Case No. D18/97

Penalty tax – omission from tax return of part of salary – omission as a result of carelessness – whether penalty tax of 24.8% excessive – Inland Revenue Ordinance section 82A.

Panel: Ronny Wong Fook Hum SC (chairman), Raymond J Faulkner and James Kwan Yuk Choi.

Date of hearing: 12 April 1997.
Date of decision: 12 May 1997.

In his 1994/95 tax return, the taxpayer omitted part of his salary. Upon challenge by the Commissioner, the taxpayer explained that the omission was caused by his carelessness. Penalty was raised on the taxpayer, which amounted to 24.8% of the tax which would have undercharged if the omission had not been detected.

Held:

(1) The alleged breach in the year of assessment 1992/93, being previous alleged non-compliance should not be a potential aggravating factor for subsequent non-compliance. The taxpayer might have valid explanation for such alleged breach.

(2) Although carelessness is not a reasonable excuse, a 24.8% penalty tax is not appropriate bearing in mind the magnitude of the tax understated. On the fact of present case, and bearing in mind that consistency in tax appeals is desirable, the penalty tax was reduced to 15%.

Appeal allowed.

Cases referred to:

D48/93, IRBRD, vol 8, 366
D4/94, IRBRD, vol 9, 75
D21/94, IRBRD, vol 9, 182

Go Min Min for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

The facts

1. This is an appeal against the additional tax imposed on the Taxpayer by the Commissioner under section 82A of the Inland Revenue Ordinance ['the IRO'] for the year of assessment 1994/95.

2. By his return dated 6 July 1995, the Taxpayer declared $105,699 as his earnings for the period between 9 March 1994 to 15 August 1994 working as assistant to the general manager in Company X. He omitted to state in this return his earnings as assistant manager in Company Y for the period between 22 September 1994 and 31 March 1995 amounting to $120,291. The amount so omitted amounted to 53.2% of his total income of $225,990. The amount of tax which would have been undercharged if the return had been accepted as correct is $21,366.

3. In response to the Revenue's notice under section 82A of the IRO, the Taxpayer explained that the omission arose as a result of his carelessness. He urged the Commissioner to take into account that 'it is my first time to make this mistake'.

4. By notice dated 10 May 1996, the Commissioner imposed additional tax in the sum of $5,300 which amounted to 24.8% of the amount of tax which would have been undercharged had the tax return been accepted as correct.

5. In his notice of appeal dated 26 August 1996, the Taxpayer further explained that he overlooked the employer's return of Company Y.

At the hearing before us

6. The Taxpayer candidly admitted his error. His principal dispute relates to quantum.

7. The Board drew the parties' attention to the decisions of this Board in D48/93, D4/94 and D21/94. The Board in D48/93 clearly pointed out that 'our system of taxation is simple and relies upon taxpayers in Hong Kong filing true and correct tax returns. It behoves all of us to take care when completing our tax returns, and if we are careless then we must expect to be penalised. 'Those cases indicate that in relation to negligent non-compliance with the provisions of the Inland Revenue Ordinance and without more, a penalty of 10% of the tax involved is not excessive.

8. The Revenue sought to justify the sum of $5,300 on 2 grounds:

   a. the Taxpayer had erroneously declared his income for the year of assessment 1992/93 and

b. LS No 2 to Gazette No 29/1995 dated 19 July 1995 had revised the penalty under section 80 of the IRO by repealing the sum of $5,000 and substituting therefor a penalty 'at level 3'. Representatives appearing on behalf of the Revenue failed to identify before us what that level entails. We are also puzzled by the reference to section 80 of the IRO.

Our decision

9. We are of the view that the alleged breach in the year of assessment 1992/93 should not have been taken into account in arriving at the amount of penalty. The Revenue took no action at all in relation to that alleged breach. This Board has repeatedly pointed out that previous alleged non-compliance should be dealt with in the relevant year of assessment and should not be left pending as a potential aggravating factor for subsequent non-compliance. The Taxpayer might well have good and valid explanation for such alleged breach.

10. Bearing in mind the inability of the Revenue's representative to identify before us what 'level 3' entails, we entertain serious doubts whether the amendments in LS No 2 to Gazette No 29/1995 were matters that the Commissioner actually took into account in arriving at the figure for additional tax. Those amendments made no alteration to the maximum penalty that could be imposed under section 82A. The Taxpayer in default remains liable to additional tax of an amount not exceeding treble the amount of tax which has been undercharged in consequence of the failure or which would have been undercharged if such failure had not been detected.

11. Whilst conscious of our duty not to second guess the Commissioner, we are of the view that the amount of additional tax imposed is excessive in this case. Bearing in mind the magnitude of the sum understated, we are of the view that a penalty of $3,205 being 15% of the tax which would have been undercharged if such failure had not been detected should be substituted therefor.

12. We allow the appeal and direct that the amount of additional tax be $3,205.