Case No. D40/03

Penalty tax – the appellant omitted to report 41.64% of her total income for six years of assessment from 1993/94 to 1998/99 – attempt to conceal earnings from the purview of the Revenue – submission of incorrect tax returns without reasonable excuse – imposition of additional assessments at the average rate of 73.85% of the tax undercharged – it is the basic obligation of every taxpayer to report all income to the Revenue – such basic obligation was personal to taxpayers – such obligation cannot be compromised by pretending that its non-fulfillment might be of benefit to the Revenue – claim to rely on the advice of a professional accountant as a reasonable excuse – need proof to substantiate such claim – relatively small amount of incomes received was not a reasonable excuse for their omissions – little co-operation of the appellant in the course of the Revenue's investigation – adopted a wait and see attitude even after being reminded of the basic obligation – time consuming investigation – ample justification for adopting a higher rate of additional assessments.

Panel: Ronny Wong Fook Hum SC (chairman), Christine Koo and Agnes Ng Ka Yin.

Date of hearing: 26 April 2003.
Date of decision: 15 July 2003.

Since 1992, the appellant was employed as a sales executive of motor vehicles by Company A, which was subsequently acquired by Company B in 1997. Apart from receiving earnings from Company A, the appellant also received commission from Companies C, D, E, F, G and H for introducing clients regarding car purchase finance facilities, car insurance, etc in the course of dealings with motor vehicles.

Investigations by the Revenue revealed that the appellant failed to report to the Revenue her income from Companies C, D, E, F, G and H for six years of assessment between 1993 and 1999.

As a result, the Revenue imposed additional tax on the appellant by way of penalty against the appellant for the said six years of assessment at the average rate of 73.85% of the tax undercharged.

The appellant appealed against these additional assessments so imposed on the grounds that she had a reasonable excuse in respect of each of the omitted items and that the amounts so imposed were excessive.

The facts appear sufficiently in the following judgment.

Held:

1. No reasonable excuse

(a) This case was clearly distinguishable from D18/91 which related to non-inclusion in returns of profits arising from disposals of assets which the taxpayers maintained on professional advice to be capital as opposed to trading assets.

(b) There was no credible evidence before the Board of any alleged agreement between Company C and the appellant for Company C to shoulder the tax liability of the appellant. There was no evidence of any step taken by the appellant to verify the due discharge by Company C of the alleged obligation assumed by Company C.

(c) Mr K, a professional accountant, had not been called to give evidence to explain the basis of any advice that he might have given to the appellant.

(d) It was neither clear whether Mr K's alleged advice was confined to the burden of tax liability nor whether he went to the extent that there was no need to report the income in view of the tax burden.

(e) In their letter dated 14 June 2000, the Revenue gave a clear explanation to the appellant as to her basic obligation under the Inland Revenue Ordinance ('IRO'). There was no effective refutation against such exposition by the Revenue. The Board therefore entertained serious reservations as to the reasonableness of any advice which Mr K might have proffered to the appellant.

(f) There was no disclosure to the Revenue of the underlying facts. This was not a case where the Revenue and the appellant had a dispute on the interpretation to be placed on the disclosed fact. This was a case where the facts had to be uncovered by time consuming efforts on the part of the Revenue.

(g) For these reasons, the Board held that the appellant had no reasonable excuse for omitting the commissions from Company C.

(h) Her position vis-a-vis the commission she received from Company E was no better.

(i) It was her basic obligation to report her income to the Revenue.

(j) This basic obligation could not be compromised by pretending that its non-fulfillment might be of benefit to the Revenue. The Board failed to see the risk of any double reporting arising from the special group relationship. The Board was inclined to the view that the arrangement was a convenient means to keep the Revenue in the dark.

(k) The appellant did not provide full particulars to the Revenue in support of her claim that the commissions she received from Company D were paid over to her relatives. She eventually accepted that $6,722 was part of her income. It was too late for her to re-open this issue before the Board.

(l) The payments from Companies D, G and H were small as compared to the payments from Companies C and E but that was not a good reason for their omissions.

(m) For these reasons, the Board was of the view that the appellant had no reasonable excuse for her incorrect returns.

2. Level of penalty

(a) In D103/01, the average penalty imposed on a sales executive of motor vehicles who omitted to report 51.66% of her total income for the years of assessment 1993/94 to 1998/99 was 65.79% of the tax undercharged. The Board refused to interfere with the additional tax so imposed.

(b) In the present case, the appellant omitted 41.64% of her total income for the years of assessment 1993/94 to 1998/99. The average penalty tax imposed was 73.85% of the tax undercharged.

(c) The Board was of the view that, given the attitude of the appellant, there was justification for adopting a higher rate in this case. The appellant displayed little co-operation in the course of the Revenue's investigation. After being reminded of her basic obligation, she adopted a wait and see attitude.

(d) The appellant did not volunteer any information about her receipts of her income but reluctantly accepted the results of the Revenue's investigations when it became clear that there was no escape.

(e) For these reasons, the Board was not prepared to differ from the Commissioner on the additional tax which he imposed.

Appeal dismissed.

Cases referred to:

BR80/76, IRBRD, vol 1, 259
D18/91, IRBRD, vol 6, 36
CIR v Mayland Woven Labels Factory Ltd 1 HKTC 630
D103/01, IRBRD, vol 16, 837

Mei Yin for the Commissioner of Inland Revenue.
Taxpayer represented by her tax representative.

Decision:

1. The Appellant commenced employment with Company A selling motor cars on 16 June 1992. On top of a basic salary, Company A paid her commission and bonus.

2. Company B acquired the entire shareholding of Company A on 12 May 1997. The terms of the Appellant's employment remained unchanged after such acquisition.

3. In the course of her employment with Company A, the Appellant received commission from

(a) finance companies in respect of instalment loans extended by such companies to purchasers of motor vehicles. Company C was one of those companies.

(b) insurance companies in respect of policies of insurance taken out by purchasers of motor vehicles. Company D and Company E were amongst the insurance companies making such payments in favour of the Appellant.

(c) motor companies in the course of dealings with motor vehicles. We are concerned with three such companies: Company F; Company G and Company H.

4. Investigations by the Revenue revealed that the Appellant failed to report to the Revenue her income from Companies C, D, E, F, G and H as follows:

Year of assessment	Company C	Company D	Company E	Company F	Company G	Company H	Total
	$	$	$	$	$	$	$
1993/94	314,826	6,722	20,284				341,832
1994/95	61,097		99,566	146,615	6,471		313,740
1995/96	34,981		102,513				137,494*
1996/97	30,822		43,440	20,280		4,608	99,150
1997/98	19,114		45,183	12,801			77,098
1998/99	96,825		33,212				130,037
	557,665	6,722	344,198	179,696	6,471	4,608	1,099,360*

5. By notices dated 27 January 2003, the Commissioner imposed additional tax on the Appellant computed as follows:

Year of assessment	Income after investigation	Income returned	Income short returned	Amount of tax undercharged	Additional tax imposed	Percentage of additional tax over amount of tax undercharged
	$	$	$	$	$	%
1993/94	918,432	576,600	341,832	41,019	30,700	74.84
1994/95	557,944	244,195	313,749	49,737	37,300	74.99
1995/96	318,286	180,791	137,495*	21,763	16,300	74.89
1996/97	202,415	103,265	99,150	15,864	11,800	74.38
1997/98	216,509	139,411	77,098	13,878	10,400	74.93
1998/99	425,058	296,021	130,037	22,106	14,900	67.40
	2,638,644	1,540,283	1,099,361*	164,367	121,400	

* Minor discrepancies between the figures which are not material

6. This is the Appellant's appeal against the additional tax so imposed. We are concerned with two issues. First, the Appellant says that she has a reasonable excuse in respect of each of the omitted items. Secondly, she says that the amount imposed is excessive.

Any reasonable excuse

7. The Appellant contends as follows:

(a) In respect of Companies C and F: She relied on the advice of a professional accountant to the effect that she was not liable to salaries tax for the sums she received.

(b) In respect of Company E: ' [Company E] and [Company A] were the member companies of [Group I]. In view of their special relationship, [the Appellant] was told by Account Department of [Company A] ... that the commission payable to [the Appellant] by [Company E] and [Company A] would be combined together for tax return and administration purposes' . ' Due to the wrong information given by the staff concerned and special group relationship between [Company E] and her then employer' , she omitted the commission she received from Company E ' to avoid double reporting' .

(c) In respect of Company D: She refunded the commission received to her relatives and friends.

(d) In respect of Companies G and H: She made a genuine mistake in relation to two insubstantial amounts.

8. The Revenue commenced investigations into the affairs of the Appellant in 2000. By letter dated 13 May 2000, the Appellant asserted that:

' As promised by [Company C], the tax liabilities of [the Appellant] on the above commission would be totally borne and taken up by [Company C] in either one of the following treatments.

(a) The commission payable to [the Appellant] was not charged to [Company C' s] profit and loss account, so that such amount had been taxed under the profit tax regime. The nature of which is similar to dividend income received from corporations.

(b) The salary tax of the above commission is paid by [Company C]' .

9. Mr J is the husband of the Appellant. Mr J acted as the Appellant' s tax representative in her correspondence with the Revenue. Mr J had apparently consulted Mr K, a professional accountant, and Mr K advised him that the Appellant ' could be exempted from [her] salary tax liability under any one of the above arrangements ...' .

10. By letter dated 14 June 2000, the Revenue explained to the Appellant that:

' All taxpayers are required by law to report their income or profits chargeable to tax in their tax returns ... The reporting obligation is imposed on the taxpayers by law and cannot be shifted or waived by the action or inaction of others.

Any person may enter into an agreement with his/her employer or principal for arranging the payment of tax in respect of the income received. The tax, if paid by

> the employer or principal, will form part of his/her income and subject to tax. In your case, there is no evidence to support that you entered into such an agreement with [Company C] ... If [Company C] did fail to honour its agreement, it would be a personal matter between you and the company'.

11. By letter dated 31 May 2002, Company C informed the Revenue that 'We would not pay any tax on the commission for the sales representatives. As such, there is no written or verbal agreement between our company and the sales representatives that we would pay the tax on commission paid to the sales representatives'.

12. By letter also dated 31 May 2002, Company E denied there was any agreement between Company E and the sales representatives for Company E to pay tax on the commissions paid to the sales representatives. Company E further pointed out that 'the sales representatives were supposed to report their income to I.R. directly by themselves'.

13. Mr J appeared on behalf of the Appellant at the hearing before us. He reiterated the advice he received from Mr K. He drew our attention to two decisions of this Board in BR80/76, IRBRD, vol 1, 259 and D18/91, IRBRD, vol 6, 36. Both cases relate to non-inclusion in returns of profits arising from disposals of assets which the taxpayers maintained on professional advice to be capital as opposed to trading assets. D18/91 provides a good illustration of the applicable principles. The tax representative gave evidence. She said she formed the view that the properties in question were investment properties and advised her client accordingly. She pointed out that there was never any intention to keep the fact that the properties had been disposed of from the Revenue: it was a fact that the Revenue already knew. She gave reasons why she considered that the properties in question were investment properties. It was not put to her that she could not honestly have reached that view or that her view was otherwise unreasonable. The Board there pointed out that:

> *'Our finding in no way detracts from the undoubted requirement of making a proper return with supporting information as stressed by McMullin J in CIR v Mayland Woven Labels Factory Ltd 1 HKTC 630. The mere fact that the taxpayer was acting upon professional advice would not necessarily furnish a reasonable excuse for failure to comply with the requirement: indeed the fact that he was assisted by professional advisers could sometimes make it more difficult for the taxpayer to put forward any reasonable excuse for not having made a correct return. Everything depends on the facts of each case. Here there was disclosure of the fact of disposition (and the aggregate proceeds) prior to the return, followed by further information shortly after the making of the return in circumstances in which estimated assessments had already been made prior to the return and objection thereto actively pursued by the Taxpayer who acted on professional advice throughout and reasonably left the manner and form of the return to the professional advisers who, as we*

have found, also acted honestly and reasonably throughout with no intention to withhold any requisite supporting information'.

14. This case is clearly distinguishable from D18/91.

(a) There is no credible evidence before us of any agreement between Company C and the Appellant for Company C to shoulder the tax liability of the Appellant. There is no evidence of any step taken by the Appellant to verify the due discharge by Company C of the alleged obligation assumed by Company C.

(b) Mr K has not been called to give evidence to explain the basis of any advice that he might have given to the Appellant via Mr J. It is not clear to us whether Mr K's alleged advice was confined to the burden of tax liability or whether he went to the extent that there was no need to report the income in view of the tax burden. In their letter dated 14 June 2000, the Revenue gave a clear explanation to the Appellant as to her basic obligation under the IRO. There was no effective refutation against such exposition by the Revenue. We therefore entertain serious reservations as to the reasonableness of any advice which Mr K might have proffered to the Appellant.

(c) There was no disclosure to the Revenue of the underlying facts. This is not a case where the Revenue and the Appellant had a dispute on the interpretation to be placed on the disclosed fact. This is a case where the facts had to be uncovered by time consuming efforts on the part of the Revenue.

15. For these reasons, we are of the view that the Appellant has no reasonable excuse for omitting the commissions from Company C.

16. Her position vis-a-vis the commission she received from Company E is no better. It is her basic obligation to report her income to the Revenue. That obligation cannot be compromised by pretending that its non-fulfillment might be of benefit to the Revenue. We fail to see the risk of any double reporting arising from the special group relationship. We are inclined to the view that the arrangement was a convenient means to keep the Revenue in the dark.

17. The Appellant did not provide full particulars to the Revenue in support of her claim that the commissions she received from Company D were paid over to her relatives. She eventually accepted that $6,722 was part of her income. It is now too late for her to re-open this issue before us. The payments from Companies D, G and H are small as compared to the payments from Companies C and E but that is not a good reason for their omissions.

18. For these reasons, we are of the view that the Appellant has no reasonable excuse for her incorrect returns.

Level of penalty

19. In D103/01, IRBRD, vol 16, 837 the average penalty imposed on a sales executive of motor vehicles who omitted to report 51.66% of her total income for the years of assessment 1993/94 to 1998/99 was 65.79% of the tax undercharged. The Board refused to interfere with the additional tax so imposed.

20. In this case the Appellant omitted 41.64% of her total income for the years of assessment 1993/94 to 1998/99. The average penalty tax imposed is 73.85% of the tax undercharged.

21. We are of the view that there is justification for adopting a higher rate in this case. The Appellant displayed little co-operation in the course of the Revenue's investigation. After being reminded of her basic obligation, she adopted a wait and see attitude. She did not volunteer any information about her receipts but reluctantly accepted the results of the Revenue's investigations when it became clear that there was no escape. For these reasons, we are not prepared to differ from the Commissioner on the additional tax which he imposed.