Case No. D126/95

Penalty tax – omission from tax return of one of two sources of salary – omission claimed to be simple mistake due to change of job – whether penalty tax of 25% excessive in the circumstances – Inland Revenue Ordinance sections 82A and 82B.

Panel: Andrew Halkyard (chairman), Albert Ho Chun Yan and Edwin Wong.

Date of hearing: 28 February 1996.
Date of decision: 28 March 1996.

In her 1993/94 tax return the taxpayer omitted an amount of salary income. She claimed that she changed jobs during the year and simply made a mistake by only recording income from one of her two jobs in her tax return. 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:

On the basis of unchallenged oral evidence, it appeared that the taxpayer had a good compliance record and that she had been careless on a single occasion by neglecting to include in her tax return one of her two sources of income. Although carelessness is not a reasonable excuse, it equally did not justify a penalty tax of 25%. In line with previous Board decisions, the penalty tax was reduced to 10% (D54/93, IRBRD, vol 8, 391 and D4/94, IRBRD, vol 9, 75 considered).

Per curiam 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. However, on the facts of the present case, and bearing in mind that consistency in tax appeals is desirable, the penalty was excessive in the circumstances.

Appeal allowed.

Cases referred to:

D54/93, IRBRD, vol 8, 391
D4/94, IRBRD, vol 9, 75

Tung Wai Wah for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

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

The agreed facts are as follows:

1. In her tax return-individuals for the year of assessment 1993/94, the Taxpayer declared the following particulars of income:

Salary/Wages	$114,707
Name of employer	Employer A
Capacity in which employed	Secretary
Period of employment	April to September 1993

2. Employer's returns submitted to the Inland Revenue Department revealed that the Taxpayer had the following sources of income for the year of assessment 1993/94:

Name of Employer	**Period of Employment**	**Amount**
Employer A	1-4-93 to 30-9-93	$114,707
Employer B	1-10-93 to 31-3-94	158,874
		273,581

3. On 16 March 1995 the assessor raised a salaries tax assessment on the Taxpayer for the year of assessment 1993/94 showing total assessable income of $273,581.

4. The Taxpayer did not object to this assessment.

5. Correspondence was then exchanged between the Commissioner and the Taxpayer. After considering the Taxpayer's representations, the Commissioner issued an assessment under section 82A for additional (penalty) tax on the Taxpayer for the year of assessment 1993/94 in an amount of $9,100. This amount represents 24.96% of the tax which would have been under charged had the Taxpayer's tax return been accepted as correct.

6. The Taxpayer appealed to this Board against the assessment described at fact 5. In her notice of appeal she stated:

> 'It was extremely unfair to impose the fine on me. The omission was not made deliberately. It was the first time in 10 years that I changed jobs formally, and owing to my negligence, I mistook that I had to report tax in two separate tax returns. … If I had meant to falsify the income, I would not have reported every single cent of the incomes I received from two different companies for the years 1991-93 and paid the tax in full.
>
> … Ever since 1987, the first year I was subject to salaries tax, I had never incorrectly filed or withheld any information.'

The proceedings before the Board

During the course of the hearing the Taxpayer accepted that she had no reasonable excuse for filing an incorrect return. She did, however, claim that the amount of penalty tax raised on her was excessive.

The Taxpayer then gave sworn evidence. She simply stated that:

1. She had no intent to evade tax.

2. Her past compliance record was good – she always paid her tax on time.

3. When she changed jobs in 1993, she made a mistake by not including both amounts in her tax return. Although she received a copy of two separate employer's returns for the year of assessment 1993/94 (fact 2 refers), she had simply got used to recording one amount in her tax return. Her mistake in not recording both amounts may have been due to carelessness.

The Commissioner's representative ('the representative') did not cross-examine the Taxpayer on this evidence.

In light of her evidence (point 3) set out above, the Board asked the Taxpayer to explain the statement in her notice of appeal (fact 6 refers) that in prior years of assessment she returned income from *two* different companies and paid the tax in full. She replied that previously she had received income from two associated companies: one paid her salary, the other paid her commission. She then sought to draw an analogy between her appeal and her circumstances in that earlier period. She stated that if she had intended to evade tax she could also have done so in this earlier period by omitting to declare a source of income – and she did not. The Taxpayer then explained that although she received two employer's returns for this earlier period, which showed that she earned both salary and commission, for the sake of convenience she also received a consolidated statement from her employer

showing the total amount of income from both companies. She indicated that she then filed her tax return for this earlier period on the basis of the figure disclosed in that consolidated statement.

The representative did not cross-examine the Taxpayer in relation to this additional evidence.

The contentions for the Commissioner

The representative argued that the duty to complete a true and correct return falls solely on the taxpayer. The fact that a taxpayer had submitted true and correct returns in the past does not form a reasonable excuse for not doing so in subsequent returns.

As to the quantum of penalty in the amount of $9,100, the representative stressed that this was only 5.73% of the income omitted and 24.96% of the amount of tax which would have been under charged had the Taxpayer's tax return been accepted as correct. To bolster this argument, the representative stated that the Commissioner had already been lenient in this case given that in the preceding year of assessment, 1992/93, the Taxpayer had also submitted an incorrect return by omitting another (albeit smaller) amount of income from Employer B.

Analysis

Upon reading the appeal papers, it initially appeared to us that the level of penalty tax in this case, which amounted to nearly 25%, was high given that this appeal apparently involved carelessness by a taxpayer who otherwise had a good tax compliance record. That is not to say that carelessness is a reasonable excuse for filing incorrect returns – clearly it is not. But there are gradations of lack of care and the Taxpayer's explanations did not indicate that this was an egregious case.

Our initial impression was confirmed upon hearing the Taxpayer's *unchallenged* sworn testimony. That testimony was totally consistent with the statements contained in the Taxpayer's notice of appeal.

Subsequently, upon hearing the representative's arguments, it seemed implicit (if not explicit) that the level of penalty tax imposed in this case was, in part, based on the background that the Taxpayer had filed an incorrect return in the preceding year of assessment. In this regard, the representative submitted documents to us which were said to be the Taxpayer's tax return and an employer's return from Employer B in respect of the Taxpayer for the year of assessment 1992/93. The tax return did not include the amount referred to in this employer's return.

The fact remains, however, that none of these documents were put to the Taxpayer. The documents were only produced to the Board once the Taxpayer had concluded her evidence. The Taxpayer was not cross-examined by the representative on any matter, let alone asked to explain the discrepancies, if any, between these documents

and the Taxpayer's sworn evidence. In these circumstances, we are unable to draw the adverse inferences from the documents which the representative urged upon us. To do so would simply not be fair to the Taxpayer.

In the result, the facts before us are that the Taxpayer has been careless on a single occasion by neglecting to include in her tax return one of her two sources of income. As stated above, her explanation for this carelessness is not a reasonable excuse; however, in light of the explanation she has offered, it equally does not justify a penalty tax of 25%. Previous decisions of Boards of Review have held that in cases such as the one before us, a reasonable level of penalty tax is 10% (compare D54/93, IRBRD, vol 8, 391 and D4/94, IRBRD, vol 9, 75).

Before reaching our decision we have 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. However, on the facts before us, and bearing in mind that, to the extent possible, consistency in penalty tax appeals is desirable, we conclude that the penalty tax raised in this case is excessive in the circumstances.

Accordingly, the penalty tax is hereby reduced to $3,600, which in round figures represents 10% of the tax which would have been avoided had the Taxpayer's tax return been accepted as correct.