Case No. D104/96

Penalty tax – omission from tax return of part of salary – omission claimed to be simple mistake due to wrongly copying income figures provided by employer for the previous year of assessment – whether penalty tax of 25% excessive in the circumstances – Inland Revenue Ordinance sections 82A and 82B.

Panel: Andrew Halkyard (chairman), Erwin A Hardy and Victor Hui Chun Fui.

Date of hearing: 16 January 1997.
Date of decision: 17 March 1997.

In his 1993/94 tax return the taxpayer omitted an amount of salary. Upon challenge by the Commissioner, the taxpayer claimed that he simply made a mistake by copying into his tax return income figures provided to him by his employer for the previous year of assessment. Penalty tax was raised on the taxpayer in the amount of approximately 25% of the tax which would have been undercharged if the omission of income had not been detected.

Held:

(1) A 25% penalty tax is not appropriate in *all* cases of neglect or carelessness where an individual omits income from his or her tax return. However, without good reason the Board should not second guess the Commissioner simply because its inclination would be to conclude that the penalty is more than it would have imposed.

(2) On the basis of unchallenged oral evidence, it appeared that the taxpayer had a good compliance record and that he had been careless on a single occasion by wrongly copying in his tax return his salary from his employer's return in relation to the previous year of assessment. Although carelessness is not a reasonable excuse, it equally did not justify a penalty tax of 25%. On the facts of the present case, and bearing in mind that consistency in tax appeals is desirable, the penalty tax was reduced to 10% (D8/96, IRBRD, vol 11, 400 followed).

Appeal partly allowed.

Cases referred to:

Cheng v CIR (1979) 1 HKTC 1087
D15/89, IRBRD, vol 4, 252

D4/94, IRBRD, vol 9, 75
D52/95, IRBRD, vol 11, 7
D8/96, IRBRD, vol 11, 400
D25/96, IRBRD, vol 11, 478

Yip Sham Yin Har for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

This is an appeal against an assessment for the amount of additional or penalty tax imposed by the Commissioner under section 82A(1) of the Inland Revenue Ordinance.

The facts

The following facts are not in dispute

1. In the Tax Return – Individuals for the year of assessment 1993/94, the Taxpayer declared the following particulars of income:

Employer:	Association X
Capacity in which employed:	Teacher
Salary/Wages (1.4.1993 to 31.3.1994):	$104,475

2. An employer's return files with the Inland Revenue Department in respect of the Taxpayer revealed that the Taxpayer had the following sources of income for the year of assessment 1993/94:

Employer	**Period of Employment**	**Amount**
Association X	1.4.1993 to 31.3.1994	$203,955

3. On 11 October 1994 the assessor raised the following salaries tax assessment on the Taxpayer for the year of assessment 1993/94:

Self Income	$203,955

4. The Taxpayer did not lodge any objection to this assessment.

5. On 24 August 1995 the Commissioner gave a notice to the Taxpayer under section 82A(4) that he proposed to assess the Taxpayer to additional tax by way of penalty in respect of the year of assessment 1993/94 for making an incorrect return by omitting part of the income disclosed at fact 2. The notice was addressed to the Taxpayer at c/o

Association. For reasons which are not known, this notice was not delivered to him. The Taxpayer did not, therefore, make any representations to this notice.

6. On 10 November 1995 the Commissioner issued an assessment for additional tax in respect of the year of assessment 1993/94 in the sum of $5,500. This amount is approximately 25% of the tax which would have been undercharged if the Taxpayer's omission of chargeable income from his return had not been detected. This notice of assessment was not delivered to the Taxpayer (compare fact 5) until 8 March 1996, when a copy was given to him.

7. On 23 March 1996 the Taxpayer appealed to this Board against the assessment of additional or penalty tax on the ground that the amount imposed was excessive. Apart from explaining why he did not receive the section 82A(4) notice from the Commissioner, the Taxpayer simply stated that he 'mistakenly' wrote down his total payroll emoluments of $104,475 according to the tax information given to him by his employer for the previous year of assessment 1992/93. He requested the Commissioner to 'accept my apology for filling in the return incorrectly out of mistake'.

Preliminary issues before the Board

With the assistance of the Commissioner's representative, Mrs Yip Sham Yin-har, we have found that in terms of section 82B(1) the notice of assessment to additional tax was not given to the Taxpayer until 8 March 1996 (fact 6 refers). On the basis of this finding, we decided that the Taxpayer's notice of appeal was given in time and that we had jurisdiction to hear the substantive issue in dispute in this case.

In opening his case, the Taxpayer initially endeavoured to rely upon the argument that the assessment should not stand because he did not receive the section 82A(4) notice issued by the Commissioner (fact 5 refers). We ruled against this argument on the basis of the decision of Cons J in Cheng v CIR (1979) 1 HKTC 1087, which is binding upon us. Following the approach adopted in that case, we explained to the Taxpayer that, as he had lodged a valid appeal to the Board of Review, he could now introduce before us all the mitigating matters which he would have brought to the attention of the Commissioner. This related to whether, in terms of section 82B(2)(c), the additional tax was excessive having regard to the circumstances.

The proceedings before the Board

The Taxpayer gave sworn evidence before the Board. Little in the way of new evidence was introduced by the Taxpayer. The Taxpayer simply stated that he made a mistake in completing his return for the assessment 1993/94 by relying upon the figure used in his employer's return for the year of assessment 1992/93, that he was careless, and that he had no intention to evade tax. In this respect, Mrs Yip did not seek to cross-examine the Taxpayer.

Contentions of the Commissioner

Mrs Yip presented a written submission. She emphasised that it was the Taxpayer's responsibility to ensure that the information contained in his tax return was true and correct (see D15/89, IRBRD, vol 4, 252). She accepted that the Taxpayer had genuinely neglected to report his correct income. However, Mrs Yip noted that the maximum amount of tax that could be levied under section 82A was 300% and that, overall, a penalty of only 25% was low, being only 5.53% of the income omitted. She also noted that, based upon the Taxpayer's return for the year of assessment 1992/93, which the Taxpayer admitted signing, his total income amounted to $175,575 and not $104,475 which the Taxpayer copied to his return for the year of assessment 1993/94 (facts 1 and 7 refer). According to the earlier return, the difference of $71,100 was paid to the Taxpayer by 'School B'.

Mrs Yip concluded by submitting that, in all the circumstances, the amount of additional or penalty tax imposed for the Taxpayer's omission of income from his return for the year of assessment 1993/94 was not excessive.

Reasons for our decision

The key facts before us are not in dispute. The Taxpayer, who apparently had an otherwise good taxation compliance record, was careless on a single occasion by wrongly copying his salary from his then employer's return for the year of assessment 1992/93 onto his individual tax return for the year of assessment 1993/94. Mrs Yip noted that the amount copied by the Taxpayer was, in any event, different from the total income declared by the Taxpayer in his return for the year of assessment 1992/93. That is true, but the reasons for that discrepancy were not put to the Taxpayer in cross-examination. More importantly, Mrs Yip expressly accepted that this is a case where the Taxpayer had genuinely neglected to report his correct income. It was on this basis that we reached our decision.

Our starting point is that we agree with Mrs Yip that carelessness is not a reasonable excuse for filing an incorrect return. But there are gradations of lack of care and the Taxpayer's explanations did not indicate that this was an egregious case. Previous Boards of Review have held that in cases such as the one before us a reasonable level of penalty is 10% (compare D4/94, IRBRD, vol 9, 75 and D52/95, IRBRD, vol 11, 7).

In this case, however, and in line with recent practice commenced in 1995, the Commissioner has issued an additional or penalty tax assessment of 25% where a taxpayer has negligently omitted income from his tax return. Appeals against this practice have been partially allowed on at least two occasions (see D8/96 and D41/96). Although these decisions are unreported at the time of writing this decision, they are relevant to the present case because they show that differently constituted Boards of Review could not support an increase in the so-called 'normal tariff' of penalty tax for *all* cases involving omission of salary income by individuals regardless of the degree of negligence or lack of care on the part of the taxpayer.

The Commissioner is, of course, aware of these precedents. Although it is unusual for a Board of Review to refer to unreported decisions (although they will soon be reported), we have done so in order to illustrate an apparent early trend emerging from the present type of appeal. Specifically, the flavour of these decisions can be seen from D8/96 where the Board stated:

> *In the present case for reasons which we do not know the Commissioner has decided that the facts are more serious than the simple failure to perform an obligation under the IRO and that they are of such seriousness and magnitude as to merit increasing the penalty from the norm of 10% to an amount of approximately 25%. On the facts before us we can see no justification for such a decision. As we have said above this is a simple case. The Taxpayer made a genuine mistake and it seems to us that the norm of 10% is appropriate.*

Unlike the Board in D8/96 we know, but in broad outline only, why the Commissioner raised the additional assessment of 25%. But like the Board in D8/96 and D41/96 we do not think that a normal tariff of 25% is appropriate in *all* cases of neglect or carelessness where a taxpayer omits income from his or her tax return. Clearly, there are cases where such a level of penalty is appropriate (see D25/96 where the taxpayer 'displayed a cavalier disregard' to his tax compliance obligations); but we are loathe to agree that a 25% penalty is appropriate in all cases where negligence or lack of care in omitting income is in issue.

Before reaching our decision we cautioned ourselves that, without very good reason, we should not second guess the Commissioner simply because our inclination would be to conclude that the penalty tax assessed is more than we would have imposed. But, in the result, we have concluded on the basis of the facts before us that this is not an egregious case. We also consider that, to the extent possible, consistency in penalty tax appeals before the Boards of Review is desirable. Having then examined previous Board of Review decisions, including the more recent cases referred to above, we have concluded that the penalty tax raised in this case is excessive in the circumstances. We note, in passing, that in the only case cited on behalf of the Commissioner, D15/89, a 10% penalty tax was levied.

On the basis of the facts we have found and for the reasons given above, the penalty tax is hereby reduced to $2,200 which is approximately 10% of the tax which would have been undercharged if the Taxpayer's tax return had been accepted as correct.

It is left to us to thank Mrs Yip who at all times acted with exemplary fairness in rendering all possible assistance to the unrepresented Taxpayer throughout this appeal.