

Case No. D49/08

Penalty tax – additional tax assessment – return filed out of time – absence of reasonable excuse – assessment excessive or incorrect - onus wholly on the appellant – sections 51(1), 51C(1), 68(4), 68(8)(a), 68(9), 82A(1)(d), 82B, 66(2), 66(3), 68, 69 and 70 of the Inland Revenue Ordinance ('IRO').

Panel: Kenneth Kwok Hing Wai SC (chairman), Wendy O Chan and Lisa K Y Wong SC.

Date of hearing: 5 December 2008.

Date of decision: 12 January 2009.

The appellant failed to submit its profits tax return for the 2006/07 year of assessment by the extended deadline. It was out of time by more than 2 months.

The appellant 'opposed' the penalty / additional tax assessment of \$30,000 which was equivalent to 4.5% of the tax undercharged and 'wanted' the Board to waive the penalty.

Held:

1. There was no reasonable excuse for the appellant's failure to report within the extended time limit.
2. It is the duty of taxpayers to regulate its own affairs in such a way so as to comply with the requirements of the IRO.
3. In this case, the appellant's attitude and approach to put its house in order were far from re-assuring.
4. Penalty tax imposed under the IRO does not depend on the pleasure or agreement of the defaulting taxpayer.
5. The penalty of 4.5% of the amount of tax involved is by no means incorrect or excessive in the circumstances of this case.

Appeal dismissed and costs order in the amount of \$5,000 imposed.

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Cases referred to:

D25/97, IRBRD, vol 12, 204
D134/00, IRBRD, vol 16, 10
D57/06, (2006-07) IRBRD, vol 21, 1061

Taxpayer represented by its director.

Trevor Richmond, Ho Fung Sin and Mak Siu Ha Himmy for the Commissioner of Inland Revenue.

Decision:

Introduction

1. This is an appeal against the following assessment ('the Assessment') dated 8 September 2008 by the 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:

<u>Year of assessment</u>	<u>Additional tax</u>	<u>Charge no</u>
2006/07	\$30,000	X-XXXXXXXX-XX-X

2. The appellant failed to submit its profits tax return for the 2006/07 year of assessment by the extended deadline. It was out of time by more than 2 months.

3. Subject to adding back commercial building allowance over claimed, its return was accepted as correct.

4. The appellant was out of time by 6 days and 7 days in the preceding 2 years of assessment.

5. The Assessment, or penalty, was equivalent to 4.5% of the tax which would have been undercharged if the failure to comply with the statutory duty to report by the deadline had not been detected.

6. The appellant 'opposed' the penalty and 'wanted' the Board to waive the charges.

The agreed facts

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7. Based on the agreed Statement of facts, we make the following findings of fact.

8. The appellant has appealed against the imposition of additional tax by way of penalty assessed upon it under section 82A of 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 ('the Return') for the year of assessment 2006/07 within the prescribed time allowed.

9. Particulars of the appellant's delay in filing the Return for the year of assessment 2006/07 leading to the issue of the assessment of additional tax by way of penalty is as follows:

Year of assessment	2006/07
Date of issue of Return	2 April 2007
Extended due date for filing Return	15 November 2007
Date of receipt of Return	21 January 2008
Period of delay in filing Return	2 months and 6 days
Tax undercharged	\$661,407
Additional tax by way of penalty imposed	\$30,000
Percentage of additional tax on tax undercharged	4.5%

10. The appellant is a private company incorporated in Hong Kong on 20 February 1998. It commenced business in the year of assessment 1998/99 with its first accounts ended on 31 March 1999. At all relevant times, the appellant's principal business activity was import and export trade.

11. The appellant closes its accounts on 31 March each year.

12. On 2 April 2007, the Profits Tax Return for the year of assessment 2006/07 was issued to the appellant. The appellant was required to furnish and file the Return within one month from 2 April 2007. Under the block extension scheme for lodgement of 2006/07 tax returns, the deadline for submission of the Return was extended to 15 November 2007.

13. The Return was not submitted by the extended date. On 29 November 2007, an estimated assessment for the year of assessment 2006/07 and notice for payment of provisional tax for 2007/08 was raised on the appellant as follows:

	<u>2006/07</u>	<u>2007/08</u>	<u>Total tax payable</u>
	(Final)	(Provisional)	
Estimated assessable profits	\$3,200,000	\$3,200,000	
Tax payable	\$560,000	\$560,000	
<u>Less: Provisional tax already charged</u>	<u>\$507,880</u>	<u>NIL</u>	

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Net tax payable \$52,120 \$560,000 \$612,120

14. The assessor's Note to the notice of assessment stated that:

'This is an estimated assessment under section 59(3) of [the Ordinance] in the absence of a Profits Tax Return. If your company wishes to object to this assessment, your company must give the Commissioner notice in writing. The notice of objection together with a properly completed return must be received by the Commissioner WITHIN 1 MONTH after the date of this notice of assessment'.

15. The appellant has not lodged an objection against the assessment.

16. On 21 January 2008, a firm of certified public accountants ('CPA') submitted the Return of the appellant for the year of assessment 2006/07 together with the directors' report, financial statements and proposed [profits tax] computation for the year ended 31 March 2007. The Return showed assessable profits of \$3,602,501.

17. The Return for the year of assessment 2006/07 was accepted as correct but an adjustment was made to disallow the commercial building allowance over claimed. On 22 February 2008, a notice of additional assessment for the year of assessment 2006/07 and notice of payment of provisional tax for 2007/08 was issued to the appellant as follows:

	<u>2006/07</u>	<u>2007/08</u>	<u>Total tax payable</u>
	(Final)	(Provisional)	
Profit per Return	\$3,602,501	\$3,602,501	
<u>Add: Commercial Building Allowance</u> over claimed (\$198,333 - \$21,363)	<u>\$176,970</u>	<u>\$176,970</u>	
	\$3,779,471	\$3,779,471	
<u>Less: Profit already assessed</u>	<u>\$3,200,000</u>	<u>\$3,200,000</u>	
Additional profit	\$579,471	\$579,471	
Tax payable	<u>\$101,407</u>	<u>\$101,407</u>	<u>\$202,814</u>

The appellant has not lodged an objection against the additional assessment.

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

19. On 1 August 2008, the Commissioner of Inland Revenue ('the Commissioner') issued the notice of intention to assess additional tax under section 82A of the Ordinance ('the Notice') to the appellant in respect of its failure to file the Return for the year of assessment

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2006/07 by the due date and invited the company to make written representations. The Notice also stated that the penalty may be up to 3 times the amount of tax that would have been undercharged if the Department had not detected the failure. The tax which would have been undercharged if the failure had not been detected is an amount of \$661,407.

20. In response to the Notice, CPA, on 12 August 2008, submitted representations on behalf of the appellant.

21. On 8 September 2008 the Commissioner, having considered the representations, assessed the appellant to additional tax by way of penalty under section 82A of the Ordinance in the amount of \$30,000.

22. By a letter dated 26 September 2008, the appellant filed a notice of appeal to the Board of Review against the assessment of additional tax by way of penalty.

23. The appellant's previous failures in filing Profits Tax Returns are shown as follows:

Year of assessment	<u>2004/05</u>	<u>2005/06</u>
Date of issue of Return	1 April 2005	3 April 2006
Due date / extended due date for filing Return	15 November 2005	22 November 2006
Date of receipt of Return	21 November 2005	29 November 2006
Period of delay in filing Return	6 days	7 days
Tax undercharged	\$242,874	\$507,880

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 2004/05 and 2005/06.

The grounds of appeal

25. The notice of appeal reads as follows (written exactly as it stands in the original):

'In reference to the above penalty of HK\$30,000.00, we would like to object to this penalty imposed on our company.

Our company has consistently maintained a good tax payment record and we are constantly improving our sales volume and revenue.

Due to the extreme pressure in meeting client's projects and delivery deadlines we have had to hire additional temporary staff to cope with our increasing sales.

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Between September & November 2007 we were under-staffed and did not have any time to train new staff. Therefore we put advertisements in January and February of this year to recruit new staff without any suitable candidates.

The directors have, therefore, had to work longer hours to cope with the increasing sales and surging number of new enquiries.

The directors have also had to make some overseas trips to promote and increase the sales volume.

In lieu of the above explanation, we respectfully request that you review our case and waive the HK\$30,000.00 penalty.

We assure you that we shall file our future taxes promptly without any further delays.

We await your reply.

Thank you.'

Relevant provisions of the Ordinance

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 ... profits tax ...'

27. Section 51C(1) provides that:

'Subject to subsection (2)¹, every person carrying on a trade, profession or business in Hong Kong shall keep sufficient records in the English or Chinese language of his income and expenditure to enable the assessable profits of such trade, profession or business to be readily ascertained and shall retain such records for a period of not less than 7 years after the completion of the transactions, acts or operations to which they relate.'

28. Sections 68(4), (8)(a) & (9) provide that:

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

¹ Sub-section (2) is not relevant in this case.

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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 I of Schedule 5, which shall be added to the tax charged and recovered therewith.*’

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

29. Section 82A(1)(d), so far as relevant, provides that:

‘(1) *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 –

(i) *...*

(ii) *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.*’

30. Section 82B, so far as relevant, provides that:

‘(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.*’

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(3) *Sections 66(2) and (3), 68, 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.*

The Board's Decision

31. It is clear from the notice of appeal that the only issue in this appeal is the amount of the penalty. In any event, we do not think there is any reasonable excuse for the failure to report within the extended time limit.

32. The amount of tax which would be undercharged had the failure to comply not been detected is \$661,407.

33. The maximum amount of penalty under section 82A is $\$661,407 \times 3 = \$1,984,221$.

34. The penalty of \$30,000 is 4.5% of \$661,407.

35. The appellant's audited financial statements for the year ended 31 March 2007 and the 3 preceding years showed the following:

	<u>Year ended 31</u> <u>March 2004</u>	<u>Year ended 31</u> <u>March 2005</u>	<u>Year ended 31</u> <u>March 2006</u>	<u>Year ended 31</u> <u>March 2007</u>
	\$	\$	\$	\$
Turnover	22,774,973	21,617,084	32,621,055	50,649,846
Staff costs	1,935,170	2,052,773	2,308,952	3,046,898

36. The Return was issued on 2 April 2007. The extended deadline was 15 November 2007. The appellant had nearly 7 ½ months to furnish its profits tax return. No taxpayer is allowed to point to its own breach of section 51C as a mitigating factor in respect of penalty tax. In our Decision, bearing in mind the appellant's statutory duty under section 51C, 7 ½ months should have been ample if the appellant had treated its statutory reporting duties with the seriousness they deserved.

37. The appellant's representative, a director of the appellant, testified that it did not have a full-time book-keeper. Whether to employ a full-time book-keeper was and is a matter of choice for the appellant. Choosing not to employ a full-time book-keeper is an aggravating factor, not a mitigating factor, in considering the amount of penalty tax. The appellant is not a small company as the representative would have us believed. It had low to mid 8-digit turnovers for 4 successive years of assessment, charging \$1,900,000 to \$3,000,000 staff costs in its accounts.

38. By reason of its default, the Revenue had incurred administrative costs in the issue on 29 November 2007 of the estimated profits tax assessment, estimating profits at \$3,200,000, see

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paragraph 13 above. We infer from the fact that the appellant did not object to it, within the 1-month time limit for objection or at all, that it knew that its assessable profits exceeded the amount of \$3,200,000. Yet it took its time and did not submit the Return until 21 January 2008 reporting assessable profits of \$3,602,501. The Revenue had to incur administrative costs in issuing an additional profits tax assessment on 22 February 2008.

39. The appellant's representative said the directors had other things to attend to. Statutory duties are to be complied with. Compliance does not depend on the pleasure or leisure of the taxpayers or their directors.

40 The Board has said time and again that it is the duty of taxpayers to regulate its own affairs in such a way so as to comply with the requirements of the Ordinance. There are ample examples of the Board's consistent approach, see:

- (1) D25/97 (Robert Wei Wen Nam SC, Arthur Chan Ka Pui and Peter R Griffiths), IRBRD, vol 12, 204, at paragraphs 11.1, 11.3 and 11.4 and the cases there cited;
- (2) D134/00 (Kenneth Kwok Hing Wai SC, Philip Kan Siu Lun and Adrian Wong Koon Man), IRBRD, vol 16, 10, at paragraph 32; and
- (3) D57/06 (Kenneth Kwok Hing Wai SC, Ip Tak Keung and Horace Wong Yuk Lun SC), (2006-07) IRBRD, vol 21, 1061, at paragraph 13.

41. An important factor in the consideration of the amount of penalty is the extent to which, if at all, the taxpayer has taken steps to put its house in order. The appellant's attitude and approach are far from re-assuring. What the appellant's representative said at the hearing was that (written exactly as it was said):

' ... I oppose on the tax because I felt that it was too much and I didn't want to pay the penalty. I oppose to the penalty because I felt, yes, I have delayed, but I still paid the tax on time and I wanted you to waive the charges.

...

We don't have an in-house bookkeeper who will be working in our office the whole day so they come and do the books, and now we are planning to change our bookkeeper for another auditor, a bookkeeper who can do it on a more regular basis starting this year ... So, taking that into consideration and I love to pay tax but I hate to pay penalty. If possible, I would like to avoid it.

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So, instead of paying a penalty, I am trying to change my bookkeeper, which we are in the process, hoping that we could pay it on time and have less problems, you know. I mean I can concentrate on other things. Today, going through all this, it does take the time of Inland Revenue. It does take some of my time and my company's time, so it does have a lot of time, which I could use it for my business. But I have to do everything, even this is important, I can't ignore it.'

42. Penalty tax is imposed by the decision maker under the Ordinance. It does not depend on the pleasure or agreement of the defaulting taxpayer.

43. In our decision, the penalty of 4.5% of the amount of tax involved is by no means incorrect or excessive in the circumstances of this case.

44. It follows that the appeal must be dismissed.

Disposition and costs

45. We dismiss the appeal and confirm the Assessment.

46. We are of the opinion that this is a wholly unmeritorious appeal which should never have been pursued, despite having had the previous decisions of the Board drawn to its attention. We see no reason why the upstanding and compliant taxpayers should bear the costs of this appeal.

47. Pursuant to sections 82B(3) and 68(9), we order the appellant to pay the sum of \$5,000 as costs of the Board, which \$5,000 shall be added to the Assessment of \$30,000.