

Case No. D45/13

Penalty tax – late filing of tax returns – sections 51(1), 59(3), 60(1), 68, 80(2), 82(1), 82A and 82B of the Inland Revenue Ordinance.

Panel: Kenneth Kwok Hing Wai SC (chairman), Lam Ting Kwok Paul SC and Timothy Shen Ka Yip.

Date of hearing: 29 November 2013.

Date of decision: 10 March 2014.

The Appellant was late for 3 consecutive years in its submission of profits tax returns. No penalty action was taken in respect of the Appellant's late filing for the 2009/10 and 2010/11 years of assessment. By an assessment dated 7 July 2013 ('the Assessment'), the Appellant was assessed to penalty tax of the amount of \$30,000 for its late filing of the return for the 2011/12 year of assessment (with a delay of 21 days), which represented 3.04% of the tax undercharged.

The Appellant appealed against the assessment. However, before the appeal hearing, the Appellant informed the Board that the Commissioner had agreed to reduce the amount of the additional tax from \$30,000 to \$10,000. The Clerk to the Board informed the Appellant that the Board was the decision maker on an appeal to the Board and the Appellant's letter contained no information for the Board to reduce the penalty assessment. There was no response to the Clerk's letter by the Appellant.

In its grounds of appeal, the Appellant claimed, among other things, that the delay was only 21 days and was due to the cancer sickness of the wife/partner, and that it was the auditors who prepared the accounts. The Appellant also raised that after filing the tax returns it had to pay more tax than that assessed under the estimated assessment by the Assessor before the filing.

Held:

1. The Appellant closes its account annually on 31 March. The Return was issued on the 16 April 2012 and the Appellant had 7 months to complete and submit the Return. The audited financial statements were approved by the Appellant's director on 29 November 2012 and the audited financial statements were dated the same date. It was past the Extended Due Date and yet the Appellant managed to take 7 days to submit the Return to the Revenue.

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2. A second or further contravention is an aggravating factor. A heavier penalty should, as a general rule, be imposed for subsequent contraventions. This was the Appellant's third contravention in 3 consecutive years of assessment.
3. Payment of tax, whether by the taxpayer-Appellant or by somebody else, is not a relevant factor. It is the duty of every taxpayer to pay the correct amount of tax. If he/she does not pay tax, on time or at all, he/she will be subject to enforcement action.
4. It was open to the Assessor to assess on the basis of the profits as reported by the Appellant. The issue of an estimated assessment and the issue of a subsequent adjustment assessment was a waste of the Revenue's resources. Nothing was further from the truth than the Appellant's assertion that 'more tax had been paid'. The statutory scheme is that the maximum penalty is treble the tax which has been undercharged *or which would have been undercharged if such failure had not been detected* (see Dodge Knitting co Ltd and Dodge Trading Ltd v CIR 2 HKTC 597).
5. There is **no** evidence of any oversight on the part of the auditor. Even if the auditor were at fault, that is a matter between the Appellant and the auditor. The statutory reporting duty falls fairly and squarely on the Appellant.
6. In the circumstance, the penalty assessment of 3.04% was so lenient that there is simply no room for reduction.
7. The Board found the Appeal frivolous and vexatious and plainly unarguable.

Appeal dismissed and costs order in the amount of \$2,000 imposed.

Cases referred to:

D7/11, (2011-12) IRBRD, vol 26, 93
Shui On Credit Company Limited v Commissioner of Inland Revenue (2009) 12
HKCFAR 392
Commissioner of Inland Revenue v Nina T H Wang [1993] 1 HKLR 7
Dodge Knitting Co Ltd and Dodge Trading Ltd v CIR 2 HKTC 597

Sandhu Kirpal Singh of Appellant for the Appellant.
Tang Siu Fung and Wong Yuk Yee for the Commissioner of Inland Revenue.

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Decision:

Introduction

1. The Appellant was late for 3 consecutive years in its submission of profits tax returns:

| <u>Year of assessment</u> | <u>Return issue date</u> | <u>Return due date</u> | <u>Date of audited financial statements</u> | <u>Date of receipt of the return</u> | <u>Period of delay</u> | <u>Tax undercharged</u> |
|---------------------------|--------------------------|------------------------|---|--------------------------------------|------------------------|-------------------------|
| 2009/10 | 09-01-2012 | 09-02-2012 | 01-12-2011 | 28-02-2012 | 19 days | \$131,423 |
| 2010/11 | 09-01-2012 | 09-02-2012 | 01-12-2011 | 28-02-2012 | 19 days | \$529,253 |
| 2011/12 | 16-04-2012 | 15-11-2012 | 29-11-2012 | 06-12-2012 | 21 days | \$988,209 |

2. (1) No penalty action was taken in respect of the Appellant’s late filing for the 2009/10 and 2010/11 years of assessment.

(2) By an assessment dated 7 July 2013 (‘the Assessment’), the Appellant was assessed to penalty tax for its late filing of the return for the 2011/12 year of assessment:

| Return issue date | Return extended due date | Date of audited financial statements | Date of receipt of the return | Period of delay | Tax undercharged | Amount of additional tax by way of penalty | Percentage of additional tax on tax undercharged |
|-------------------|--------------------------|--------------------------------------|-------------------------------|-----------------|------------------|--|--|
| 16-04-2012 | 15-11-2012 | 29-11-2012 | 06-12-2012 | 21 days | \$988,209 | \$30,000 | 3.04% |

3. By ‘Notice of Appeal’ dated ‘5 July 2012’ (*sic*), the Appellant gave notice of appeal against the Assessment.

4. By letter dated 8 November 2013, the Assessor wrote to the Clerk to the Board of Review informing the Board that:

‘... an agreement, subject to the approval of the Board of Review, has been reached between the Appellant and the Commissioner for settling the captioned appeal.’

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It was stated in the compromise agreement that:

‘ The Appellant has subsequently provided further information to the Commissioner in respect of its delay in filing the Return. Having considered the further information, the Commissioner agrees to take a more lenient approach and reduce the amount of the additional tax [from \$30,000 to \$10,000].’

5. By letter dated 11 November 2013, the Clerk wrote to the Respondent, copied to the Appellant, stating that:

‘ The Board is the decision maker on an appeal to the Board.

Your letter contains no information for the Board to reduce the penalty assessment.

Unless the Appellant satisfies the Board at the hearing on appeal to reduce, or unless the appeal is withdrawn under section 68(1A)(a) of the Inland Revenue Ordinance, Cap. 112, the hearing of the appeal will proceed on 29 November 2013.’

6. There was no response to the Clerk’s letter and the hearing of the Appeal took place on 29 November 2013.

Finding of facts

7. The Appellant has appealed against the imposition of additional tax by way of penalty assessed upon it under section 82A of the Inland Revenue Ordinance, Chapter 112 (‘the Ordinance’), for the failure to comply with the requirement of a notice under section 51(1) of the Ordinance to furnish a profits tax return for the year of assessment 2011/12 (‘the Return’) within the prescribed time allowed.

8. Particulars of the Appellant’s delay in filing the Return and the additional tax by way of penalty are as follows:

| Return issue date | Return extended due date | Date of audited financial statements | Date of receipt of the return | Period of delay | Tax undercharged | Amount of additional tax by way of penalty | Percentage of additional tax on tax undercharged |
|-------------------|--------------------------|--------------------------------------|-------------------------------|-----------------|------------------|--|--|
| 16-04-2012 | 15-11-2012 | 29-11-2012 | 06-12-2012 | 21 days | \$988,209 | \$30,000 | 3.04% |

9. The Appellant is a private company incorporated in Hong Kong in November 2004. It closes its accounts annually on 31 March.

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10. The principal activity of the Appellant as reported in the Return was property investment and the provision of consultancy services.

11. On 16 April 2012, the Assistant Commissioner of Inland Revenue issued a notice for filing the Return to the Appellant. By virtue of section 51(1) of the Ordinance, the Appellant was required to complete and submit the Return within one month from 16 April 2012.

12. Pursuant to a Block Extension Scheme for lodgement of 2011/12 profits tax returns, which applied also to the Appellant, the due date for filing the Return was extended to 15 November 2012 ('the Extended Due Date'). The Appellant did not submit the Return by the Extended Due Date.

13. On 6 December 2012, the Assessor raised on the Appellant an estimated assessment for the year of assessment 2011/12 pursuant to section 59(3) of the Ordinance as follows:-

| | |
|------------------------------|--------------------|
| Estimated assessable profits | <u>\$3,530,000</u> |
| Tax payable thereon | <u>\$570,450</u> |

14. The Appellant did not lodge any objection against the estimated assessment in paragraph 13.

15. On 6 December 2012, the Department received the Return with the tax computation and audited financial statements for the year ended 31 March 2012 submitted by the Appellant, reporting assessable profits of \$6,031,637. The Auditor's Report was signed on 29 November 2012. The financial statements were approved by the Appellant's director on the same day.

16. On 21 December 2012, the Assessor raised on the Appellant an additional assessment for the year of assessment 2011/12 as follows:-

| | |
|---|--------------------|
| Profits per return | \$6,031,637 |
| <u>Add</u> : Adjustment of depreciation allowance | <u>30,241</u> |
| Adjusted assessable profits | \$6,061,878 |
| <u>Less</u> : Profits already assessed | <u>3,530,000</u> |
| Additional assessable profits | <u>\$2,531,878</u> |
| Tax payable thereon | <u>\$417,759</u> |

17. The Appellant did not lodge any objection against the additional assessment for the year of assessment 2011/12 in paragraph 16.

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

19. On 23 April 2013, the Respondent issued to the Appellant a notice of intention to assess additional tax under section 82A of the Ordinance ('the Notice') in respect of its failure to furnish the Return within the prescribed time allowed. If the Department had not detected the failure, tax amounting to \$988,209 would have been undercharged. The Notice stated that additional tax by way of penalty up to three times the amount of tax that would have been undercharged might be imposed if the Appellant did not have a reasonable excuse for the failure. The Appellant was invited to submit written representations to the Respondent.

20. By a letter received by the Department on 25 April 2013, the Appellant made written representations to the Respondent.

21. On 7 June 2013, the Respondent, having considered and taken into account the written representations, issued a notice of assessment for additional tax by way of penalty under section 82A of the Ordinance in the amount \$30,000¹.

22. By a letter dated 5 July 2012 (*sic*), the Appellant gave a notice of appeal to the Clerk to the Board of Review against the Assessment.

23. The Appellant's previous failure in filing profits tax returns are shown as follows:-

| Year of assessment | Return issue date | Return due date | Date of audited financial statements | Date of receipt of the return | Period of delay | Tax undercharged |
|--------------------|-------------------|-----------------|--------------------------------------|-------------------------------|-----------------|------------------|
| 2009/10 | 09-01-2012 | 09-02-2012 | 01-12-2011 | 28-02-2012 | 19 days | \$131,423 |
| 2010/11 | 09-01-2012 | 09-02-2012 | 01-12-2011 | 28-02-2012 | 19 days | \$529,253 |

24. No penalty action was taken in respect of the Appellant's failure to file profits tax returns within the prescribed time allowed for the years of assessment 2009/10 and 2010/11.

¹ That is to say, the Assessment.

Grounds of Appeal

25. The Appellant's grounds of appeal, as written by the Appellant, read as follows:

1. The letter of representation made to the Director (*sic*) in response to the director's (*sic*) letter dated 23.4.2013 are repeated herewith (*sic*) as grounds of appeal.
2. The director (*sic*) had erred in its exercise of its (*sic*) discretion and/or the exercise of its (*sic*) discretion is Wednesbury unreasonable on the following grounds:
 - 2.1 The director (*sic*) failed to take into account that the delay was just for 21 days;
 - 2.2 The director (*sic*) had failed to take into account that the delay was due to the cancer sickness of the wife/partner [name omitted here] of the sole director and shareholder of [the Appellant]. She had passed away on 5.5.2013.
 - 2.3 The director (*sic*) had failed to take into account that [the Appellant] had paid taxes punctually for many years and had reported tax returns voluntarily and paid big sums as taxes in the past.
 - 2.4 The director (*sic*) had failed to take into account that the sole director [name omitted here] had loyally paid taxes to the Hong Kong Government since 1985 until 2009/2010, and again commencing since 2012/2013.
 - 2.5 The director (*sic*) had failed to adequately consider or had given not enough weight to the fact that there would have been no undercharge of taxes and in fact more tax had been paid than what the Respondent had raised as tax on the unfiled accounts. Furthermore, the director (*sic*) had failed to take adequate notice of the fact that auditors prepared the accounts and the delay is really due to extraneous circumstances surrounding the serious illness of the directors (*sic*) wife/partner, who eventually died and the delay was only for 21 days.
 - 2.6 The returns would have been filed in any event as it is not a case of not filing but a delay in filing due to very tough circumstances. The filed account led to bigger tax liability than originally imposed by the director (*sic*).

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- 2.7 [The Appellant] would wish to inform the director (*sic*) that the auditor also had a responsibility to seek an extension for filing which they have failed to do so and [the Appellant] should not be penalized for their oversight although this is not a case of blaming the auditor but part of the factual basis of the appeal.
3. Alternatively, the penalty of (*sic*) 30,000 is manifestly excessive and the director (*sic*) is urged to consider a more lenient penalty failing the above grounds of appeal.’

The relevant statutory provisions

26. Section 51(1) provides that:

‘An assessor may give notice in writing to any person requiring him within a reasonable time stated in such notice to furnish any return which may be specified by the Board of Inland Revenue for ... property tax, salaries tax and profits tax.’

27. Section 59(3) provides that:

‘Where a person has not furnished a return and the assessor is of the opinion that such person is chargeable with tax, he may estimate the sum in respect of which such person is chargeable to tax and make an assessment accordingly, but such assessment shall not affect the liability of such person to a penalty by reason of his failure or neglect to deliver a return.’

28. Section 60(1) provides that:

‘Where it appears to an assessor that for any year of assessment any person chargeable with tax has not been assessed or has been assessed at less than the proper amount, the assessor may, within the year of assessment or within 6 years after the expiration thereof, assess such person at the amount or additional amount at which according to his judgment such person ought to have been assessed, and the provisions of this Ordinance as to notice of assessment, appeal and other proceedings shall apply to such assessment or additional assessment and to the tax charged thereunder ...’

29. Section 68(4), (8)(a) and (9) provide that:

(4) *‘The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.’*

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(8)(a) *'After hearing the appeal, the Board shall confirm, reduce, increase or annul the assessment appealed against or may remit the case to the Commissioner with the opinion of the Board thereon.'*

(9) *'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 1 of Schedule 5, which shall be added to the tax charged and recovered therewith.'*

The amount specified in Part 1 of Schedule 5 is \$5,000.

30. Section 82A(1) provides that:

'Any person who without reasonable excuse ... (d) fails to comply with the requirements of a notice given to him under section 51(1) ... 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 ... has been undercharged in consequence of the failure to comply with a notice under section 51(1) ... or which would have been undercharged if such failure had not been detected.'

31. Section 82B(2) and section 82B(3) provide that:

82B (2) *'On an appeal against assessment to additional tax, it shall be 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.'*

82B (3) *'Sections 66(2) and (3), 68, 68A, 69 and 70 shall, so far as they are applicable, have effect with respect to appeals against additional tax as if such appeals were against assessments to tax other than additional tax.'*

Consideration of the grounds of appeal

32. By way of introductory observation, the grounds of appeal evince the Appellant's lack of proper concern for its statutory reporting duties. It is not clear whom the Appellant was referring to by 'the Director' or 'the director'.

33. More importantly, the grounds of appeal disclose no arguable ground of appeal.

34. As the Board said in D7/11, (2011-12) IRBRD, vol 26, 93, paragraph 3:

'The issue in an appeal before the Board is whether the assessment appealed against is incorrect or excessive, not whether the reasons given by the Commissioner were wrong². The appeal is a hearing de novo³. The onus of proving that the assessment appealed against is excessive or incorrect is on the taxpayer⁴. As the appeal is a hearing de novo and the onus of proof is on the Appellant, it will be more helpful and constructive for tax representatives to seek the agreement of the Respondent on facts which are not in dispute and adduce evidence with a view to proving facts in issue. The Revenue's treatment of facts at the objection stage is at best of historical interest and it is seldom, if ever, helpful to indulge in criticism of the Revenue's treatment of facts at the objection stage.'

35. Hong Kong's appellate courts have held that the Board must:

- (1) consider the matter from the beginning, anew; and
- (2) perform its 'ultimate function' to 'confirm, reduce, increase or annul the assessment' appealed against.
 - (a) In Shui On Credit Company Limited v Commissioner of Inland Revenue, (2009) 12 HKCFAR 392, Lord Walker NPJ said in the Court of Final Appeal judgment at paragraphs 29 and 30 that the Board's function is to consider the matter de novo (meaning starting from the beginning; anew) and the appeal is an appeal against an assessment:

'29. As the Board correctly observed, by reference to the decisions in Mok Tsze Fung v. CIR [1962] HKLR 258 and (after the amendment of s.64 of the IRO) CIR v. The Hong Kong Bottlers Ltd [1970] HKLR 581, the Commissioner's

² CIR v The Board of Review, ex parte Herald International Ltd [1964] HKLR 224 page 237; and Cheung Wah Keung v CIR [2002] 3 HKLRD 773 at paragraph 43.

³ Shui On Credit Company Ltd v CIR (2009) 12 HKCFAR 392 at paragraph 30.

⁴ Section 68(4) of the Ordinance and Mok Tsze Fung v CIR [1962] HKLR 258 at page 281; and All Best Wishes Limited v CIR (1992) 3 HKTC 750 at page 772.

function, once objections had been made by the taxpayer, was to make a general review of the correctness of the assessment. In Mok Tsze Fung v Commissioner of Inland Revenue, Mills-Owens J said at pp 274-275:

“His duty is to review and revise the assessment and this, in my view, requires him to perform an original and administrative, not an appellate and judicial, function of considering what the proper assessment should be. He acts de novo, putting himself in the place of the Assessor, and forms, as it were, a second opinion in substitution for the opinion of the Assessor.”

30. *Similarly the Board’s function, on hearing an appeal under s.68, is to consider the matter de novo: CIR v. Board of Review ex parte Herald International Limited [1964] HKLR 224, 237. The taxpayer’s appeal is from a determination (s.64(4)) but it is against an assessment (s.68(3) and (4)) ...’*

(b) In Commissioner of Inland Revenue v Nina T H Wang [1993] 1 HKLR 7, CA, Fuad VP said at page 23 that the Board must perform its ‘ultimate function’ to ‘confirm, reduce, increase or annul the assessment’ appealed against.

36. On an appeal to the Board:

- (1) The Board is the fact finding body. The onus is on the Appellant through the representative to adduce intelligible evidence on how the late filing came about [section 68(4)].
- (2) The Board, not the Commissioner, is the decision maker. If there is any discretion in any matter, such discretion is to be exercised by the Board.

37. The Appellant closes its account annually on 31 March. The Return was issued on the 16 April 2012 and the Appellant had 7 months to complete and submit the Return. The audited financial statements were approved by the Appellant’s director on 29 November 2012 and the audited financial statements were dated the same date. It was past the Extended Due Date and yet the Appellant managed to take 7 days to submit the Return to the Revenue.

38. A second or further contravention is an aggravating factor. A heavier penalty should, as a general rule, be imposed for subsequent contraventions. This was the Appellant’s third contravention in 3 consecutive years of assessment.

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39. Payment of tax, whether by the taxpayer-Appellant or by somebody else, is not a relevant factor. It is the duty of every taxpayer to pay the correct amount of tax. If he/she does not pay tax, on time or at all, he/she will be subject to enforcement action.
40. The assertions in grounds of appeal no. 2.5 and no. 2.6 misstate the facts.
41. Had the Appellant discharged its statutory reporting duties on time, it was open to the Assessor to assess tax on the basis of the profits as reported by the Appellant.
42. What happened was that the Appellant did not file the Return on time, the Assessor issued an estimated assessment under section 59(3). When the Assessor received the Return, it was open to the Assessor to assess on the basis of the profits as reported by the Appellant. The issue of an estimated assessment and the issue of a subsequent adjustment assessment was a waste of the Revenue's resources.
43. Nothing was further from the truth than the Appellant's assertion that 'more tax had been paid'.
44. The statutory scheme is that the maximum penalty is treble the tax which has been undercharged *or which would have been undercharged if such failure had not been detected.*
45. In Dodge Knitting co Ltd and Dodge Trading Ltd v CIR 2 HKTC 597, Liu J held that:
- ' Whilst limb one deals with an actual undercharge, limb two deals with an hypothetical undercharge - a hypothetical situation in a case where the failure was in fact detected - thus enabling the same penalty to be computed on a hypothetical sum of what would have been undercharged if such failure had not been detected.'*
46. The Board has repeatedly held that penalty tax should be considered as a percentage of the amount of tax involved.
47. Section 82A does not lay down any amount in dollar terms as a maximum. What it does provide for as the maximum is 'an amount not exceeding treble the amount of tax ...'
48. The maximum amount varies, depending on the size of the tax involved.
49. This is precisely the reason why there are numerous Board decisions making it clear that the correct approach in penalty tax cases is to look at the penalty tax as a percentage of the amount of tax involved.

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50. Where the amounts of tax involved are high, the maximum amount of additional tax will correspondingly be high in dollars.

51. There is **no** evidence of any oversight on the part of the auditor. Even if the auditor were at fault, that is a matter between the Appellant and the auditor. The statutory reporting duty falls fairly and squarely on the Appellant.

Conclusion and disposition

52. In the circumstance, the penalty assessment of 3.04% was so lenient that there is simply no room for reduction.

53. We dismiss the Appeal and confirm the Assessment.

Costs

54. This Appeal is frivolous and vexatious and plainly unarguable. We see no reason why other taxpayers should bear the costs of such a waste of public resources. Pursuant to sections 82B(3) and 68(9), the Appellant is **ordered to pay** the sum of **\$2,000 as costs** of the Board, which \$2,000 shall be added to the additional tax.