

**Case No. D37/07**

**Penalty tax** – understating income in tax return – whether additional tax is excessive – sections 12(1)(a), 64(3), 68, 70, 80(2), 82(1), 82A and 82B of the Inland Revenue Ordinance ('IRO').

**Costs** – frivolous and vexatious and an abuse of the process – section 68(9) of the IRO.

Panel: Kenneth Kwok Hing Wai SC (chairman), Lawrence Lai Wai Chung and Peter Malanczuk.

Date of hearing: 30 November 2007.

Date of decision: 31 December 2007.

The appellant objected against additional salaries tax assessment on the grounds that contribution to recognised retirement scheme and medical deduction should be deductible. The assessor explained to the appellant that medical deduction was not deductible under section 12(1)(a) of the IRO. The appellant agreed to the assessor's proposed revised assessment. Based on the agreement reached with the appellant, the assessor issued a revised notice of salaries tax assessment under section 64(3) of the IRO. The appellant was penalised for understating his income in his tax return. The assessment is about 7% of the tax which would have been undercharged had the tax return filed by the appellant been accepted as correct.

**Held:**

1. The appellant's objection to the additional salaries tax assessment was compromised and the additional salaries tax assessment objected to was revised by the assessor. Thus the amount of the assessable income has been agreed to under section 64(3) and by virtue of section 70, the revised salaries tax assessment as agreed to shall be final and conclusive for all purposes of the IRO as regards the amount of such assessable income. The appellant understated his income by nearly 70%. The appellant has no reasonable excuse for understating his income and is liable to be assessed to additional tax.
2. The Board does not think that the assessment is excessive. The Deputy Commissioner erred, if at all, in being too lenient.
3. The Board is of the opinion that this appeal is frivolous and vexatious and an abuse of the process. Pursuant to section 68(9) of the IRO, the Board order the appellant to pay the sum of \$2,500 as costs of the Board.

**Appeal dismissed and costs order in the sum of \$2,500 imposed.**

Case referred to:

D16/07, IRBRD, vol 22, 454

Taxpayer in person.

Leung Shuk Fun and Go Shun Yuk for the Commissioner of Inland Revenue.

**Decision:**

1. This is an appeal against the following assessment ('the Assessment') dated 8 August 2007 by the Deputy Commissioner of Inland Revenue, assessing the appellant to additional tax under section 82A of the Inland Revenue Ordinance, Chapter 112, ('the Ordinance') in the following sum:

<b>Year of assessment</b>	<b>Additional tax</b>	<b>Charge no</b>
2005/06	\$10,000	9-1975238-06-4

2. The appellant was penalised for understating his income in his tax return.

***The salient facts***

3. The parties agreed the facts in the Agreed Statement of Facts and we find them as facts.

4. The salient facts are as follows.

5. From June 1999 to May 2002, the appellant was employed in a senior capacity by various companies in the same group of companies. Through a leading firm of certified public accountants, he filed Tax Returns – Individuals for the 1999/2000, 2000/01, 2001/02 and 2002/03 years of assessment reporting employment and income as follows:

<b>Year of assessment</b>	<b>Capacity employed</b>	<b>Period</b>	<b>Total Income (\$)</b>
1999/2000	Director – Customer	'1/6/1999 –	779,335

(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

	Technical Support	31/3/2000'	
2000/01	Director – Customer Technical Support	'1/4/2000 – 31/3/2001'	1,112,333
2001/02	Director	'1/4/2001 – 31/3/2002'	1,246,139
2002/03	Director	'1/4/2002 – 31/5/2002'	180,026

6. From June 2002 to September 2004, the appellant was relocated outside Hong Kong by his employers. With effect from 1 October 2004, the appellant was relocated back to Hong Kong.

7. The appellant reported the following in the returns filed by him for the years of assessment 2004/05 and 2005/06:

<b>Year of assessment</b>	<b>Capacity employed</b>	<b>Period</b>	<b>Total Income (\$)</b>	<b>Date of return</b>
2004/05	Director	'1.10.2004 – 31.3.2005'	'703,393'	'30/5/2005'
2005/06	Director	'1.1.2006 – 31.3.2006'	'310,073.25'	'8/5/2006'

8. A booklet 'Guide to Tax Return – Individuals' ('the Guide Book') was sent by the Revenue with the 2005/06 return to the appellant. The term 'year' was defined on page 1 of the Guidebook as follows:

'The term "year" refers to the year of assessment printed on the front page of the return. A year of assessment runs from 1 April to 31 March, e.g. Year of Assessment 2005/06 runs from 1 April 2005 to 31 March 2006.'

9. The appellant's employer filed returns reporting the following in respect of the appellant:

<b>Year of assessment</b>	<b>Period</b>	<b>Total Income</b>	<b>Date of return</b>
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(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

		(\$)	
2004/05	'20041001 –20050331'	'703,393'	'03/05/2005'
2005/06	'20050401 – 20060331'	'1,006,204'	'28/04/2006'
2005/06 Revised	'01042005 – 31032006'	'1,033,131'	'03/05/2006'

10. Based on the employer's initial return, the assessor raised on 4 July 2006 the following 2005/06 salaries tax assessment on the appellant:

Income		\$1,006,204
<u>Less:</u> Mandatory contribution to Recognised Retirement Scheme	3,000	
Home Loan Interest	5,900	
Basic Allowance	100,000	
Dependent Parent Allowance	30,000	
Additional Dependent Parent Allowance	<u>30,000</u>	<u>268,900</u>
Net chargeable income		<u>837,304</u>
Tax payable thereon		<u>156,660</u>

The appellant did not object to this assessment.

11. Based on the employer's revised return, the assessor raised on 5 October 2006 the following 2005/06 additional salaries tax assessment on the appellant:

Income		\$1,033,131
<u>Less:</u> Mandatory contribution to Recognised Retirement Scheme	3,000	
Home Loan Interest	5,900	
Basic Allowance	100,000	
Dependent Parent Allowance	30,000	
Additional Dependent Parent Allowance	<u>30,000</u>	<u>168,900</u>
Net chargeable income		<u>864,231</u>
Tax thereon		162,046
<u>Less:</u> tax already charged		<u>156,660</u>
Tax payable thereon		<u>\$5,386</u>

(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

12. By letter dated 16 October 2006, the appellant objected against the 2005/06 additional salaries tax assessment on the grounds that contribution to recognised retirement scheme and medical deduction in the respective amount of \$41,556 and \$831 should be tax deductible.

13. By letter dated 29 December 2006, the assessor explained to the appellant that medical deduction of \$831 was not deductible under section 12(1)(a) of the Ordinance and proposed to revise the 2005/06 additional salaries tax assessment as follows:

Income		\$1,033,131
<u>Less:</u> Mandatory contribution to Recognised		
Retirement Scheme	12,000	
Home Loan Interest	5,900	
Basic Allowance	100,000	
Dependent Parent Allowance	30,000	
Additional Dependent Parent Allowance	<u>30,000</u>	<u>177,900</u>
Net chargeable income		<u>855,231</u>
Tax thereon		<u>160,246</u>

The appellant agreed to the assessor's proposed revised assessment.

14. Based on the agreement reached with the appellant, the assessor issued a revised notice of 2005/06 salaries tax assessment on 27 June 2007 under section 64(3) of the Ordinance with a tax refund of \$1,800.

15. On 29 June 2007, notice was given to the appellant under section 82A(4) of the Ordinance. In response to the appellant's request on 6 July 2007, the assessor supplied the appellant with a copy of the section 82A(4) notice and a copy of the employer's revised return. By letter dated 13 July 2007, the appellant made representations, having telephoned the assessor on the same date and been advised to put his explanation in writing.

16. By another letter dated 13 July 2007, the appellant wrote to the assessor in respect of his 2006/07 Tax Return. Since we are only concerned with the Assessment which related to the 2005/06 year of assessment, we say no more about the return in respect of the 2006/07 year of assessment.

17. The Assessment is about 7% of the tax which would have been undercharged had the 2005/06 tax return filed by the appellant been accepted as correct.

18. No prosecution under section 80(2) or section 82(1) of the Ordinance has been instituted in respect the same facts.

***Grounds of appeal***

(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

19. By letter dated 17 August 2007, the appellant gave notice of appeal in these terms (written exactly as it stands in the original):

‘I have received (Attachment A) the Notice of Assessment and Demand for additional tax by way of penalty under section 82A of the Inland Revenue Ordinance in the sum of \$10,000 on Aug 8, 2007 and I would like to appeal for this penalty.

On July 6, 2007, I received the Salaries Tax Notice of file [XXX-XXXXXXXXXX] (see attachment B) I called [Mr A] (Unit-2 Assessor) to discuss and clarify the issue. After the phone conversation, he suggested me to write a letter (see attachment C) to him to explain why there was an inconsistency of the 2005-2006 salary income, and he will take action accordingly.

As I explained in that letter (attachment C) that the difference of the \$723,058 income vs I put in my tax assessment of year 2005-2006 (attachment D) of the \$310,073.25 was because

- 1) I thought the assessment is from Jan 1, 2006 – March 31, 2006 and you can see from attachment D that I put down the period of 1-1-2006 – 3-31-2006, so I only reported the three months income. I found out this mistake while [Mr A] (Assessor) pointed out to me during the phone conversation.
- 2) This is my first time to file my Hong Kong income tax since I transferred from my US company to the Hong Kong company end of 2004 (See attachment E) I thought the tax year is the beginning of Jan till end of Dec of the year. And the tax 2005-2006 assessment form is the quarter report for the first three months of 2006.

As you can see from Salaries Tax [XXX-XXXXXXXXXX] (attachment F) I had paid the 2005-2006 tax of \$160,246 and received a refund of \$1,800 overpaid tax. I have paid all the 2005-2006 income tax together with the 2006-2007 provisional tax on Jan, 2007. This proves that I honestly and on-time paid my income tax to the Inland Revenue Department and I have no intention to hide my income.

If I did not pay my income tax for 2005-2006, I will accept the penalty for not paying the Inland Revenue Department. Since I have already fully paid amount my 2005-2006 tax of \$160,246 on time and ahead of deadline, and I did not own the government any income tax, the penalty of \$10,000 will not be fair in my case due to my misunderstand of the tax reporting.

(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

I hope the Board of Review will review my case and wave the penalty. If you have any further questions or request in-person for interview, feel free to contact me at [telephone number given by the appellant omitted here] anytime.'

***The appeal hearing***

20. The appellant gave evidence asserting that he thought he was filing a quarterly return for the calendar year 2006. He alleged that he had not received the original and revised returns filed by his employer by the time he completed his return. He gave no intelligible explanation why the title of the form was 'Year of Assessment 2005/06' or why the year '2005' appeared in the title of the form if it were a quarterly report for the calendar year 2006. The item for box 100 was for:

'Claim for Dependant Parent/Grandparent Allowance:

- (i) The dependent resided with me continuously during the year without paying full costs.

(Enter "1" for full year; or "2" for at least 6 months) ...'

He gave no intelligible explanation why he filled in '1' in box 100 if he thought he was filling in a report for the first quarter of the calendar year 2006.

21. The appellant cited no authority and did not deal with any of the previous Board decisions cited by the assessor.

***Relevant statutory provisions on additional tax***

22. Section 64(3) of the Ordinance provides that:

*'(3) In the event of the Commissioner agreeing with any person assessed, who has validly objected to an assessment made upon him, as to the amount at which such person is liable to be assessed, any necessary adjustment of the assessment shall be made.'*

23. Section 70, so far as relevant, provides that:

*'Where no valid objection or appeal has been lodged within the time limited by this Part against an assessment as regards the amount of the assessable income ... assessed thereby ... or where the amount of the assessable income ... has been agreed to under section 64(3) ... the assessment as made or agreed to ... as the case may be, shall be final and conclusive for all purposes of this Ordinance as regards the amount of such assessable income ...*

(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

*Provided that nothing in this Part shall prevent an assessor from making an assessment or additional assessment for any year of assessment which does not involve re-opening any matter which has been determined on objection or appeal for the year.'*

24. Section 82A(1) provides that:

*'(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) ...*

*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 ...'*

25. Section 82B(2) provides that:

*'(2) On an appeal against assessment to additional tax, it shall open to the appellant to argue that –*

*(a) he is not liable to additional tax;*

*(b) the amount of additional tax assessed on him exceeds the amount for which he is liable under section 82A;*

*(c) the amount of additional tax, although not in excess of that for which he is liable under section 82A, is excessive having regard to the circumstances.'*

26. Section 82B(3) provides that section 68 shall, so far as applicable, have effect with respect to appeals against additional tax as if such appeals were against assessments to tax other



(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

than additional tax. The Board's power under section 68(8)(a) includes the power to increase the assessment appealed against.

27. Section 68(4) provides that the onus of proving that the assessment appealed against is excessive or incorrect shall lie on the appellant.

28. Section 68(9) provides that:

*'Where under subsection (8), the Board does not reduce or annul such assessment, the Board may order the appellant to pay as costs of the Board a sum not exceeding the amount specified in Part I of Schedule 5, which shall be added to the tax charged and recovered therewith.'*

29. The amount specified in Part I of Schedule 5 is \$5,000.

***Incorrect return***

30. The appellant's objection to the 2005/06 additional salaries tax assessment referred to in paragraph 11 above was compromised and the additional salaries tax assessment objected to was revised by the assessor on 27 June 2007, see paragraphs 13 and 14 above.

31. Thus the amount of the assessable income has been agreed to under section 64(3) and by virtue of section 70, the revised salaries tax assessment as agreed to shall be final and conclusive for all purposes of this Ordinance as regards the amount of such assessable income.

32. The appellant submitted his return reporting \$310,073.25 as his salary income.

33. The correct amount of his income was \$1,033,131.

34. Thus, the appellant made incorrect return, understating his income.

***Whether liable for additional tax***

35. The appellant understated his income by \$723,057.75. In percentage terms, he understated his income by nearly 70%.

36. The appellant's assertion that this was his 'first time to file [his] Hong Kong income tax since ... end of 2004' is untrue and we reject it. He filed his return for the 2004/05 year of assessment reporting income for the period which he put down as '1.10.2004 – 31.3.2005' and dated it '30/5/2005', see paragraph 7 above.

37. Even on the basis of the appellant's assertion, he was reckless.

(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

38. As the Board has stated time and again, see paragraphs 125 – 128 in D16/07, IRBRD, vol 22, 454 (Kenneth Kwok Hing Wai, SC, Eva Chan Yee Wah and Paul Lam Ting Kwok) and the authorities there cited, carelessness or recklessness is not an excuse.

39. In our decision, the appellant has no reasonable excuse for understating his income and is liable to be assessed to additional tax.

***Maximum amount of additional tax***

40. The maximum amount is treble the amount of tax undercharged or which would have been undercharged had her return been accepted as correct. The amount undercharged or which would have been undercharged was \$142,812 and treble that is \$428,436.

41. The maximum amount of additional tax depends on the size of the tax undercharged or would have been undercharged if the return had been accepted as correct. If the tax undercharged or would have been undercharged if the return had been accepted as correct is large, the maximum amount is three times as large.

42. The Assessment in the sum of \$10,000 does not exceed the amount for which he is liable under section 82A.

***Whether excessive having regard to the circumstances***

43. For reasons given in paragraphs 125 – 128 in D16/07, including paragraph 128(c), (d), (f), (g) and (i) and having considered all the matters urged by the appellant, we do not think that the Assessment is excessive. The Deputy Commissioner erred, if at all, in being too lenient.

***Disposition***

44. We dismiss the appeal and confirm the Assessment.

***Cost order***

45. From time to time, taxpayers like the appellant who:

- (a) are in middle or senior management;
- (b) earn no less than high six digit annual income;

(2007-08) VOLUME 22 INLAND REVENUE BOARD OF REVIEW DECISIONS

- (c) have the knowledge and means of reporting the correct amounts of their aggregate employment income if they have intended or taken the trouble so to do;
- (d) through carelessness, or not caring whether the returns they filed be correct or not, filed incorrect returns, understating or omitting a substantial portion of their aggregate employment income;
- (e) show no or no genuine remorse;
- (f) take no steps to put their houses in order;
- (g) argue that it is unfair to penalise them; and
- (h) demand a waiver of penalty.

46. It is difficult to see how such taxpayers could hope to win the sympathy of the Board in cases of additional tax of 15% or below.

47. The matters put forward by the appellant in this appeal have been consistently rejected by the Board in published decisions, some of which were included in the assessor's bundle of authorities.

48. We are of the opinion that this appeal is frivolous and vexatious and an abuse of the process. Pursuant to section 68(9) of the Ordinance, we order the appellant to pay the sum of \$2,500 as costs of the Board, which \$2,500 shall be added to the tax charged and recovered therewith.