

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D166/01

Penalty tax – understating income – whether penalty excessive.

Panel: Patrick Fung Pak Tung SC (chairman), Henry Lau King Chiu and Leung Hing Fung.

Date of hearing: 15 January 2002.

Date of decision: 13 March 2002.

The taxpayer was a car salesman. He failed to report the receipt of commission from finance companies for introducing purchasers of motor cars for hire-purchase transactions.

As a result, additional tax of 74.9% and 58.19% of the undercharged tax was assessed against him for the years of assessment 1993/94 and 1997/98 respectively.

The taxpayer appealed against the assessment as being excessive.

Held:

1. The Board found the taxpayer had no reasonable excuse for not reporting to the Inland Revenue Department (‘IRD’) the receipt of the commission in question.
2. The penalty in this case was actually below the standard practice, that is, 100% of the tax underpaid.

Appeal dismissed.

Cases referred to:

D179/98, IRBRD, vol 14, 78

D71/91, IRBRD, vol 7, 1

D52/93, IRBRD, vol 8, 372

Mei Yin for the Commissioner of Inland Revenue.

Taxpayer in person.

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Decision:

1. This is an appeal by the Appellant (' the Taxpayer') against an assessment for additional tax under section 82A of the Inland Revenue Ordinance (' IRO') by the Respondent (' the Commissioner').

2. The additional tax assessed and demanded are contained in two notices of assessment and demand both dated 15 October 2001 and are in relation to the following years of assessment:

		\$
(a)	1993/94	16,700
(b)	1997/98	<u>3,100</u>
		<u>19,800</u>

The facts

3. The Taxpayer had been in the motor car sale business since at least 1988. He had a chequered history of employment with various car dealers. At all times material to this appeal, the Taxpayer was a car salesman employed by Company A during the year of assessment 1993/94 and a car salesman employed by Company B during the year of assessment 1997/98. The Taxpayer probably acted also as a sales representative of various insurance companies.

4. The Taxpayer submitted tax returns - individuals for the years of assessment 1993/94 to 1998/99 as follows:

Year of assessment	Source of income	Total reported income	Deduction for expenses claimed	Date
		\$	\$	
1993/94	Company A	218,432	30,000	20-5-1994
1994/95	Company A	158,548	16,000	20-5-1995
	Company C	5,204		
1995/96	Company A	75,870	17,262	14-2-2001
	Company C	13,538		
	Company D	75,628		
	Company E	3,640		
	Other car dealers	3,946		

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1996/97	Company A	21,223	10,361	14-2-2001
	Company C	2,158		
	Company B	40,922		
	Company F	40,842		
	Company G	11,442		
	Other car dealers	531		
1997/98	Company B	247,608	0	29-11-1998
1998/99	Company B	191,159	26,891	26-5-1999
	Company F	101,030		

5. Assessments and demands for tax were issued by the IRD in accordance with the tax returns submitted by the Taxpayer.

6. Subsequently, as a result of investigation by the IRD, it was discovered that the Taxpayer had under-declared income as follows:

Source	1993/94	1994/95	1995/96	1996/97	1997/98
	\$	\$	\$	\$	\$
Company A	-	-	75,870	21,223	-
Company D	96,206	9,932	75,628	-	-
Company C	1,869	-	13,538	2,158	-
Company B	-	-	-	40,922	-
Company F	-	-	-	40,842	118,486
Company E	-	-	3,640	-	-
Company G	-	-	-	11,442	-
Other car dealers	<u>15,351</u>	<u>1,296</u>	<u>3,946</u>	<u>531</u>	<u>3,300</u>
Total	<u><u>113,426</u></u>	<u><u>11,228</u></u>	<u><u>172,622</u></u>	<u><u>117,118</u></u>	<u><u>121,786</u></u>

7. It transpired that, at least for the years of assessment 1993/94 to 1997/98, the Taxpayer was in receipt of commission from various finance companies for introducing purchasers of motor cars for hire-purchase transactions which had not been declared or fully declared by the Taxpayer.

8. The Taxpayer attended various interviews with the IRD and admitted that he had failed to report fully the income received by him for the relevant years of assessment.

9. The interviews culminated in the Taxpayer signing an agreement dated 14 February 2001 (' the Agreement ') wherein he stated as follows:

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‘ 1. I hereby propose that my net assessable income be computed as follows:-

<u>Year of Assessment</u>	<u>Net Assessable Income</u>	<u>Net Assessable Income already Reported/Assessed</u>	<u>Additional Net Assessable Income</u>
	\$	\$	\$
1993/94	301,072	205,249	95,823
1994/95	165,312	158,282	7,030
1995/96	155,360	-	155,360
1996/97	106,757	-	106,757
1997/98	334,850	247,608	87,242
1998/99	265,298	265,298	-

2. I also agree to accept the following revised net assessable/additional net assessable income in settlement of the objections against the previous assessments:-

<u>Year of Assessment</u>	<u>Revised Net Assessable Income</u>	<u>Revised Additional Net Assessable Income</u>
	\$	\$
1993/94	-	95,823

3. I also understand that acceptance of the above-mentioned assessable income does not conclude the whole matter and that the case will be put up to the Commissioner or Deputy Commissioner for consideration of penal actions under Part XIV of the Inland Revenue Ordinance, which include prosecution, compounding or imposition of Additional Tax. If Additional Tax is imposed, the maximum amount could be treble the amount of the tax undercharged.’

The Agreement is backed up by an income schedule also dated 14 February 2001 and signed by the Taxpayer which shows the receipt of commission from various finance companies which had not previously been reported by the Taxpayer.

10. Thus, after investigation by the IRD, it was discovered that for the years of assessment 1993/94 to 1998/99, the Taxpayer had under-declared income and underpaid tax as follows:

Year of assessment	Assessable income after investigation	Assessable income before investigation	Under-declared assessable income	Underpaid tax
	\$	\$	\$	\$
1993/94	331,858	218,432	113,426	22,296

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1994/95	174,980	163,752	11,228	-
1995/96	172,622	-	172,622	-
1996/97	117,118	-	117,118	-
1997/98	369,394	247,608	121,786	5,327
1998/99	<u>292,189</u>	<u>292,189</u>	<u>-</u>	<u>-</u>
	<u>1,458,161</u>	<u>921,981</u>	<u>536,180</u>	<u>27,623</u>

The under-declared assessable income amounts to 36.77% of the assessable income after investigation.

11. Accordingly, on 28 February 2001, the IRD issued notices of revised assessment and demand for salaries tax against the Taxpayer.

Year of assessment	Tax demanded
	\$
1993/94	22,296
1997/98	5,327

12. On 16 August 2001, the Commissioner issued a notice under section 82A(4) of the IRO informing the Taxpayer of his intention to assess and demand against him additional tax under section 82A of the IRO for having made incorrect tax returns.

13. By a letter dated 18 August 2001, the Taxpayer objected to such notice.

14. On 15 October 2001, the Commissioner issued the two notices referred to in paragraph 2 above.

15. The percentage analysis of the additional tax assessed is set out below:

Year of assessment	Undercharged tax	Additional tax assessed under section 82A	Percentage of additional tax assessed over undercharged tax
	\$	\$	%
1993/94	22,296	16,700	74.90
1997/98	<u>5,327</u>	<u>3,100</u>	58.19
	<u>27,623</u>	<u>19,800</u>	71.68

The law

16. Section 82A(1) of the IRO provides as follows:

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'82A. Additional tax in certain cases

- (1) *Any person who without reasonable excuse –*
- (a) *makes an incorrect return by omitting or understating anything in respect of which he is required by this Ordinance to make a return, either on his behalf or on behalf of another person or a partnership; or*
 - (b) *makes an incorrect statement in connection with a claim for any deduction or allowance under this Ordinance; or*
 - (c) *gives any incorrect information in relation to any matter or thing affecting his own liability to tax or the liability of any other person or of a partnership; or*
 - (d) *fails to comply with the requirements of a notice given to him under section 51(1) or (2A); or*
 - (e) *fails to comply with section 51(2),*

shall, if no prosecution under section 80(2) or 82(1) has been instituted in respect of the same facts, be liable to be assessed under this section to additional tax of an amount not exceeding treble the amount of tax which –

- (i) *has been undercharged in consequence of such incorrect return, statement or information, or would have been so undercharged if the return, statement or information had been accepted as correct; or*
- (ii) *has been undercharged in consequence of the failure to comply with a notice under section 51(1) or (2A) or a failure to comply with section 51(2), or which would have been undercharged if such failure had not been detected.'*

17. Section 68(4) of the IRO provides that on an appeal: '*The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant*' .

The case of the Taxpayer

18. Basically, the case put forward by the Taxpayer is that, when he filed the tax return for the year of assessment 1993/94, he had been given to understand by Company A that there was no

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need to report the commission in question because it was the practice of the trade, and that he was in grave financial difficulty. He further stressed that he had no intention to cheat the IRD.

Conclusion

19. We are of the view that the Taxpayer has not proved that he had any ‘reasonable excuse’ within the meaning of section 82A(1) of the IRO for not reporting to the IRD the receipt of the commission in question.

20. The advice or information allegedly given to the Taxpayer by Company A was obviously wrong. There are well-established authorities to the effect that a taxpayer cannot seek to excuse himself from complying with his duty to make correct returns by claiming that he was ignorant of the law or that he had been misled by someone. See, for example, the decision of the Board of Review in D179/98, IRBRD, vol 14, 78. Nor can the practice of a particular trade be a valid reason, otherwise the people in the trade would be creating their own law.

21. In fact, the notes accompanying all tax return forms each year make it clear that a taxpayer has to report all commission received in the course of his work or employment for tax purposes. Furthermore, the Taxpayer admitted in evidence that he was actually told by Company F in 1996 that he would have to report to the IRD all commission received.

22. The financial difficulty on the part of the Taxpayer is also not a valid reason for not paying the penalty. In D71/91, IRBRD, vol 7, 1 at page 7, it was said by the Board of Review:

‘...the ability of a taxpayer to pay an assessment is not a matter for the Board...’

23. There is in fact very little room for the Board to manoeuvre after the Taxpayer had made the admission that he had under-declared his assessable income or profit and signed the Agreement.

24. It is clear from the authorities, for example, Board of Review decision D52/93, IRBRD, vol 8, 372, that the standard practice is to use as a starting point penalty equivalent to 100% of the tax underpaid in cases of this nature. Here, the Taxpayer has been given only an average penalty of about 71% which is some way below the standard of 100%.

25. In all the circumstances, we have no basis or justification for saying that the Commissioner has been wrong in imposing such a penalty and, accordingly, we must dismiss the appeal.