# Case No. D80/96

**Penalty tax** – incorrect salaries tax return – failure to disclose gains from exercise of share options – first offender – ignorant of law – unintentional – 10% penalty under section 82A of Inland Revenue Ordinance.

Panel: Christopher Chan Cheuk (chairman), Daniel Cheung Kwok Chun and Elsie Leung Oi Sie.

Date of hearing: 8 November 1996.
Date of decision: 14 December 1996.

The taxpayer was employed by a public company and served as its director. He was given certain share options. He exercised them in two respective years of assessment, 1992/93 and 1993/94.

The taxpayer did not disclose in his tax returns the gains realised on exercise of share options. On 23 May 1995 and 8 June 1995 the Revenue made assessments for those gains. The taxpayer did not object to the assessments.

On 12 February 1996 the Commissioner issued notices of assessment for additional tax under section 82A in the amounts of $6,900 and $9,600 for the two respective years of assessment.

Held:

The Board was satisfied that the taxpayer was a first offender, that he was ignorant of the law and that the omissions were unintentional. The Board held the view that each case should be decided on its own merits. Tax Case D25/96 was distinguished. The Board followed the tariff rate in recent cases and decided that the additional taxes under section 82A be reduced to the sums equivalent to about 10% of the taxes undercharged.

**Appeal allowed.**

Cases referred to:

D25/96, IRBRD, vol 11, 478
D54/93, IRBRD, vol 8, 391
D46/94, IRBRD, vol 9, 282
D52/95, IRBRD, vol 11, 7

D58/95, IRBRD, vol 11, 24

Tung Wai Wah for the Commissioner of Inland Revenue.
Taxpayer represented by his wife.

**Decision:**

## Appeal

1. This is an appeal against the assessment for additional tax under section 82A of the Inland Revenue Ordinance (the IRO) for respective years of assessment 1992/93 in the amount of $6,900 and 1993/94, $9,600. However, Ms TUNG representing the Revenue has conceded that these two sums should be amended to the figures of $6,200 and $9,100 respectively if the Board dismisses the appeal.

## Facts and Evidence

2. The Taxpayer did not personally appear but had duly authorised his wife, Mrs A to handle the case for him. Mrs A was capable not only in presenting the facts of the case but also citing cases in support; she cogently argued in favour of the Taxpayer in her submission.

3. Before hearing Ms TUNG for the Revenue had submitted the agreed bundle of documents and the agreed facts which were confirmed by Mrs A on behalf of the Taxpayer. After the procedure had been explained to her, Mrs A decided not to give any evidence or call any witness. She relied purely on the facts and documents agreed.

4. Facts of the case are briefly set out below:

(a) On 28 April 1994 and 22 May 1994 the Taxpayer filed his salaries tax returns for years of assessment 1992/93 and 1993/94 respectively.

(b) Information available to the Revenue revealed that the Taxpayer had omitted the gains realised on exercise of share options for the following years:

| **Year of Assessment** | **Amount** **$** |
|---|---|
| 1-4-1992 to 31-3-1993 | 167,000 |
| 1-4-1993 to 31-3-1994 | 244,000 |

(c) On 23 May 1995 and 8 June 1995 assessments were made on the two incomes and the additional taxes were assessed to be $25,125 and $36,675 respectively. The Taxpayer did not object to the assessments.

(d) On 12 February 1996 the Commissioner issued notices of assessment for additional tax under section 82A of the IRO in the amounts of $6,900 for the year of assessment 1992/93 and $9,600 for the year of assessment 1993/94.

(e) The Taxpayer appealed against such additional assessments.

5. It was confirmed by Mrs A on behalf of the Taxpayer that the Taxpayer did not appeal against liability and that the only ground of appeal was that the additional taxes imposed under section 82A were excessive and unreasonable. Hearing proceeded on this basis.

**Taxpayer's Submission**

6. The Taxpayer's reasons for appeal could be found in the following documents:

(a) Letter dated 12 January 1996 to the Commissioner of Inland Revenue;

(b) Letter dated 2 March 1996 to the Clerk to the Board of Review; and

(c) the Written Submission delivered to the Board at the hearing.

Mrs A orally supplemented and explained the reasons before the Board.

7. The Taxpayer was a first offender and in the past years he had never omitted or inaccurately completed any return. The Revenue did not dispute this fact.

8. The Taxpayer claimed that he had no knowledge and was ignorant of the law that gains realised by exercise of share option were taxable. Whilst ignorance of the law was no defence, the Taxpayer urged the Board to consider this as a mitigating factor. The Revenue's reply was that for each return issued to a taxpayer, it was accompanied with relevant 'notes' to assist the taxpayer to compete the return. In item 8(g) of the notes, the legal position was clearly set out. In case of doubt, a telephone hotline was available for enquiry. The Board has found that the Taxpayer did not complete the returns with due care but the omissions were not intentional.

9. The Taxpayer also argued that he relied on the information supplied by his employer to complete his return. As his employer's returns did not disclose such information and he thought they were complete and correct, he accordingly copied and followed the information contained therein. The Board cannot accept such argument for the following reasons:

(a) The Taxpayer was at all material times a director, most probably an executive director of the employer, a public company; and

(b) The duty to complete a true and correct return falls solely upon the Taxpayer.

10. The Taxpayer had not disposed of all the shares he obtained from exercise of the option. The gain at the time of taxation was only a notional gain and had he known that tax would be imposed on exercise and not on disposal of the shares he would have exercised the option when the share price was low. It is not proper for the Board to speculate when he should exercise the option. Neither does the Board think that whether the shares have been sold is a relevant factor for consideration.

11. Mrs A cogently argued that had the Revenue discovered the mistake during the period after the employer had filed its returns and before he completed his, the Taxpayer would have avoided the mistake. The Board had no knowledge of how Inland Revenue Department operated. For reasons stated in paragraph 9 above the Board does not find favour in this argument.

12. Mrs A stated that the two returns came almost at the same time and the Taxpayer was required to complete them almost together. It could be construed as 'double penalty'. The Revenue representative explained that the Taxpayer changed address and did not inform the Revenue. This was the reason why the two returns reached the Taxpayer at such late stage and almost at the same time. The Board accepted the explanation of the Revenue.

13. The Revenue had the right to make amendment when it committed a mistake; Mrs A queried why the Taxpayer could not be given such a chance. The simple answer is that the law stipulates that the Revenue has the right to impose additional assessment for any incorrect return by omission or understatement under section 82A.

**Revenue's Submission**

14. Ms TUNG's submission was very well prepared and apart from those the Board has referred to earlier she also submitted on what the right amount should be for this case. She referred to D25/96 and asked the Board to adopt a rate of 25% of tax undercharged as the rate for this case. The Board having read D25/96 has come to the conclusion the present case is different from D25/96 significantly. The Board in the latter case described the Taxpayer's attitude in the following words at page 3 of the decision:

> 'In short, the Taxpayer's evidence showed, at best, a cavalier disregard for complying with the obligations imposed upon him by IRO…'

The Board thinks that D25/96 was decided on its own merits and has no application to the present one.

**Board's Findings**

15. The Board holds the view that each case should be decided on its own merits and has found that the Taxpayer was a first offender, that he was at that time ignorant of the law and that the omissions were unintentional.

16. The Board has also made reference to other cases including the two submitted by Mrs A: D54/93 and D46/94 and the cases recently reported: D52/95 and D58/95; all indicate that the rate was about 10% of the tax undercharged.

**Determinated**

17. For reasons stated above the Board has found that additional taxes of $6,900 and $9,600 or even $6,200 and $9,100 which represent 24.7% and 24.8% of the taxes undercharged are too high and excessive in the circumstances of the case. The Board allows the appeal to the extent, and it doth hereby order, that the additional taxes imposed under section 82A be reduced to $2,500 for year of assessment 1992/93 and $3,700 for year of assessment 1993/94.