in consequence additional tax assessed on such profits was charged to him under section 60 of the Inland Revenue Ordinance. An assessment to additional tax under section 82A which was in the nature of a penalty was then raised against the appellant.

On appeal against the penalty assessment the appellant contended that there was reasonable excuse for the incorrect return in that he had honestly believed the sales were not trading transactions and therefore the profits derived therefrom were not taxable. Furthermore, he had relied on the advice of qualified accountants whom he had employed to look after his tax affairs.

Decision: Appeal allowed. Penalty assessment set aside.

M. Jackson-Lipkin Q.C. for the appellant.

D. O'Dwyer for the Commissioner of Inland Revenue.

Reasons:

A person who without reasonable excuse makes an incorrect return by omitting or understating his profits is liable to be assessed under section 82A of the Inland Revenue Ordinance to additional tax in a sum not exceeding treble the amount of tax which he had been undercharged in consequence of such incorrect return. The Revenue's case is that the Appellant had failed to include profits derived from the sale of two properties in the New Territories (which we will hereafter refer to for convenience as Lots. DD300 and DD131) in returns which he had submitted for the year of assessment 1973/74 and 1974/75. The amount of tax undercharged in consequence of such incorrect returns is \$473,674.00 in respect of both these years of assessment. The Appellant has since paid this sum in tax and

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the Revenue now seeks to impose additional tax amounting \$156,000.00. This additional tax is in the nature of a penalty which we will hereafter for convenience refer to as the 'penalty assessment'.

The Appellant now appeals against the penalty assessment on the grounds that the incorrect return was not made deliberately and as there was reasonable excuse he is not liable under the section.

At the hearing a Statement of Agreed Facts was produced. It contained, *inter alia*, the following paragraph:-

“12. The Commissioner does not contend that the Appellant deliberately omitted the profits in question with the intent to defraud the Inland Revenue of the tax payable.”

As there can be no penalty assessment under Section 82A unless the incorrect return was made “without reasonable excuse” Mr. Jackson-Lipkin Q.C. (appearing for the Appellant) made it clear at the outset that the result of this Appeal turns on the narrow issue of whether, in the circumstances of this case, there was “reasonable excuse.”

In justification of the Appellant's plea, the facts before us can be summarized as follows:-

The Appellant is aged 73. He is a property dealer. He also holds properties for investment purposes. He speaks no English and does not understand accounts. For a number of years Messrs. Lowe Bingham & Matthews acted as his accountants. All his tax affairs were handled by that firm. He pays them a retainer for attending to all his affairs and they are instructed to look after his accounts and submit all returns to the Inland Revenue Department. He gives to them all necessary information relating to his transactions and they have his authority to direct enquiries from his solicitors for any other information they may require. In 1960 and 1961 he purchased plots of land in the New Territories comprised in DD300 and DD131. He states in evidence that they were bought as an investment, his intention being to build bungalows for rental income and a hotel for a summer resort. When the Assessor queried the purpose of his purchase the same information was given by his accountant to the Assessor in 1962. These plots were agricultural land. He applied for a conversion permit and also had plans prepared for developing the land, but during the period in which he held the land he received no positive reply from the Government in regard to his application. Subsequently, the Government decided to resume part of the land in order to build a road from Castle Peak to Yim Tim and his land was then divided into two parts. When an approach was made for him to dispose of the land he decided to do so. At the time of sale the land was still agricultural land although it would appear that after the sale conversion was permitted resulting in a land being part of Pearl Island Development scheme.

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The land was held by the Appellant for upward of 12 years prior to sale. In 1975 it came to the knowledge of the Revenue that these lots were sold and queries were addressed to the Appellant's accountants to which apparently no reply was received. The Appellant then decided to change his accountants and when Messrs. C. C. Choy & Co. were appointed to act in the place of Messrs. Lowe Bingham & Matthews there were difficulties in obtaining or locating from his former accountants the files, paper and accounts relating to these lots. Additional assessments under section 60 for profits tax derived from the sale of these plots were then raised against the Appellant. The Appellant's new accountant did not object to these raised assessments and, indeed, appear to have conceded that the profits made were assessable to tax. As the additional assessments were not appealed against they became final and conclusive. The Appellant again changed his accountants and instructed Messrs. K. K. Young and Co. to act in place of Messrs. C. C. Choy & Co.

In giving evidence the Appellant stated, *inter alia*,: (a) that from the inception of the purchase and at all times even up to the present time he did not believe that he was liable to profits tax on the sale of these lots as they were not purchased with a view to re-sale at a profit but for investment; (b) that he provided to his accountants Messrs. Lowe Bingham & Matthews with all necessary information regarding these lots and all his transactions and tax affairs and he answered all queries and questions put to him by Messrs. Lowe Bingham & Matthews truthfully; (c) that his belief that the profits derived on sale on these properties are not taxable was also shared by Mr. B. J. Young the accountant of Messrs. Lowe Bingham & Matthews who handled his tax affairs, and (d) that he did not know and was not aware that Messrs. C. C. Choy & Co. had conceded that the sale of these properties was taxable and that he only came to know of it when he received the tax demand note. The Appellant's evidence as to (a), (b), (c) & (d) above was not challenged and no questions were put to him in regard thereto which was assumed is accountable by reason of the Revenue's acceptance that the Appellant had no intention to deliberately defraud the Inland Revenue.

At the close of the Appellant's case the representative for the Commissioner elected to call Mr. B. J. Young formerly of Messrs. Lowe Bingham & Matthews to give evidence. The evidence of Mr. B. J. Young in no way assisted the Revenue's case.

Mr. Young clarified the manner in which he took instructions from and his contacts with the Appellant. In regard to computations which he prepared they were explained in detail to the Appellant. His evidence included queries he put to the Appellant in regard to these lots that were sold and on information received it was Mr. Young's view that these were not trading transactions and he so advised the Appellant. For these reasons the gains made on these transactions were not included by him in the returns which were filed on behalf of the Appellant.

On the evidence before us it was submitted by counsel for the Appellant that in the circumstances of this case a penalty assessment is not justified as there is 'reasonable excuse'. We agree. If the Appellant honestly believed that the sales were capital transactions this would amount to reasonable excuse since returns need not include profits

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or losses in transactions involving capital assets. The Appellant does not understand accounts and he employs professional accountants to advise and deal with these matters. It would seem to us that reliance on the advice of an expert could also amount to reasonable excuse within the meaning of the section.

Finding as we do that when the returns were filed neither the Appellant nor his accountant believed that these transactions were trading transactions and that this belief was honestly entertained (whether rightly or wrongly) a penalty assessment does not become exigible for reasons which we have stated. This appeal is, therefore, allowed and the penalty assessment set aside.