

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D10/01

Penalty tax – whether reasonable excuse – whether excessive.

Panel: Ronny Wong Fook Hum SC (chairman), Arthur Chan Ka Pui and Berry Hsu Fong Chung.

Date of hearing: 16 December 2000.

Date of decision: 17 April 2001.

On 17 August 1999, Mr A, Madam B and Mr F reached a settlement with the Revenue with respect to the liabilities of Company D and Company C for periods which they were respectively interested.

Subsequently, the Commissioner imposed additional tax on Company D and Mr A. They appealed against some of the assessments on the grounds that Mr A had little knowledge of accounting matters and the Revenue did not issue returns to Company D for the relevant years. Besides, the additional tax is excessive.

Held:

1. They had no reasonable excuse for their omissions. Furthermore, it is for them to report to the Revenue their accessibility (D24/84, IRBRD, vol 2, 136 followed).
2. The Board did not find any mitigation and the additional tax is not excessive (D2/88, IRBRD, vol 3, 125 and D52/93, IRBRD, vol 8, 372 followed).

Appeals dismissed.

Cases referred to:

D2/88, IRBRD, vol 3, 125
D24/84, IRBRD, vol 2, 136
D52/93, IRBRD, vol 8, 372

Wu Lee Sui Lan for the Commissioner of Inland Revenue.

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Yeung Mui Kwan David of Messrs David M K Yeung & Co for the taxpayer.

Decision:

Background

1. Mr A and Madam B were husband and wife. The marriage between them was dissolved on 9 November 1999.
2. On 1 July 1975, Mr A commenced business in the name of Company C. Madam B became an equal partner of Company C on 1 December 1993. Mr A withdrew from Company C on 28 February 1994.
3. By 4 January 1995, the following returns had been submitted in respect of the business in the name of Company C.

Year of assessment	Date when return issued	Date when return submitted	Basis period	Profit returned \$
1991/92	1-4-1992	17-10-1992	Up to 31-3-1992	120,605
1992/93	1-4-1993	13-12-1993	Up to 31-3-1993	101,081
1993/94	12-12-1994	4-1-1995	Up to 31-3-1994	107,094

4. On 1 October 1987, Mr A commenced business in the name of Company D. Mr E was his equal partner during the period between 1 April 1991 and 30 May 1991. As from 31 May 1991, Mr F took over the interest of Mr E. Mr F remained an equal partner until 25 August 1992. In so far as it is necessary, the business in the name of Company D for the period:
 - (a) between 1 April 1991 and 30 May 1991 will hereinafter be referred to as Company D I;
 - (b) between 31 May 1991 and 25 August 1992 will hereinafter be referred to as Company D II; and
 - (c) after 25 August 1992 will hereinafter be referred to as Company D III.
5. On 7 April 1992, Mr A submitted a return in respect of Company D I for the year of assessment 1990/91 reporting a loss of \$184,011. No further return in respect of Company D was submitted until 2 August 1994. As from 2 August 1994, the following returns were submitted on behalf of Company D III.

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Year of assessment	Date when return issued	Date when return submitted	Basis period	Profit returned \$
1993/94	2-5-1994	2-8-1994	Up to 31-3-1994	148,247
1994/95	1-5-1995	2-10-1995	Up to 31-3-1995	141,641
1995/96	1-5-1996	10-9-1996	Up to 31-3-1996	127,528
1996/97	1-5-1997	30-9-1997	Up to 31-3-1997	169,439

6. In September 1997, the Revenue commenced an investigation into the affairs of Mr A and Madam B. On 8 October 1997, the Revenue sent to Company D returns for the years of assessment 1991/92 and 1992/93. Company D applied to the Revenue for an extension of time for the submissions of these returns. The returns eventually submitted on 5 January 1998 reported the following profits:

Year of assessment	Basis period	Profit returned \$
1991/92	Up to 31-3-1992	289,191
1992/93	1-4-1992 to 14-9-1992	90,100

7. On 8 October 1997, the Revenue also sent to Mr A a return in respect of Company D III for the year of assessment 1992/93. A like application was made by Mr A for extension of time to submit this return. The return eventually submitted on 2 January 1998 reported the following profits:

Year of assessment	Basis period	Profit returned \$
1992/93	15-9-1992 to 31-3-1993	95,946

8. On 23 February 1998, the Commissioner made the following assessments in respect of the year of assessment 1991/92:

Entity assessed	Estimated profits \$
Company D	420,000
Company C	300,000 (additional)

9. By notice dated 25 March 1998, the Revenue asked Mr A to submit particulars of his assets and liabilities. The Revenue was informed by Mr A and Madam B on 18 May 1998 that they had appointed Messrs David M K Yeung & Co to handle their tax affairs. On 21 July 1998,

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the Revenue pressed Mr A for an answer to their earlier request of 25 March 1998. Mr A made partial compliance via Messrs David M K Yeung & Co on 24 August 1998 and 21 October 1998.

10. On 10 March 1999, the Revenue made the following assessments in respect of the year of assessment 1992/93:

Entity assessed	Profits assessed \$
Company D	200,000
Company C	200,000 (additional)
Company D III	295,946

11. On 17 August 1999, in the presence of their tax representative, Mr A, Madam B and Mr F reached a settlement with the Revenue with respect to the liabilities of Company D and Company C for periods which they were respectively interested. The effect of the settlement may be summarised as follows:

The entity	Year of assessment	Profit returned before investigation \$	Profit after investigation \$	Shortfall in profit \$	Tax undercharged \$
Company D	1991/92	0	227,887	227,887	40,113
	1992/93	0	172,009	172,009	31,996
Company D III	1992/93	0	195,270	195,270	34,457
	1993/94	354,836	354,836	0	0
	1994/95	347,077	347,077	0	0
	1995/96	253,535	290,616	37,081	6,022
	1996/97	226,900	256,286	29,386	10,107
		1,182,348	1,444,085	261,737	50,586
Company C	1993/94	107,094	229,328	122,234	11,523

Mr A, Madam B and Mr F were expressly warned that such settlement was without prejudice to the power of the Commissioner to impose additional tax.

12. On 31 August 1999, the Revenue issued revised assessments against the relevant entities on the basis of this settlement.

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13. By notice dated 14 February 2000, the Commissioner informed Company D of his intention to impose additional tax in respect of the years of assessment 1991/92 and 1992/93. By notice also dated 14 February 2000, the Commissioner informed Mr A trading as Company D III of his intention to impose additional tax for the years of assessment 1992/93, 1995/96 and 1996/97. After considering representations from Messrs David M K Yeung & Co dated 25 May 2000, the Commissioner imposed the following additional tax:

The entity	Year of assessment	Shortfall in profit \$	Tax undercharged \$	Additional tax \$	Relationship between additional tax and tax undercharged
Company D	1991/92	227,887	40,113	45,000	112%
	1992/93	172,009	31,996	36,000	112%
Company D III	1992/93	195,270	34,457	39,000	113%
	1995/96	37,081	6,022	6,000	100%
	1996/97	29,386	10,107	9,000	89%

14. By notice dated 25 May 2000, Company D appealed against the assessments for the years of assessment 1991/92 and 1992/93 on the following grounds:

- (a) There is a reasonable excuse for not notifying the Inland Revenue Department of its chargeability to profits tax.
- (b) There is no understatement of profits in the profits tax returns submission for the years of assessment 1991/92 and 1992/93.
- (c) Penalty of \$45,000 for the year of assessment 1991/92 and \$36,000 for the year of assessment 1992/93 representing 112% and 113% respectively on the profits tax amounts were excessive in view of the nature of non-compliance.

These are the issues raised in the first appeal.

15. By notice also dated 25 May 2000, Mr A trading as Company D III appealed against the additional tax assessment for the year of assessment 1992/93 in the sum of \$39,000 on similar grounds. This is the subject matter in the second appeal.

Case of the Taxpayers

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16. Mr A did not give evidence before us although he was present throughout the hearing.
17. Mr David Yeung on behalf of the Taxpayers submitted that:
- (a) Prior to the departure of Mr E, Mr A entrusted Mr E to handle all tax affairs. He began handling the fiscal matters of Company D after the departure of Mr E. Mr A was inexperienced and had little knowledge of accounting matters.
 - (b) The Revenue did not issue any return to Company D for the years of assessment 1991/92 and 1992/93. This is a relevant factor to be taken into consideration.
 - (c) Reliance is placed on the decision of this Board in D2/88, IRBRD, vol 3, 125 to support the contention that the penalties levied were excessive.

Our decision

18. We are surprised that the Taxpayers see fit to lodge these appeals. In D24/84, IRBRD, vol 2, 136 this Board emphatically stated that:

‘ Anyone who carries on business has obligations in respect to that business which include obligations under the Inland Revenue Ordinance. Such obligations cannot be avoided by saying that the taxpayer was ignorant, illiterate or unable to understand what the obligations required. Nor is it an excuse that qualified accountants were employed, as they could do no more than act on the information provided to them and in accordance with the instructions given to them.’

19. We have no doubt that the Taxpayers do not have reasonable excuse for their omissions. Mr A carried on two substantial businesses at the material times. The duty rests squarely on a taxpayer to report to the Revenue his accessibility. That duty will be rendered nugatory if its discharge is made dependent upon the Revenue’s notification.

20. The Taxpayers’ reliance on D2/88 is misplaced. The Board there thought ‘ *that the Commissioner has been very lenient in the present case*’ and the ‘ *future Boards may not be so lenient*’. Subsequent Board of Review cases [See, for example, D52/93, IRBRD, vol 8, 372] make it clear that ‘ *The normal measure of a penalty is 100% of the tax undercharged, assuming that there are no aggravating or mitigating factors. Here there are no mitigating factors, but there are aggravating ones. The penalties in question work out at an average of 116% of the tax undercharged; that, in our view, is not excessive.*’

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21. We are of the view that there are no mitigating factors in this case. As a result of their defaults, substantial public funds had been incurred in the investigation of the Taxpayers' affairs. the degree of co-operation from the Taxpayers was less than enthusiastic. We are not prepared to interfere with the penalties imposed.

22. For these reasons, we dismiss both appeals.