HCIA 1/2017
[2018] HKCFI 2593

IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
COURT OF FIRST INSTANCE
HIGH COURT INLAND REVENUE APPEAL NO 1 OF 2017
(on appeal from Board of Review Cases No. B/R 16/13 and B/R 17/13)

_____

BETWEEN

KOO MING KOWN — 1st Applicant
MURAKAMI TADAO — 2nd Applicant

and

THE COMMISSIONER OF INLAND REVENUE — Respondent

_____

Before: Hon G Lam J in Court
Dates of Hearing: 18-19 April 2018
Date of Judgment: 23 November 2018

_____

J U D G M E N T

_____

A. Introduction

1. This is an appeal by the appellants, Mr Koo and Mr Murakami, against two decisions ("**Decisions**") of the Inland Revenue Board of Review ("**Board**") in ***D32/16*** and ***D33/16*** respectively[1] on points of law under s 69 of the Inland Revenue Ordinance (Cap 112) ("**Ordinance**"). References to Parts and sections below are to the Ordinance.

2. The Decisions concern the assessments to additional tax raised by the Commissioner of Inland Revenue ("**Commissioner**") under s 82A against the appellants for incorrect statements made in the tax returns of Nam Tai Trading Company Limited, formerly called Nam Tai Electronics & Electrical Products Limited ("**NT Trading**").[2] *D32/16* was Mr Koo's appeal and *D33/16* Mr Murakami's. References below to numbered paragraphs of a Decision are to the Decision in *D32/16*.

B. Factual background

3. I only outline the facts briefly here as the details were agreed and set out in the statement of agreed facts before the Board which is appended to this judgment.

[1] Cases No. B/R 16/13 and B/R 17/13
[2] Abbreviated to "**NTEE**" in some other documents including the Decisions.

4. The appellants were directors of NT Trading. In its tax returns (which attached relevant accounts), NT Trading claimed it had incurred certain expenses, principally management fees paid to its parent company, Nam Tai Electronics, Inc ("**NTEI**"), and deducted them in arriving at the assessable profits. Profits tax assessments were made in 1996/97, 1997/98 and 1998/99 on the basis of these returns and were paid. In 2002, after a tax audit, an assessor of the Inland Revenue Department ("**IRD**") decided to apply ss 16, 17, 61 and 61A to disallow those expenses and raised on NT Trading additional profits tax assessments for the three years of 1996/97 to 1998/99 and profits tax assessment for the year 1999/2000.

5. Following objections raised by NT Trading, the Deputy Commissioner revised or confirmed the assessments (as the case may be). As stated in §16 of the statement of agreed facts, the Deputy Commissioner decided that the fees were not deductible under ss 16 and 17 and further determined that s 61A was applicable. Dissatisfied with the result, NT Trading appealed to the Board (**D41/08**).

6. On 9 December 2008, the Board dismissed the appeal. Further steps taken by NT Trading to challenge the assessments and the Board's decision in *D41/08* were unsuccessful.

7. NT Trading did not pay the tax payable pursuant to the additional assessments for 1996/97 to 1998/99 and the assessment for 1999/2000. On 4 June 2012, NT Trading was wound up by the court on the petition of the Commissioner.

8. Meanwhile, in January 2011, the Commissioner took steps to invoke s 82A(1)(a) against both appellants herein, alleging that they had made incorrect returns by understating NT Trading's assessable profits. The procedure culminated in the assessments to additional tax in question which were issued in April 2013. The assessments against Mr Koo in relation to the years 1996/97 and 1999/2000 were in the amount of $6,400,000 and $6,200,000 respectively and that against Mr Murakami in relation to the year 1997/98 was in the amount of $5,400,000. Essentially, each of them was said to be liable to be assessed to additional tax on the ground that, having signed the tax returns of NT Trading for the relevant year as a director, he had made an incorrect return on behalf of NT Trading within the meaning of s 82A. The incorrectness was said to be the understatement of assessable profits by reason of the deduction of the relevant fees. (NT Trading's tax return for 1998/99 was signed by one Francis Li, the financial controller, who was not assessed to additional tax.)

9. The appellants appealed to the Board against the assessments to additional tax but the appeals backfired as the overall amounts payable were *increased* by the Board. In January 2017, the Board (differently constituted from *D41/08*) issued its Decisions dismissing the appeals and revising the amounts of additional tax, concluding that: (i) each of the appellants did make a return on behalf of NT Trading within the meaning of s 82A(1)(a); (ii) they also gave incorrect information within the meaning of s 82A(1)(c); (iii) the appellants were bound by the Board's decision in *D41/08* as regards the amounts of assessable profits and thus precluded from contending that the returns were not "incorrect"; (iv) the appellants failed to establish any "reasonable excuse"; and (v) the

quantum of penalty on them should respectively be 140% and 90% of the amount of tax undercharged, in addition to compound interest with monthly rests.

10. The relevant figures in the assessments and additional tax assessments are set out in the table below:

Year		**1996/97**	**1997/98**	**1999/2000**
Assessment against NT Trading				
Assessable profits / (loss) per NT Trading's return		$9,889,250	$8,667,488	($3,803,183)
Tax originally assessed		$1,631,726	$1,287,121	-
Assessable profits as determined by Deputy Commissioner and, on appeal, by the Board in *D41/08*		$46,632,080	$43,458,129	$36,694,629
Assessable profits understated		$36,742,830	$34,790,641	$36,694,629
Tax undercharged in original assessment		$6,062,567	$5,166,411	$5,871,140
Additional tax assessed by the Commissioner against the Appellants				
Person assessed to additional tax		**Mr Koo**	**Mr Murakami**	**Mr Koo**
Additional tax assessed by Commissioner	Amount	$6,400,000	$5,400,000	$6,200,000
	As percentage of tax undercharged	105.57%	104.52%	105.60%
Additional tax determined by the Board against the Appellants				
Additional tax assessed by Board	Amount	$8,487,593	$4,649,769	$8,219,596
	As percentage of tax undercharged	140%	90%	140%
	Interest	$2,683,170	$2,041,295	$2,405,875
	Total amount	$11,170,763	$6,691,064	$10,625,471
	Total amount as percentage of tax undercharged	184.26%	129.51%	180.98%

11. With leave given by this court, the appellants now appeal under s 69 on grounds involving questions of law.

C. The key provisions on additional tax

12. Assessment to additional tax is governed by s 82A which provides:[3]

> "(1) Any person who without reasonable excuse—
>
> (a) makes an incorrect return by omitting or understating anything in respect of which he is required by this Ordinance to make a return, either on his behalf or on behalf of another person; or
>
> (b) makes an incorrect statement in connection with a claim for any deduction or allowance under this Ordinance; or
>
> (c) gives any incorrect information in relation to any matter or thing affecting his own liability (or the liability of any other person) to tax; or
>
> (d) fails to comply with the requirements of a notice given to him under section 51(1) or (2A); or
>
> (e) fails to comply with section 51(2),
>
> 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) has been undercharged in consequence of such incorrect return, statement or information, or would have been so undercharged if the return, statement or information had been accepted as correct; or
>
> (ii) has been undercharged in consequence of the failure to comply with a notice under section 51(1) or (2A) or a failure to comply with section 51(2), or which would have been undercharged if such failure had not been detected.
>
> (2) Additional tax shall be payable in addition to any amount of tax payable under an assessment, or an additional assessment under section 60.

[3] The version set out here is the version as at 2017 which includes certain amendments made after the relevant years and excludes the amendments made in 2018 but nothing turns on these amendments.

(3) An assessment of additional tax may be made only by the Commissioner personally or a deputy commissioner personally.

(4) Before making an assessment of additional tax the Commissioner or a deputy commissioner, as the case may be, shall—

(a) cause notice to be given to the person he proposes so to assess …

(b) consider and take into account any representations which he may receive under paragraph (a) from or on behalf of a person proposed to be assessed for additional tax.

…

(7) A person who has been assessed to additional tax under subsection (1) shall not be liable to be charged on the same facts with an offence under section 80(2) or 82(1).

…"

13. Appeals against assessment to additional tax are provided for by s 82B which stipulates:

"(1) Any person who has been assessed to additional tax under section 82A may within—

(a) 1 month after the notice of assessment is given to him; or

(b) such further period as the Board of Review may allow under subsection (1A),

either himself or by his authorized representative give notice of appeal to the Board; but no such notice shall be entertained unless it is given in writing to the clerk to the Board and is accompanied by—

(i) a copy of the notice of assessment;

(ii) a statement of the grounds of appeal from the assessment;

(iii) a copy of the notice of intention to assess additional tax given under section 82A(4), if any such notice was given; and

(iv) a copy of any written representations made under section 82A(4).

(1A) If the Board is satisfied that an appellant was prevented by illness or

absence from Hong Kong or other reasonable cause from giving notice of appeal in accordance with subsection (1)(a), the Board may extend for such period as it thinks fit the time within which notice of appeal may be given under subsection (1). …

(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.

(3) Sections 66(2) and (3), 68, 68AA, 68AAB, 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."

D. The questions of law

14. The questions in respect of which leave to appeal was given may be summarised as follows:

(1) Question 1

(a) Does s 82A permit a penalty assessment to be made upon an agent of a corporate taxpayer who assists the taxpayer to make a tax return?

(b) If so, do ss 70 and 82B(3) preclude the agent from (i) re-opening questions of the taxpayer's liabilities to all or part of the profits tax; and (ii) challenging the assertion that the taxpayer's return was "incorrect"?

(c) If so, did the Board's decision in *D41/08* conclusively determine that the statements in the taxpayer's returns were "incorrect"?

(2) Question 2

(a) Is an agent's subjective belief in the correctness of the content of the taxpayer's return capable of constituting a "reasonable excuse" for mis-statements therein?

(b) Is the conduct of an agent, in signing a taxpayer's return in reasonable reliance upon his belief that the views of the taxpayer's accounting staff or officers and/or professional advisers, such as its auditors or tax advisers, that the contents of the taxpayer's returns are correct, capable of constituting "reasonable excuse" for mis-statements therein?

(c) If the answer to (a) or (b) is "yes", do the findings of fact made by the Board in its decisions require the conclusion in law that the appellants had shown "reasonable excuse" for any incorrectness in the taxpayer's returns?

(3) Question 3

(a) Is the Board entitled to adopt and to rely upon a statement of the administrative policy of the Inland Revenue Department which fails to distinguish between the penalties/additional tax that is appropriate for misstatements in a taxpayer's return (which are liable to prosecution under section 80) and tax evasion or other tax fraud (which is liable to prosecution under section 82) when determining the correct amount of the penalty/additional tax?[4]

15. The arguments raised in connection with these questions will be dealt with in turn below.

E. Question 1(a) — construction of s 82A(1)(a)

E1. The issue

16. Question 1(a) as formulated, referring as it does to "an agent" who "assists" the taxpayer to make a tax return, seems to me to be unnecessarily wide and inexact. We are in this case concerned with directors who signed the company's tax returns, and attention should be focused on this setting. In essence two elements in s 82A(1)(a) are called into question: (i) did each of the appellants as a director who signed the company's return "make" the return, and (ii) were the assessable profits stated in each return something in respect of which the relevant appellant was "required" by the Ordinance to "make" a return on behalf of NT Trading?

17. The appellants' case is that for the purposes of s 82A(1)(a), it was NT Trading and NT Trading alone who made the return and that, assuming for present purposes the return was incorrect, it was incorrect by understating NT Trading's assessable profits in respect of which NT Trading was required by the Ordinance to make a return on its own behalf. The Commissioner takes issue in both aspects, contending that

[4] There was initially a Question 3(b) which was subsequently not pursued by the appellants.

the appellants made the returns because they signed them, and that they were required by virtue of s 57 to make those returns on behalf of NT Trading.

18. The question is one of construction of s 82A(1)(a). In *Chu Ru Ying v Commissioner of Inland Revenue* [2010] 2 HKLRD 1052 it was common ground that s 82A involved a criminal charge for human rights purposes (see §30). That was also the conclusion of the Board in *D17/08* (2008) 23 IRBRD 301, §§169-170. But regardless of whether it involves a criminal charge attracting the application of article 11 of the Hong Kong Bill of Rights, there is no doubt that additional tax is a penalty. The general principle against doubtful penalisation must therefore be borne in mind in the construction of the statute: *T v Commissioner of Police* (2014) 17 HKCFAR 593, §§196 & 261 *per* Fok PJ; *Commissioner of Police v Privacy Commissioner for Personal Data* [2012] 3 HKLRD 710, §§18 & 37 *per* Kwan JA; *Ricketts v Ad Valorem Factors Ltd* [2004] 1 BCLC 1 at §30; *ESS Production Ltd (in administration) v Sully* [2005] 2 BCLC 547 at §71.

19. It should also be noted that s 82A(1)(a)-(e) is identical to s 80(2)(a)-(e), a parallel but alternative provision under which the same conduct constitutes an offence punishable with a fine at level 3 and a further fine of treble the amount of tax undercharged. Construing s 82A(1)(a) would therefore for all intents and purposes also determine the scope of s 80(2)(a).

20. The Commissioner's construction has serious ramifications. It would mean that whenever there was material incorrectness in a company's tax return, the person who signed it, at least where he is a director, manager, secretary or liquidator, could be subjected to an administrative penalty plus compound interest up to treble the amount of tax undercharged, unless he established a reasonable excuse.

21. There have been many cases concerning additional tax imposed on the taxpayer, including corporate taxpayer. There is, however, no previous case that actually decided the point about assessing a third party such as a director to additional tax for incorrectness in the company's return. There are two decisions of the Board (*D47/90* and *D46/01*) that upheld assessments to additional tax against directors arising out of incorrect returns of the company, but in neither of them was the point argued, nor did the decisions contain any analysis of s 82A(1)(a) relevant for present purposes.

E2. History

22. The history of ss 82A and 82B was set out in *D17/08* (2008) 23 IRBRD 301, at §135 onwards. They arose from the proposals of the Commissioner and the recommendations of the Inland Revenue Ordinance Review Committee which considered those proposals and reported in 1968. Their report stated:

> "397. The Commissioner felt there was need for an alternative to Court action which would authorize him to impose penalties for most offences except those of wilful intent to evade tax. He pointed out that it would save the taxpayer's time as well as an unpleasant appearance in Court and would also save the time spent by officials

> of the Inland Revenue Department, the Legal Department, and the Court on the preparation and hearing of comparatively minor cases. He agreed that he had the power to compound offences, and this worked reasonably well in routine offences such as failing to lodge returns by due date. However, he had found difficulty in convincing a person who has understated his income that he should pay a penalty in addition to the additional tax payable by assessment. Where an offender is unwilling to compound his offence, the only alternative available to the Department is to prepare a case for prosecution in Court for an offence under either Section 80(2) or Section 82(1).
>
> 398. The Commissioner submitted that where any person has been undercharged to tax as a consequence of any incorrect return, statement or information made or given to the Department, or where he would have been undercharged if the return, etc. had been accepted, it would be reasonable to empower the Department to impose a penalty, up to the amount of the tax undercharged, according to the acceptability of the excuse offered by the offender: similar powers are to be found in the tax laws of other territories, including South Africa, Australia, Malaysia and Singapore. …"

23. The Review Committee, being in general agreement with providing an administrative penalty as an alternative to court proceedings for at least certain offences which were punishable under Part 14, made recommendations which led to the enactment of ss 82A and 82B in 1969, with s 82A(1)(a)-(e) tracking the language of the pre-existing s 80(2)(a)-(e). The maximum amount of the administrative penalty at that time was the amount of the tax undercharged. An amendment trebled it in 1975.

24. It is fair to say that from the legislative materials there does not appear to have been any discussion of the liabilities of corporate officers to the penalty for signing on companies' incorrect returns. Instead, the explanatory memorandum to the Inland Revenue (Amendment) Bill 1969 stated as follows:

> "Clause 38 adds two new sections which would enable the Commissioner or deputy commissioner personally to impose additional tax <u>where the taxpayer</u> without reasonable excuse has acted in breach of section 80(2) by omitting an amount from or understating an amount in a return, or making an incorrect statement in connexion with a claim for a deduction or an allowance, or giving incorrect information in relation to any matter affecting his liability. Additional tax may be imposed up to an amount not exceeding the amount of tax undercharged in consequence of the incorrect return, statement or information.
>
> Before making an assessment to additional tax, <u>notice will be given to the taxpayer</u> and he will have the right to make written representations which the Commissioner or deputy commissioner must take into

account. …" (emphasis added)

25. The focus at the time was no doubt on imposing the penalty on the taxpayer himself. From that point of view the label "additional tax" may be considered apt since the amount payable — even though in truth a penalty rather than a tax — is additional to what the taxpayer has to pay as tax.

E3. Statutory framework

26. Both s 80(2) and s 82A(1) concern returns and information provided to the IRD. The primary provisions on the furnishing of returns and information are found in Part 9 (ss 51-58). S 51(2) requires every person chargeable to tax to inform the Commissioner of that fact (unless he has already been required to furnish a return under s 51(1)).

27. S 51(1) — the general empowering provision for requiring returns — provides:

> "(1) 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—
>
> (a) property tax, salaries tax or profits tax; or
>
> (b) property tax, salaries tax and profits tax,
>
> under Parts 2, 3, 4, 10A, 10B, and 10C."

In the case of companies which may be chargeable to profits tax, this is done by the IRD sending them blank profits tax returns with a requirement printed thereon.[5]

28. S 51(3) empowers an assessor by notice to require any person to furnish "fuller or further returns" in respect of any matter of which a return is required or prescribed.

29. S 51(4), (4AA), (4A) and (4B) empower an assessor by notice to require any person (including a person's employee) to furnish "full information" in regard to any matter which may affect the tax liabilities of that person.

30. S 51(5) provides for two rebuttable presumptions, one as to authority and the other as to knowledge, as follows:

> "A return, statement, or form purporting to be furnished under this Ordinance by or on behalf of any person shall for all purposes be deemed

[5] S 51AA(1) now stipulates that a return required to be furnished under s 51(1) must be in a form specified by the Board of Inland Revenue and provided by the Commissioner, but this was only enacted in 2003.

> to have been furnished by that person or by his authority, as the case may be, unless the contrary is proved, and any person signing any such return, statement, or form shall be deemed to be cognizant of all matters therein."

31. Under s 51A, where the Commissioner considers that a person has "made an incorrect return" or supplied false information understating his income or profits without reasonable excuse, Commissioner may by notice, with the consent of the Board, require him to furnish a statement of all assets, liabilities, expenditure or disbursements and all sums received.

32. S 51B deals with search warrants issued by a magistrate on the application of the IRD. Subsection (1)(a) provides that a search warrant may be granted where there are reasonable grounds for suspecting that a person has "made an incorrect return" or supplied false information understating his income or profits without reasonable excuse.

33. S 52(2)-(8) deal with the returns that an employer is required to furnish.

34. S 53, concerning incapacitated or non-resident persons, provides:

> "An act or thing required by or under this Ordinance to be done by any person shall, if such person is an incapacitated or non-resident person, be deemed to be required to be done by the trustee of such incapacitated person or by the agent of such non-resident person, as the case may be."

So far as non-resident persons are concerned, this is to be read together with s 20A(1), which provides that a non-resident person is chargeable to tax either directly or in the name of his agent.

35. S 54 deals with the position of an executor of a deceased taxpayer. He is chargeable with the tax for all periods prior to the deceased's death with which the deceased would be chargeable if he were alive, and liable to do all the things the deceased would be liable to do under the Ordinance if he were alive. It is specifically provided that no proceedings, other than an assessment to additional tax under s 82A, may be instituted against the executor under Part 14 (Penalties and Offences) in respect of any act or default of the deceased person.

36. S 56 states that the precedent partner of a partnership is answerable for doing all such things as would be required to be done by an individual. This is to be read together with s 22 which deals with assessment of partnerships. S 22(1) provides that tax is charged in the partnership name. S 22(2) specifically states that the precedent partner "shall" make and deliver a statement of the profits or losses "on behalf of the partnership", and that where no active partner is resident in Hong Kong, the return shall be furnished by the manager or agent of the partnership in Hong Kong.

37. S 56A states that any joint owner is answerable for doing all such things as would be required to be done by a sole owner.

38. S 57(1), which is heavily relied upon by the Commissioner in this case, provides:

> "The secretary, manager, any director or the liquidator of a corporation and the principal officer of a body of persons shall be answerable for doing all such acts, matters, or things as are required to be done under the provisions of this Ordinance by such corporation or body of persons."[6]

39. Part 10 (ss 59–63) governs assessments. Where a return is furnished, the assessor may accept the return and make an assessment accordingly (s 59(2)(a)). If a person does not furnish a return, the assessor may make an estimated assessment (s 59(3)). S 61 deals with artificial or fictitious transactions and dispositions that may be disregarded, and s 61A deals with tax avoidance transactions.

40. Part 11 (ss 64-70B) provides for objections and appeals against assessments. S 64 enables objections to be made to the Commissioner and empowers the Commissioner to confirm, reduce, increase or annul the assessment objected to. S 66 provides for a right of appeal to the Board, and s 69 provides for an appeal from the Board to the Court of First Instance on points of law (previously, by way of case stated, and now, with leave of the court). S 70, quoted in full in §68 below, provides that in specified circumstances the assessment as made or agreed to or determined on objection or appeal shall be final and conclusive for all purposes of the Ordinance as regards the amount of assessable income or profits or net assessable value. S 70A provides for a power for an assessor to correct errors or omissions.

41. Part 14 (ss 80-84) makes provisions for penalties and offences. S 80 creates offences and penalties for failure to make returns, making incorrect returns and the like. As explained above, s 82A provides an alternative regime for imposing administrative penalties on persons liable to prosecution under s 80(2). S 82 creates offences, punishable by imprisonment, for tax evasion and other tax frauds. To be liable under s 82 a person must have done the act or omission in question "wilfully with intent to evade or to assist any other person to evade tax".

E4. The person who made the return

42. In the present case, the profits tax return forms — the "notice in writing" under s 51(1) — were issued by the IRD to NT Trading. Although s 51AA had not been enacted at the time, there is no doubt that these forms were specified by the Board of Inland Revenue exercising its power under s 86, as contemplated in s 51(1) itself. The notices, issued in the name of an Assistant Commissioner, stated at the outset:

"TO NAM TAI ELECTRONIC & ELECTRICAL PRODUCTS LTD

[6] This subsection has since been replaced by a new version (see Ordinance No. 16 of 2016, s 26) but the amendment is immaterial for present purposes.

> [address]
>
> By virtue of Section 51(1) of the Inland Revenue Ordinance (Cap. 112) you are required to make on this form a true and correct return of the Assessable Profits (or Adjusted Loss) arising during the basis period … For the year of assessment ended 31 March [year]. The information provided will be used for purposes relating to the administration of the Ordinance.
>
> All sections of this form MUST be completed and returned to me WITHIN ONE MONTH from the date of this Notice, … together with a certified copy of your Balance Sheet, Auditor's Report, and Profit and Loss Account in respect of the basis period, and a tax computation with supporting schedules, showing how the amount of Assessable Profits (or Adjusted Loss) has been arrived at."[7] (emphasis added)

43. At the end of each notice there was a box for a declaration to be made in these terms:

> " I, …… (full name), being SECRETARY / MANAGER / DIRECTOR / LIQUIDATOR* of …… (full name of the Corporation), declare that to the best of my knowledge and belief all the statements contained in this return are true, correct and complete and I have disclosed the whole of the Assessable Profits (or Adjusted Loss) of the Corporation arising during the basis period for the year of assessment ended 31 March as stated in the formal notice in Page 1.
>
> Signature …….....
>
> (Heavy penalties may be incurred for failing to keep sufficient business records, making an incorrect return or committing other offences — See Notes 8 and 9.)
>
> Date …….....
>
> *Delete whichever is inapplicable."

44. This box was signed by Mr Koo in the return for 1996/97 and 1999/2000 and by Mr Murakami in the return for 1997/98, in each case as a director.

45. There is no general requirement under s 51 or indeed elsewhere in the Ordinance to make a return until an assessor by notice under s 51(1) requires it. The obligation of a person chargeable to tax is to inform the Commissioner of that fact:

[7] The form for the year 1999/2000 contained modifications on the supporting documents to be submitted by a "small corporation".

s 51(2). Under s 51(1) and the notices issued, it was NT Trading that was being required to make a return. It is common ground that NT Trading did make a return as required.

46. Being a company, NT Trading could of course only furnish a return through acts of natural persons. Physical acts were necessary to achieve it: someone had to use a typewriter or a pen to fill in the form, someone had to sign in the box and someone had to post or deliver the completed form to the IRD. But it does not follow that these individuals, or one or a combination of them, or the board of directors who authorised or instructed them, *made* the return. Making or furnishing a return is a legal act capable of being said to have been done directly by a company albeit through physical steps undertaken by human beings.

47. More generally, it is not always accurate or appropriate to say that the individual who does an act in the name of a company is an "agent" acting "on behalf of" the company. Sometimes the act is properly ascribed directly to the company without any separate identity attributed to the individual concerned. As Lord Reid stated in *Tesco Supermarkets Ltd v Nattrass* [1972] AC 153 at 170E-G, in a somewhat different context:

> "I must start by considering the nature of the personality which by a fiction the law attributes to a corporation. A living person has a mind which can have knowledge or intention or be negligent and he has hands to carry out his intentions. A corporation has none of these: it must act through living persons, though not always one or the same person. Then the person who acts is not speaking or acting for the company. He is acting as the company and his mind which directs his acts is the mind of the company. There is no question of the company being vicariously liable. He is not acting as a servant, representative, agent or delegate. He is an embodiment of the company or, one could say, he hears and speaks through the persona of the company, within his appropriate sphere, and his mind is the mind of the company. If it is a guilty mind then that guilt is the guilt of the company. It must be a question of law whether, once the facts have been ascertained, a person in doing particular things is to be regarded as the company or merely as the company's servant or agent. In that case any liability of the company can only be a statutory or vicarious liability." (emphasis added)

48. As a consequence of the doctrine of the separate legal personality of a company, where an act is done by an officer in the company's name, the law does not automatically without careful consideration make the individual officer liable together with the company for the consequences of the act.

49. In my opinion, whether this is the correct way to approach s 82A(1)(a) is, by analogy with the principles established in relation to special rules of attribution, not a question of metaphysics but one of construction of the substantive rule having regard to its language (if it is a statute) and its content and policy: *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 AC 500, 507F.

50. The requirement to furnish or make a return stems from s 51(1). There is to my mind no significant difference between the terms "furnish" and "make" in this context: s 51(1) uses the former whereas the notices issued under that provision used the latter. It is clear that the power of the assessor under s 51(1) to require a return to be furnished was exercised against NT Trading and no one else. It was NT Trading who was issued a notice and required by that notice to furnish the return on the form sent to it. If no return was furnished, it would be NT Trading who would be liable under s 82A(1)(d) for "fail[ing] to comply with the requirements of a notice given to him under s 51(1)". It is true that the appellants signed a declaration at the end of the form, but it does not follow that they made the return on behalf of the company. Relying on *Dutton v Marsh* (1871) LR 6 QB 361, a case about a promissory note held to have been made by four directors personally, Mr Wong submitted that the appellants signed in their own separate capacity as directors, and not only as the company. With respect, such bills of exchange cases do not provide assistance here. The context is far removed from liability for incorrect tax returns, the question is purely one of construction of the bill itself, and depending on its construction the liability on the bill is either the director's personally or the company's but not both.

51. I am unable to discern any clear legislative intention that in addition to the corporate taxpayer who undoubtedly made a return, the individual who signed it should also liable to a penalty for making an incorrect return on behalf of the company. It seems to me to strain the language to characterise a single return as having been "made" by two separate persons: both by the company on its own behalf and by the signing officer on behalf of the company.

E5. Required to make a return on behalf of another person

52. Further, under s 82A(1)(a) the matter omitted or understated must be something in respect of which the person is *required* by the Ordinance to make a return, either on his behalf or on behalf of another person. As specified in the s 51(1) notices, it was NT Trading who was required to make a return of its assessable profits. The Commissioner submitted however that, by virtue of s 57(1) (quoted in §38 above), the appellants were also *required* to make the returns *on behalf of* NT Trading.

53. S 57(1) is a provision of considerable vintage, traceable back to at least the (UK) Income Tax Act 1803 (s 88), but its precise effects are not entirely clear. Nor is the word "manager" defined. In *D69/97*, the Board stated (at §37) that under that subsection, the directors are "collectively and singly answerable for carrying out the company's obligations imposed by the [Ordinance]".

54. I am unable to accept that s 57(1) has the effect the Commissioner contends for. Its language makes clear that under that provision the things in question are still *required* to be done *by the corporation*. S 57(1) provides that the secretary, manager, any director or the liquidator of the corporation shall be *answerable* for doing those things. The case of *Income Tax Commissioner v Chatani* [1983] STC 477 suggests that the effect of s 57(1) is that the class of persons specified are to be "responsible" for taking all administrative or ministerial action for the things which under the Ordinance are required

to be done by the corporation.[8] I accept the appellants' submission that being made answerable thus is not equivalent to being required to *make a return on behalf of another person* for the purposes of s 82A(1)(a).

55. Where the Ordinance empowers the assessor to require a person to furnish a return or information on behalf of another, it does so in explicit and clear terms. There are instances in the Ordinance where, as contemplated by s 82A(1)(a), a person is expressly required to make a return on behalf of another person: for example, trustees[9] of incapacitated persons[10] (s 53), agents[11] of non-resident persons (ss 20A and 53)[12], a precedent partner making a return of the profit or loss on behalf of the partnership (ss 22(2) and 56), and the agent or manager of a partnership where no active partner resides in Hong Kong (s 22(2)). The appellants' construction does not render the phrase "or on behalf of another person" in s 82A(1)(a) meaningless.

56. The Commissioner relied on *Lean v Brady* (1937) 58 CLR 328 where it was said (by Starke J at p 332) that many duties were cast upon the public officer of a company under the Income Tax (Management) Act 1928, such as making returns, giving information and so forth (see also p 336 *per* Dixon J). But the statute there was in materially different terms. S 78 of the Act stated that every company with an income should appoint and be represented by a person called the "public officer", and s 78(e) provided that:

> "the public officer shall be liable for the doing of all such things as are required to be done by or on behalf of the company under this Act or the regulations in force thereunder, and in the case of default in doing any of such things, shall be liable for all penalties imposed for any breach of the provisions of this Act or such regulations, and the company, as well as such public officer, shall also be liable for such penalties."

There was a single officer appointed for the purposes of the Act who was clearly and expressly made liable for penalties in the case of default. Given the very substantial difference between the legislation, I do not think the case assists the Commissioner. It may be noted that the Income Tax Assessment Act 1936 (Cth) considered in *Reynolds v Deputy Commissioner of Taxation* (1984) 3 FCR 329 similarly provided (in s 252(1)(f)) that the public officer shall be "answerable for the doing of all such things as are required to be done by the company" under the Act and "in the case of default shall be liable to the

---

[8] The statute there, s 52(2) of the Income Tax Act, provided: "The manager or other principal officer of every body of persons shall be answerable for doing all such acts, matters and things as shall be required to be done by virtue of this Act for the assessment of such body and the payment of the tax".

[9] Defined in s 2 to include "any trustee, guardian, curator, manager, or other person having the direction, control, or management of any property on behalf of any person, but does not include an executor".

[10] Defined in s 2 to mean "any minor, lunatic, idiot, or person of unsound mind".

[11] The term "agent", in relation to a non-resident person or to a partnership in which any partner is a non-resident person, is defined in s 2 to include (a) the agent, attorney, factor, receiver, or manager in Hong Kong of such person or partnership, and (b) any person in Hong Kong through whom such person or partnership is in receipt of any profits or income arising in or derived from Hong Kong.

[12] The point is not affected by the fact that the agent of non-resident taxpayer can be made personally chargeable to tax: s 20A.

same penalties", thus again making express provision for liability for penalties — a provision noticeably absent in our ss 57 or 82A.

57. I fully accept Mr Wong's submission that a high degree of compliance by taxpayers in submitting timely, true, correct and complete tax returns and information to the IRD is crucial for the effective operation of the system. But making directors, managers, secretaries and liquidators who signed companies' returns, in addition to the corporate taxpayers, potentially liable for the administrative penalty is a strong thing. There is simply no specific provision for that; nor was there any mention in the legislative materials of any possibility of these persons being held liable. If the legislature wishes to make this class of officers potentially liable for substantial administrative penalties for incorrectness in the company's tax return, it can and should do so in plain terms: *c.f. Reynolds v Deputy Commissioner of Taxation* (1984) 3 FCR 329, 340; and see the authorities cited in §18 above for the principle against doubtful penalisation.

58. It is to be noted that in relation to the parallel criminal equivalent in s 80(2), s 80(4) expressly provides that any person who aids, abets or incites another person to commit an offence under s 80 shall be deemed to have committed the same offence and to be liable to the same penalty. There is no equivalent provision in s 82A.

59. On behalf of the Commissioner it was argued that the appellants' construction of s 57(1) would mean that failure to comply with it would have no consequences. Mr Denis Chang SC, who appeared for the appellants, submitted that s 57(1) concerned the internal question of who within a company is responsible for taking steps to enable the company to do that which is required of the company under the Ordinance. But the Commissioner's construction is not free from difficulties either. Although on the Commissioner's case every secretary, manager, director and liquidator of the company is required to make a return on behalf of the company, none of them is liable under s 82A(1)(d) if no return is furnished to the IRD (as Mr Stewart Wong SC, appearing for the Commissioner, was inclined to accept, without formally conceding it). This undermines the Commissioner's submission that it makes no sense for the legislature to make the officers answerable for acts required to be done by the company without imposing sanctions on them for failing to discharge that responsibility. In *D69/97*, where the company was unable to make a tax return because its only two directors were in deadlock, it was the company, not the directors, who was assessed to additional tax. Likewise where the board of directors approved the company's tax return (which turns out to be incorrect), but it was signed by the secretary or manager on the board's instruction, none of the directors would be liable whereas the secretary or manager would be, subject to the defence of reasonable excuse. A perverse but predictable incentive would be created for the more senior officers in a company to avoid signing the company's tax return and to require the junior ones to do so. Mr Wong surmised that in such a case the junior officer might have a reasonable excuse if the return turned out to be incorrect, but such a scheme hardly conduces to the purpose he says the section serves.

E6. Statutory purpose

60. It was submitted on behalf of the Commissioner that the statutory purpose would be defeated if the appellants' construction was adopted. I do not agree. Even without personal liability on the part of a company's officers under s 82A(1)(a), there would be deterrence through the penalty that may be imposed on the company itself who, as is common ground, did make the return. Punishment of the taxpayer company is a strong deterrent to the officers who can be held accountable by the company for misfeasance or by the shareholders if they are not themselves shareholders.

61. It would moreover be mistaken to think that no personal liability could attach to delinquent officers. In appropriate cases, it seems to me they can be made liable under s 80(4) for aiding and abetting the company's breach of s 80(2) or under s 101E of the Criminal Procedure Ordinance (Cap 221), which provides:

> "Where a person by whom an offence under any Ordinance has been committed is a company and it is proved that the offence was committed with the consent or connivance of a director or other officer concerned in the management of the company, or any person purporting to act as such director or officer, the director or other officer shall be guilty of the like offence."

Where there is wilful intent to evade or assist the company to evade tax, the relevant officers may also be prosecuted under s 82.

E7. Section 51(5)

62. The Commissioner also relied on the latter part of s 51(5) (quoted in §30 above) which provided that any person signing a return, statement, or form shall be deemed to be cognizant of all matters therein. It was argued that that limb is there for the purpose of buttressing s 82A(1)(a). But s 82A does not make such cognizance a condition for liability. Nor can s 51(5), which creates only a rebuttable presumption, override the reasonable excuse defence in s 82A. Further, the function of the second limb of s 51(5) is to presume (rebuttably) that the person signing a document is cognisant of its contents (but not their falsity), relieving the Commissioner or the prosecution of having to prove such knowledge to which circumstances would in any event tend to point: see *The Queen v Ng Wing Keung* [1997] HKLRD 142; *Moulin Global Eyecare Trading Ltd (in liquidation) v Commissioner of Inland Revenue* (2014) 17 HKCFAR 218 at §120. This presumption serves a purpose regardless of whether s 82A(1)(a) applies to an officer who signs a company's tax return. Accordingly this section is in my opinion of little assistance in the present debate.

E8. Conclusion

63. For all these reasons, in relation to Question 1(a), I consider that where a company has been required by notice issued to it under s 51(1) to make a return, it is the company, rather than the individual who signs the document, that furnishes, or makes, the

return in compliance with the requirements of the notice. Accordingly, s 82A(1)(a) does not permit a penalty assessment to be made on the appellants.

F. Section 82A(1)(c)

64. On behalf of the Commissioner, it was pointed out that the Board had also decided against the appellants on the ground of s 82A(1)(c) (see §§71-75 of the Decision). It was therefore said that the appellants' attack on the Board's decision in relation to s 82A(1)(a) was academic.

65. Mr Wong, however, fairly admitted that the Commissioner had never relied on s 82A(1)(c) either in his assessments or before the Board as a separate head of liability. The appellants' opening and closing submissions before the Board did refer to s 82A(1)(c) but only to explain its structure, in support of their argument on s 82A(1)(a).[13] The Commissioner's submissions before the Board did not refer to s 82A(1)(c) at all. While the Board's function in an appeal under s 68 is to consider the matter *de novo*, it must proceed fairly, so that the taxpayer is not taken by surprise: *Shui On Credit Co Ltd v Commissioner of Inland Revenue* (2009) 12 HKCFAR 392, §§30-31. In the circumstances of this case it seems to me a breach of natural justice and hence a procedural error of law for the Board to find the appellants liable separately under s 82A(1)(c).

66. Without going into the debate whether the existing questions of law are adequate to encompass this point, I would give leave for the appellants to appeal on the additional ground that the Board's decision in relation to s 82A(1)(c) should be quashed for this reason.

67. Furthermore, the mandatory notices given to the appellants by the Commissioner pursuant to s 82A(4) in January 2011, notifying them of the right to make written representations to him before he made any assessment of additional tax against them, only alleged that they had "made incorrect tax returns in respect of [NT Trading] by understating its profits" (and over-claiming its losses in the case of the 1999/2000 return). In other words, it seems to me that only s 82A(1)(a) had been invoked against the appellants in the statutory procedure. I cannot see how the Board's finding of liability based on s 82A(1)(c) can be left to stand.

G. Question 1(b) — effect of s 70

G1. The issue

68. S 70 provides:

> "Where no valid objection or appeal has been lodged within the time limited by this Part against an assessment as regards the amount of the assessable income or profits or net assessable value assessed thereby, or

[13] The appellants' notice of appeal to the Board stated that "if and so far as the allegation is that Mr Koo or Mr Murakami … gave any incorrect information within section 82A(1)(c) …" such allegation was denied.

> where an appeal against an assessment has been withdrawn under section 68(1A)(a) or dismissed under subsection (2B) of that section, or where the amount of the assessable income or profits or net assessable value has been agreed to under section 64(3), or where the amount of such assessable income or profits or net assessable value has been determined on objection or appeal, the assessment as made or agreed to or determined on objection or appeal, as the case may be, shall be final and conclusive for all purposes of this Ordinance as regards the amount of such assessable income or profits or net assessable value:
>
> Provided that nothing in this Part shall prevent an assessor from making an assessment or additional assessment for any year of assessment which does not involve re-opening any matter which has been determined on objection or appeal for the year."

69. The issue here is whether, in the context of determining if the appellants are liable to be assessed to additional tax under s 82A(1)(a), it is open to them to argue that NT Trading's tax returns were in fact *not* "incorrect" in understating its assessable profits. The Commissioner's contention, which was accepted by the Board, is that s 70, especially when read with s 82B(3), precludes the appellants from so arguing, because the decision of the Board on NT Trading's appeal (*D41/08*) is "final and conclusive" as regards the amount of NT Trading's assessable profits for all purposes of the Ordinance including the appellants' challenge of the additional tax assessments against them.

G2. Whether final and conclusive against third parties

70. On behalf of the Commissioner, Mr Wong argued that s 70 is clear and unambiguous in providing that the assessment shall be final and conclusive for all purposes of the Ordinance, and that there is no warrant for reading in words such as "as between the Commissioner and the person assessed". To assess this submission it is necessary to examine s 70 more closely.

71. S 70 is found near the end of Part 11 on "Objections and Appeals". Objections to the Commissioner and appeals to the Board (and subsequently to the courts on points of law) are the only means for challenging an assessment provided in the Ordinance. S 70 provides for the consequences when the avenue for challenging an assessment is exhausted in specified circumstances, namely:

(1) where no valid objection or appeal has been lodged within time;

(2) where there is an objection but the Commissioner and the person assessed come to an agreement on the amount under s 64(3) (during the objection process);

(3) where there is an appeal but it has been withdrawn by the appellant under s 68(1A)(a) or dismissed for default of appearance of the appellant under s 68(2B)(c); or

(4) where the amount has been determined on objection (pursuant to s 64(2)) or on appeal.

72. These are all processes engaged in by the Commissioner and the person assessed. It is in this context that the statute provides, in s 70, that at the end of these processes, the assessment, *as made or agreed to or determined on objection or appeal*, as the case may be, is "final and conclusive" as regards the specified matters. Read in context, the phrase does not seem to me to have the sweeping effect contended for by the Commissioner.

73. "Final" means "at the end". So far as third parties are concerned, in my opinion it would as a matter of ordinary usage be inapt to speak of something being "final" when the dispute or *lis* involving them has not even started. There is simply no process begun in relation to them that can properly be said to have come to the end.

74. The combined phrase "final and conclusive" does not take the matter any further. The expression is a familiar one in the law. It is an example of the genus of provisions (sometimes called finality clauses or ouster clauses) which seek to preclude further legal challenge between the parties such as by way of appeal. This is illustrated by *R (on the application of Revenue and Customs Commissioners) v Machell* [2006] 1 WLR 609, where the issue was whether a statutory provision that a referee's decision on the value of goods wrongfully forfeited and destroyed by the UK Customs was "final and conclusive"[14] had the effect of precluding judicial review of the referee's decision. At §24, Stanley Burnton J said:

> " Provisions purporting to oust the review jurisdiction of the Courts are narrowly interpreted, although I doubt whether a narrow interpretation is necessary in this case. A decision is 'final' if there is no appeal from it: *R v Medical Appeal Tribunal*, ex p Gilmore [1957] 1 QB 574; *R v Nat Bell Liquors Ltd* [1922] 2 AC 128, per Lord Sumner at 159-60. 'Conclusive' means no more than that the decision as made is binding as between the parties." (emphasis added)

75. It seems to me that this is the sense in which the phrase "final and conclusive" is used in s 70. As a general principle of common law, "nothing can be more contrary to natural justice, than that any one should be injured by a determination, that he, or those under whom he claims, was not at liberty to controvert": quoted from *Buller's Nisi Prius* (7th ed 1817) at p 232 by Luxmoore J in *Freshwater v Bulmer Rayon Co Ltd* [1933] 1 Ch 162, 176.

[14] Para 17(4) of Schedule 3 to the (UK) Customs and Excise Management Act 1979 provides: "For the purposes of sub-paragraph (1)(*c*) above, the market value of any thing at the time of its seizure shall be taken to be such amount as the Commissioners and the claimant may agree or, in default of agreement, as may be determined by a referee appointed by the Lord Chancellor (not being an official of any government department), whose decision shall be final and conclusive; and the procedure on any reference to a referee shall be such as may be determined by the referee."

76. The potential unfairness that would result from the Commissioner's construction is illustrated in this case by Mr Murakami's position. He had ceased to be a director of NT Trading in 2002,[15] before the tax audit which led to the revised assessments and long before any step was taken by NT Trading to challenge those assessments. Yet 15 years after he signed on the tax return he was hit with an additional tax assessment and, if the Commissioner's construction is correct, is to be told that he is bound by the Board's ruling in *D41/08* — a proceeding in which he never took part — that NT Trading's tax return was incorrect and that he is precluded from contending otherwise in his own appeal against his penalty.

77. It is significant to note that s 70 is not limited to a determination by the Board on appeal, but extends to a matter assessed by an assessor, or determined by the Commissioner, or agreed between the Commissioner and the person assessed. It would be quite remarkable that an assessment in such circumstances could become binding upon and beyond challenge by a third party (other than the privies of the person assessed) without any opportunity for objection or adjudication in which the third party can take part. I would be most reluctant to conclude that a statute had such an extraordinary effect without it being expressed in the clearest language. An example of such express provision may be found in s 70B(a) which states that for a couple who have elected personal assessment, if either spouse makes an objection, appeal or application in respect of any assessment made in consequence of the election, the other spouse shall be "deemed to be joined in the objection, appeal or application."

78. Mr Wong pointed to s 82B(3) (quoted in §13 above). It was argued that this signified a clear intention of the legislature that the finality provision in s 70 applied in an appeal against additional tax assessed under s 82A so that the incorrectness of the original return cannot be re-opened by a third party assessed to additional tax.

79. With respect, this is not my reading of s 82B(3). This provision does not seek to apply only s 70, but also ss 66(2) and (3), 68, 68AA, 68AAB, 68A and 69. Plainly the purpose is to replicate the machinery of appeals to the Board and to the court for the purposes of assessments to additional tax, through incorporation by reference rather than a wholesale repetition of those provisions *mutatis mutandis* in Part 14.

80. It may be noted that s 82B(3) does not mention s 66(1) and (1A). That is clearly because these two subsections are reproduced, in long form, in s 82B(1) and (1A). The procedure of objections to the Commissioner under s 64 is also not incorporated, presumably because before any additional tax is imposed, the Commissioner or a deputy commissioner will already have considered representations made by the person to be assessed pursuant to s 82A(4).

81. Subject to exceptions, s 82B(3) effectively re-enacts the appeal mechanism found in Part 11, *mutatis mutandis*, for the purposes of assessments to additional tax under s 82A. The phrase "as if …" invites one to substitute appeals against assessments to additional tax for references to appeals against assessments to tax found in the

[15] It appears Mr Koo also retired later, in mid 2006 (see Decision §134.3).

incorporated provisions. The phrase "so far as they are applicable" recognises that there may be certain provisions which are inapt with respect to appeals against assessments to additional tax even with necessary alterations in the wording.

82. On this basis, s 82B(3) simply makes provision, in relation to appeals against assessments to additional tax, as to: service of documents on the Commissioner (s 66(2)), the procedures before the Board and its powers in disposing of an appeal (s 68), directions on the provision of documents and information (s 68AA), privileges and immunities (s 68AAB), and appeals to the Court of First Instance (s 69).

83. Likewise, in my opinion, s 82B(3), when applying s 70 by incorporation, simply means that in the equivalent circumstances mentioned in s 70 (as summarised in §71 above) such as where no appeal[16] against an assessment to additional tax has been lodged within time, the *assessment to additional tax* is itself final and conclusive as regards the matters specified, as between the parties to the additional tax assessment. S 82B(3) applies s 70 not *in* appeals against additional tax but *with respect to* such appeals *as if* they were ordinary appeals against assessments to tax. S 82B(3) is simply a drafting technique to make provision for an appellate regime and attendant matters in relation to additional tax. In my judgement it does not have the effect contended for by the Commissioner.

84. Mr Wong relied upon *Chu Ru Ying v Commissioner of Inland Revenue* [2010] 2 HKLRD 1052. There the IRD made an additional salaries tax assessment on the taxpayer pursuant to s 60. The taxpayer's objection was not wholly successful but she did not serve a compliant notice of appeal to the Board within time. The Board refused to extend time for appealing. Subsequently the Commissioner made an assessment to additional tax on the taxpayer pursuant to s 82A. On the taxpayer's appeal to the Board under s 82B, she argued that the s 60 assessments had been wrongly made. That argument was rejected by the Board, but the Board stated a case for an appeal to the court on the question whether the salaries tax assessments were by virtue of s 70 final and conclusive as regards the amounts of the assessable income. Agreeing with the judge below (Burrell J) who upheld the Board's decision, Tang VP (with whom Cheung JA and Stone J agreed) stated in §41:

> "It is clear section 70 covers situations where a taxpayer has already availed his/herself of all the channels of appeal, including appealing to the courts. In such cases, it is difficult to see why, on a section 82B appeal, section 70 should be inapplicable. In our present case, there was no effective appeal. But I believe the principle to be the same. …"

It is clear, in my respectful opinion, that s 70 itself provided the answer in that case because the additional tax was assessed against the same taxpayer as the original assessment. S 70 therefore operated, "for all purposes of [the] Ordinance", to render the original assessment final and conclusive as regards the amount of assessable income *as between the taxpayer and the IRD*.

[16] The reference in s 70 to no objection being lodged in time is inapplicable to assessment to additional tax.

85. It is true that Tang VP also mentioned s 82B(3) in his judgment (see §§28 and 40) but it is not clear that his Lordship actually relied on that subsection as rendering the original assessment final and conclusive in the appeal against the assessment to additional tax. S 82B(3) was not mentioned in Burrell J's decision at all. The taxpayer was not legally represented. Most importantly, the case did not concern the binding effect on a third party. With great respect, I do not think Mr Wong can derive any support from that decision for his argument on s 82B(3).

86. Relying on *dicta* in *Moulin Global Eyecare Trading Ltd (in liquidation) v Commissioner of Inland Revenue* (2014) 17 HKCFAR 218 at §119, *Good Mark Industrial Ltd v Commissioner of Inland Revenue* [2015] 2 HKLRD 16 at §7.2 and *Extramoney Ltd v Commissioner of Inland Revenue* [1997] HKLRD 387 at 394J, Mr Wong submitted that finality of assessments is a major policy aim of the Ordinance and that this policy applies, *inter alia*, to Part 14. I agree but in my view this policy consideration does not support the Commissioner's argument. The appellants are not seeking to upset the finality of the assessments against NT Trading or to re-open them. They merely contend that the assessments should not be treated as binding on them. It should also be noted that in *Moulin Global Eyecare Trading Ltd* at §56, Lord Walker of Gestingthorpe NPJ (with whom Ma CJ, Ribeiro PJ and Bokhary NPJ agreed) stated that the general rule embodied in s 70 "is aimed at achieving finality *as between the Commissioner and the taxpayer*" (emphasis added). The case was not concerned with the liability of a third party to additional tax under s 82A, but this description is, if I may respectfully say so, entirely consonant with the natural response of the common law to a provision of this kind.

87. The appellants' construction may also work in favour of the Commissioner who may, in some cases, particularly tax evasion cases, discover that his earlier final assessments upon insolvent or dissolved taxpayers were too low. Without seeking to re-open those assessments, the Commissioner could pursue the responsible third parties, for example under ss 80 and 82, and seek to prove that the assessable profits were understated, without being faced with an argument that he was precluded from doing so by s 70.

88. Mr Wong relied on the decision of the Court of Appeal in *Moulin Global Eyecare Trading Ltd* [2010] 4 HKLRD 283, which concerned a different aspect of the dispute that eventually resulted in the Court of Final Appeal's decision in 2014 referred to above. The liquidators of the taxpayer company contended that although the relevant profits tax assessments had become final and conclusive under s 70 because no objections had been lodged by the company within time, upon liquidation its liquidators could go behind the assessments in adjudicating the proofs of debt lodged by the Commissioner and reject them (as they did) if they were not satisfied that the debts represented real liabilities of the company. The judge (Kwan JA) and the Court of Appeal both held that the proofs could not be rejected. Mr Wong argued that the case is indistinguishable from the present one because the liquidator was a third party who was nevertheless held to be bound by the assessments. With respect, the argument is flawed. The reason for the decision was that, as settled by a long line of authorities, the only permissible way for the liquidators to challenge the debts under the assessments was the statutory procedure provided in the

Ordinance for considering objections and appeals against assessments to tax. The liquidators' duty in adjudicating upon proofs is to see whether they represent true debts *of the company*. So even though the assets of a company are not vested in liquidators, in this sense they step into the shoes of the company and cannot be regarded as real third parties.

89. The Board reasoned that despite s 70, the third party may nevertheless show that he had reasonable grounds to believe and did believe in the correctness of the return when he signed it (§§45, 47 and 49). In my view, it does not follow from the availability of the built-in "reasonable excuse" defence that the third party should be precluded from contesting the other constituent elements of the liability to the penalty. Further, the Board seems to have thought that if a third party does not succeed under the defence of reasonable excuse, then there is "no policy justification to permit repeated challenges just to ensure that a callous and reckless third party" may reopen the arguments and "avoid responsibility by the off chance that another panel might find the taxpayer not liable" (§48). With respect to the Board, I am unable to share this view which seems to me to reverse the usual policy of the law as I have sought to explain above. In addition, as already explained, under s 70 an assessment does not become final and conclusive only after a determination by a previous Board, but also where it was agreed or left to stand by default of objection or appeal, so that the Board in an additional tax appeal may be the very first panel to determine the question.

90. For the above reasons, the answer to Question 1(b) is: No.

G3. What was final and conclusive

91. If I am wrong on the construction of ss 70 and 82B(3), a question still remains as to what exactly is deemed final and conclusive as against the appellants. S 70 itself provides that the "assessment" shall be final and conclusive "as regards the amount of such assessable … profits". Mr Wong accepted that this means that only the amounts of the assessable profits (and, it implicitly follows, the amounts of tax payable) in the years in question are binding on the appellants, and "not the basis upon which it is arrived at".

92. The amounts of assessable profits of NT Trading as determined by the Deputy Commissioner and confirmed by the Board can be arrived at by at least two different routes: first, by holding that the expenses were not deductible under ss 16 and 17 in the first place, and, secondly, by acknowledging they were deductible under ss 16 and 17 but holding that s 61A is applicable so that the IRD may assess tax on NT Trading "as if" the arrangement for the payment of fees had not been entered into or carried out or in some other manner the IRD considers appropriate to counteract the tax benefit which would otherwise be obtained (see s 61A(2)). As accepted by Mr Wong, the assessable profits would be the same under either route, because the way in which s 61A operates in a case such as the present is to empower the Commissioner to disregard the expenses in question.

93. Where the s 61A route is adopted, it presupposes the tax benefit would have enured, ie the tax avoidance scheme would have worked, but for the Commissioner's

intervention under s 61A: *Shui On Credit Co Ltd v Commissioner of Inland Revenue* (2009) 12 HKCFAR 392, §6. On this basis, it is at least arguable that the tax returns were not incorrect in deducting the management fees from the assessable profits. Instead, the Commissioner and the Board would be exercising a statutory power under s 61A to counteract the tax benefit without impugning the correctness of the deduction. It would also be arguable that the returns were not incorrect in understating the amount of assessable profits, when they were increased only by the exercise of a statutory power not available to the taxpayer.

94. Accordingly, even if s 70 applies to render the amounts of assessable profits of NT Trading as determined by the Board in *D41/08* binding on the appellants, it would still be legally open to them to argue that the tax returns were not incorrect and that the "bottom line" should be arrived at by way of s 61A.

H. Question 1(c)

95. By this question, the appellants essentially contend that in *D41/08* the Board found that the expenses conferred a tax benefit which the Commissioner was entitled to counteract pursuant to s 61A. The finding that s 61A applied necessarily implied that the expenses were otherwise deductible: see *Shui On Credit Co Ltd v Commissioner of Inland Revenue* (2009) 12 HKCFAR 392, §6. It follows, the appellants argued, that NT Trading's tax returns were not incorrect in having deducted those expenses.

96. The Commissioner disputes the premise of the argument, and contends that the Board in D41/08 primarily decided that the expenses were not deductible because they did not satisfy ss 16 and 17, but that *alternatively*, if they were deductible, their effect should be reversed by virtue of s 61A.

97. In its decision in *D41/08*, the Board stated:

> " 54. … We conclude and accept the submissions put to us by Mr Ng [counsel for the Commissioner] that there was no way in which it was necessary for the Taxpayer to incur such management fees for the purpose of its trading business and indeed, as we have made it clear above, these were on top of the HK$30,000,000.00 odd administrative fees that it claimed in the relevant year of assessment.
>
> 55. We have no hesitation in coming to the conclusion that the management fees in question could never have been regarded as expenses incurred in the production of the Taxpayer's profits. It was not acceptable in our view to look at the Group as a whole. In our view, it is unequivocal and clear that each company within a group must be treated as a separate taxable entity.
>
> 56. We have no hesitation in accepting the submissions of Mr Ng that

> each company within the Group must be treated separately and one cannot attribute the overall business expenses of the Group or one member of the Group to another member in computation of the other's tax liability.
>
> …
>
> 58. … In our view, having regard to our findings and having regard to the way in which Mr Koo gave his evidence, the inevitable conclusion is that the expenses, being the management fees, the sum written off and the legal and professional fees as set out in the Determination cannot be treated as deductible expenses pursuant section 16 of the IRO."

98. The Board then went on to say that although given its conclusion on deductibility of the expenses, an analysis of s 61A would be moot, it was asked by the parties to deal with and address this particular point. The Board expressed itself in this way:

> " 62. We have had the opportunity to review very carefully the Determination by the Deputy Commissioner and in particular, with regard to paragraph 7 onwards in his Determination. We have also considered the seven specific matters pursuant to section 61A, and having considered each of them as set out in the Determination, we would also come to the conclusion that the entering into the Service Agreements between the Taxpayer and NTEI and the purported payment of management fees to NTEI are transactions entered into or carried out for the sole or dominant purpose of enabling the Taxpayer to obtain a tax benefit as provided for under section 61A of the IRO. We accept the analysis set out in the Determination by the Deputy Commissioner and would not say anything further regarding this particular point."

99. In the Determination referred to by the Board above, the Deputy Commissioner decided that the management fees to NTEI were not allowable deductions under ss 16 and 17 (see §3(6)) but went on to consider the issue under s 61A and to conclude that the service agreements and payment of management fees were transactions for the sole or dominant purpose of enabling NT Trading to obtain tax benefits (see §3(7)). Nevertheless, reading the decision in *D41/08* as a whole together with the Determination to which the Board made reference, it is in my view clear that the primary conclusion of the Board there was that the expenses were not deductible under ss 16 and 17, and that while they also agreed with the Deputy Commissioner's views on s 61A, it was a fall-back position even though it was not prefaced with "if which is denied …" or similar qualifying words. The answer to Question 1(c) is therefore: the Board did decide in *D41/08* that the expenses were not deductible under ss 16 and 17. They did not have to deal with, and did not determine, whether the returns were "incorrect" within the meaning of s 82A. In any

event, by reason of the answer to Question 1(b), their decision is not conclusive as against the appellants.

I. Question 2

100. Each of the questions raised under Question 2 concerns the concept of "reasonable excuse" within the meaning of s 82A(1). This is a familiar expression in the law, used in various statutes to create a defence exonerating a person who would otherwise be subject to civil or criminal liability.

101. In *HKSAR v Ho Loy* (2016) 19 HKCFAR 110, which concerned the offence under regulation 61(2) of contravening without reasonable excuse any relevant provision of the Road Traffic (Traffic Control) Regulations (Cap 374G), Fok PJ stated (footnotes omitted):

> "36. The expression 'without reasonable excuse' occurs in various statutory contexts. A consideration of the defence involves looking to three matters. First, self-evidently, the matters said to constitute reasonable excuse must be identified. Secondly, the court will then examine whether the excuse is genuine, since the reason asserted for departing from a relevant prescription must be the real reason for doing so. Thirdly, the court must make an assessment of whether that excuse is reasonable, which the court will do on an objective standard depending on the particular facts of the case.
>
> 37. In determining whether an excuse is reasonable or not, it will be relevant to have regard to the context in which the defence of reasonable excuse arises, since that context may suggest either a narrow or wide range of circumstances that might constitute a reasonable excuse. For example, the range of circumstances in which there is a reasonable excuse for failing to provide a sample of blood or urine in the context of the laws against driving under the influence of drink has been held to be narrow, since the circumstances giving rise to the offence are always essentially similar so that what might be a reasonable excuse for committing it can be envisaged. In other contexts, the defence may be construed more widely and the question of whether or not an excuse is reasonable will be determined in the light of the particular facts and circumstances of the individual case."

102. In a similar vein to what Fok PJ said in §37 of *Ho Loy*, the majority[17] of the High Court of Australia in *Taikato v The Queen* (1996) 186 CLR 454 stated (at p 464) that "what is a reasonable excuse depends not only on the circumstances of the individual case but also on the purpose of the provision to which the defence of 'reasonable excuse' is an

[17] Brennan CJ, Toohey, McHugh and Gummow JJ.

exception". This statement was adopted by Tang PJ in *Secretary for Justice v Chan Chi Wan Stephen* (2017) 20 HKCFAR 98 at §96, albeit his Lordship was the only member of the court who considered that the question of "reasonable excuse" was engaged in that case.

103. In approaching the defence of reasonable excuse in an appeal from the Board under the Ordinance, it is important to bear in mind that whether or not a reasonable excuse has been made out is a question of fact in each case, to be decided by the Board and not by the court: *Frank Galliers Ltd v Customs and Excise Commissioners* [1993] STC 284, 292b. In another context it has been said to be "par excellence a matter for the jury": *R v Unah* [2012] 1 WLR 545, §6. It is well established that the scope for impugning a finding of fact such as this on an appeal confined to questions of law is very limited: see eg *Kwong Mile Services Ltd (in members' voluntary winding-up) v Commissioner of Inland Revenue* (2004) 7 HKCFAR 275 at §§31-37.

104. Question 2(a) in effect asks whether a director's subjective belief in the correctness of the company's tax return is *capable* of constituting a reasonable excuse for the purposes of s 82A(1). The answer is clearly: yes. The Commissioner did not and does not contend otherwise. However, neither do the appellants, as I understand their position, disagree with the Commissioner's submission that such subjective belief is a necessary but not necessarily sufficient condition for the defence.

105. Question 2(b) in effect asks whether a director's reliance[18] on the views of the company's accounting staff and advisers such as its auditors and tax advisers that the company's tax returns are correct is *capable* of constituting a reasonable excuse. Again, the answer is clearly affirmative. Reliance on others *can be* a reasonable excuse, though the reliance must be reasonable: *R v General Commissioners of Income Tax for Sevenoaks, ex parte Thorne* [1989] STC 560, 566-567. Whether such reliance constitutes a reasonable excuse depends on the circumstances of the particular case.

106. Recognising the highly limited scope of a permissible challenge, by Question 2(c) the appellants essentially contend that the findings of fact made by the Board in their Decisions *require* the conclusion that the appellants had shown reasonable excuse for the incorrectness in NT Trading's tax returns, or in other words, that this is the true and only reasonable conclusion.

107. The critical facts relied upon by the appellants are as follows:

(1) At all material times NT Trading employed a financial controller and its annual accounts were audited by qualified professional accountants, namely Price Waterhouse or Deloitte.

(2) "The evidence of the witnesses for the Appellants tends to suggest that a very strict and proper review and audit system was adopted by

[18] The question as formulated refers to "reasonable" reliance but such formulation risks making the question tautologous.

the Group under the relevant accounting standards in the preparation of the audited accounts of the Group." (Decision §93)

(3) Mr Koo came up with the service agreements scheme. Before it was implemented in 1995 he had informally discussed it with Mr Tikku, the most senior tax partner of Price Waterhouse at the time, and while Mr Koo could not recall the exact details of that discussion, his understanding afterwards was that the arrangement was proper and appropriate. Price Waterhouse had expressed their reservation on the scheme's validity in a letter dated 26 June 1997, although their concern appeared to be about whether NTEI would be regarded as carrying on business in Hong Kong and become chargeable with profits tax in Hong Kong. Mr Koo then approached Mr Tikku with a view to talking him "into seeing things his way" and "eventually got things done his way". (Decision §§103 and 107)

(4) In the case of Mr Koo, he:

(a) had a "misguided conviction of the correctness of the Group's perspective, ie, the source of business of a taxpayer cannot be considered in isolation from the activities of the group of companies to which it belongs" (Decision §89);

(b) held a "misguided belief that in signing the tax returns, he could simply rely on the fact that in a big corporation, there are other professionals employed internally and externally, but without articulating how such professionals are allocated at a high level with clear lines of instruction pertaining to accuracy of tax information" (Decision §91);

(c) "might well have believed or deluded himself into believing, from his informal discussion with [a tax adviser], that the conceptual framework of his tax structure works" (Decision §105); and

(d) perceived the arrangement as "a valid tax avoidance scheme" when he signed the tax returns (Decision §106).

(5) In the case of Mr Murakami, it appears that the Board found that he relied on internal and external professional accountants and auditors to prepare the accounts and tax returns for the Group including NT Trading and that he genuinely believed that NT Trading's tax returns were truthful and correct (Decision §108).

(6) There were other matters relied upon by the appellants in their argument, but they seem to me to be evidence they had put forward

> which was not or not wholly accepted by the Board, rather than findings of the Board.

107. In short, the Board appears to have accepted that the tax computations were prepared by accounting staff and/or external accountants, that the appellants did rely on the fact that they were so prepared, that they did genuinely believe the service agreements scheme would work and therefore did believe that the tax returns were not incorrect in deducting the management fees before arriving at the assessable profits.

108. In the Board's view, however, what was fatal to the defence was the absence of evidence of what instructions were given to either the internal tax department or the external tax advisers, as well as evidence of whether they had been given all relevant information, including in particular matters that might suggest the management fees were not deductible, such as (i) the true "management reasons" for NT Trading to receive management fees from the Mainland subsidiaries and to pay management fees to NTEI as stated in a letter from the appellants' tax representative, and (ii) the Group's intention that the payment terms of the service agreements would not be strictly adhered to, and that management fees would only be charged when a gross profit margin was insufficient to pay NTEI, with the result that NT Trading's management fees income would always be less than its management fees payments under the back-to-back contracts. See the Decision §§86, 91, 92, 96-97, 100, 102, 104, 105 and 109.

109. There is no suggestion by the appellants that this is an irrelevant consideration which the Board was bound to exclude from its mind. The weight to be put on it and its effect on the ultimate question of reasonable excuse are matters for the Board with which this court will not interfere in the absence of an error of law.

110. Although it was not expressly found as a fact, the appellants submitted it should be inferred that the audit opinions on NT Trading's financial statements were unqualified because there was no suggestion that they were qualified by any inability of the auditors to obtain any books and records that they required in order to complete their audits. The appellants also relied on the statement contained in the auditors' opinion that they had planned and performed their audit so as to obtain "all the information and explanations … considered necessary". As the Board said (see Decision §§93 & 95), however, it was the preparation of tax computations that mattered, not the preparation of audited accounts. The accounts were concerned with whether outgoings and expenses were actually incurred, not with whether they were deductible for tax purposes. The latter question turns upon, *inter alia*, whether the outgoings and expenses in question were incurred in the production of profits in respect of which the taxpayer is chargeable to tax: see s 16. As Lord Millett NPJ explained in *Nice Cheer Investment Ltd v Commissioner of Inland Revenue* (2013) 16 HKCFAR 813 at §33, the amount of assessable profits may be ascertained from the taxpayer's accounts drawn in accordance with ordinary principles of commercial accounting, but only if this is in conformity with the Ordinance.

111. The appellants criticise the following statement in the Decision:

> " 77. The burden is on the person making incorrect return in the additional

> tax appeal to show that full instructions have been provided to the delegate, the professional adviser or internal accounting manager, and to show that the incorrect view taken is reasonable in all the circumstances, and that there was a genuine reliance on a correct [*sic*] view."

112. There is a danger, in making statements of this kind, that they may be taken as propositions of law. The question of what in concrete terms needs to be shown to establish reasonable excuse depends on the facts of each case, and cannot be put into a legal straitjacket. For the same reason I do not propose to deal with the many previous decisions of the Board Mr Wong cited on whether reasonable excuse may be established by reliance on professionals. But I do not think that in the paragraph quoted above the Board was seeking to lay down a general requirement of the law. It seems to me they were simply addressing what they would look for in the circumstances of this particular case.

113. In the circumstances of this case, the Board came to the view that a reasonable excuse was not made out. In my judgement, on the evidence as set out in the Decisions[19] and on the primary facts as found by the Board, the appellants have failed to show that the only legally permissible conclusion was that they had a reasonable excuse. Question 2(c) must therefore be answered in the negative.

J. Question 3 — Quantum of penalty

114. The orders of the Board in relation to the amount of additional tax and interest have been set out in the table in §10 above. In brief, the Board's reasoning was as follows:

(1) Following *D118/02* (2003) 18 IRBRD 90 and *D69/03* (2003) 18 IRBRD 699, the Board adopted the approach of taking 100% of the tax undercharged as the starting point for the amount of penalty when three conditions were satisfied: (i) where there has been no criminal intent but the taxpayer has totally failed in his obligations under the Ordinance; (ii) where the Commissioner has had to resort to investigations or the preparation of assets betterment statements or has otherwise had difficulty in assessing the tax; and (iii) where the failure by the taxpayer to fulfil his obligations under the Ordinance has persisted for a number of years. (Decision §§122-124)

(2) The Board considered the three conditions satisfied and applied 100% as the starting point. (Decision §§131-157)

[19] The evidential record of the proceedings before the Board was not placed before this court.

(3) In relation to Mr Koo, the Board considered there was an aggravating factor in that the deductions claimed were part of a tax avoidance scheme for which he was responsible. For this factor the Board imposed an additional 50%. (Decision §§185-190)

(4) In relation to both appellants, the Board considered there were two mitigating factors each warranting a reduction of 5%, namely, (i) the accounting records showed descriptions of the various payments including the management fees to NTEI, which enabled identification of the issue; and (ii) there was disclosure in the returns regarding the transactions with non-residents. (Decision §§173-178, 191)

(5) In the end, therefore, the Board decided to impose a penalty on Mr Koo equivalent to 140% of the amount of tax that NT Trading was undercharged, and a penalty on Mr Murakami equivalent to 90% of the amount of tax undercharged, for the respective years of assessment. (Decision §191)

(6) The Board also awarded interest (also called "commercial restitution"), compounded monthly, at 7% per annum for the period up to 30 November 2003 and at the best lending rate thereafter, for the period "from the respective dates when the tax would have been due if the original return filed were correct to the date of the actual demand note",[20] subject to the jurisdictional limit of 300% of the tax undercharged. (Decision §§117, 192-194)

115. The appellants allege that the Board fettered its powers and discretion by adopting or relying upon the "Penalty Policy" of the IRD. However, although the Penalty Policy was attached to the Decision as Schedule II, there is in my view nothing to show that the Board fettered its discretion in any way by reference to that document. On the contrary, the Board correctly reminded itself that it was not bound by it (Decision §121), stated that in adopting 100% as the starting point it was not applying the Penalty Policy (§159), and actually disagreed with the approach stated there of treating interest as part of the starting point for quantum assessment (§§151, 192). In essence, it seems to me the Board followed its decision in *D118/02* where the Board was specially constituted by its Chairman and two Deputy Chairmen.

116. Accordingly, in my judgment, Question 3(a) as formulated does not arise from the Decisions. The appellants have failed to establish the alleged error of law in the

[20] On the face of the Decisions it is not entirely clear what these dates are. If they meant, for example for the year 1996/97, from 1997 (due date under original tax assessment on NT Trading) to 2017 (date of demand note for additional tax pursuant to the Decisions), it would mean monthly compound interest for 20 years which — assuming an average interest rate of 6% per annum — would exceed 300%. It appears, however, that the Commissioner had pursuant to the Decisions demanded interest for a shorter period.

Decisions as regards the quantum of additional tax. It is unnecessary to deal with the appellants' criticisms of the contents of the Penalty Policy.

117. Mr Barlow SC, who made submissions on behalf of the appellants on Questions 2 and 3, made a number of other points on the quantum of penalties which were not within the scope of Question 3 or the statement of grounds and reasons made pursuant to s 69(3)(a)(ii) or the appellants' skeleton argument. I decline to deal with these additional points raised without proper notice to the Commissioner.

K. Conclusion and disposition

118. For the foregoing reasons, the appellants are successful on Questions 1(a) and 1(b) and on the question of s 82A(1)(c). At the request of the parties I shall not pronounce the precise orders consequent upon allowing the appeal until after I have heard them further on that matter.

119. In the absence of agreement, written submissions on the orders to be made and on the question of costs should be lodged by the Commissioner within 21 days from the date of this judgment, and by the appellants within 14 days thereafter.

(Godfrey Lam)
Judge of the Court of First Instance
High Court

Mr Dennis Chang SC, Mr Barrie Barlow SC and Ms Isabel Tam, instructed by Mayer Brown JSM, for the 1st and 2nd Appellants

Mr Stewart Wong SC and Ms Elizabeth Cheung, instructed by Department of Justice, for the Respondent

APPENDIX

(Statement of Agreed Facts placed before the Board)

INLAND REVENUE BOARD OF REVIEW

APPEAL NO. B/R 16/13 AND B/R 17/13

STATEMENT OF AGREED FACTS

…..

The parties to the above appeal agree to the following facts:

Introduction

1. This is an appeal by Mr KOO Ming-kown ("**1st Appellant**") and Mr MURAKAMI Tadao ("**2nd Appellant**") (collectively referred to hereunder as "**the Appellants**") against the following assessments [Item 47], all dated 26 April 2013, issued by the Commissioner of Inland Revenue ("**the Commissioner**"), assessing the Appellants to Additional Tax under section 82A of the Inland Revenue Ordinance ("**the Ordinance**"), Chapter 112, for making incorrect Profits Tax Returns on behalf of Nam Tai Trading Company Limited ("**NT Trading**", formerly known as Nam Tai Electronic & Electrical Products Limited, in liquidation pursuant to the Winding-up Order dated 4 June 2012):

Assessments issued to the 1st Appellant:

Year of Assessment	Charge Number	Additional Tax
1996/97	1-6008595-97-A	$6,400,000
1999/2000	1-6008579-00-1	$6,200,000

Assessment issued to the 2nd Appellant:

Year of Assessment	Charge Number	Additional Tax
1997/98	1-6008601-98-8	$5,400,000

2. The Additional Tax was assessed following the dismissal of NT Trading's appeal to the Board of Review ("**the Board**") in respect of the assessments referred to in paragraphs 16 to 18 below, whereby NT Trading was denied deductions for management fees paid to its parent company (the main issue in dispute), and legal and professional fees paid to its parent company and its subsidiaries in the mainland of China.

3. NT Trading was incorporated as a private company in Hong Kong on 1 November 1983 and commenced business on 1 January 1984. In the directors' reports, the principal activities of NT Trading were described as:

- trading of electronic products (for the years ended 31 December 1996 and 1997);
- trading of electronic products and moulds (for the years ended 31 December 1998 and 1999).

4. At all relevant times, the parent company of NT Trading was Nam Tai Electronics, Inc. ("**NTEI**"), a British Virgin Islands company listed on the NASDAQ National Market of the United States of America. NTEI was also the ultimate holding company of various subsidiaries including:

- Nam Tai Electronics (Canada) Ltd. ("**NT Canada**")

- Namtai Electronic (Shenzhen) Co. Ltd. ("**NTSZ**")

- Zastron Plastic & Metal Products (Shenzhen) Ltd. ("**Zastron**") Shenzhen Namtek Co. Ltd. ("**Namtek**")

5. At all relevant times, NTSZ, Zastron and Namtek ("**the PRC Subsidiaries**") were wholly owned subsidiaries of NT Trading. The principal activities of NTSZ and Zastron were "manufacturing" while that of Namtek was "software development". A chart showing the structure of the group of companies consisting of NTEI, NT Trading, NT Canada, NTSZ, Zastron and Namtek is at Appendix A to the Determination of the Deputy Commissioner dated 31 October 2007 ("**the Determination**") [Item 5].

6. At all relevant times, the Appellants were directors of NT Trading. They also held the following positions on the board of directors of NTEI:

	Year ended	Position
The 1st Appellant	31 December 1996	Chairman
	31 December 1997	Chairman and chief financial officer
	31 December 1998	Senior executive officer
	31 December 1999	Senior executive officer
The 2nd Appellant	31 December 1996	Chief executive officer and vice-chairman
	31 December 1997	Chief executive officer and vice-chairman
	31 December 1998	Chairman
	31 December 1999	Chairman

Returns and Accounts

7. The directors' reports for NT Trading for the year ended 31 December 1996, 31 December 1997 and 31 December 1999 were signed by the 1st Appellant, and the

directors' report for the year ended 31 December 1998 was signed by the 2nd Appellant. The audited accounts for those years were signed by the Appellants. The directors' reports and audited accounts are at [Item 4].

8. On 27 July 1997 and 26 July 2000, the 1st Appellant signed, in the capacity of director, the Profits Tax Returns of NT Trading for the years of assessment 1996/97 and 1999/2000 respectively [Item 3] and declared NT Trading's Assessable Profits (Adjusted Loss) as follows:

Year of assessment	Assessable Profits (Adjusted Loss)
1996/97	$9,889,250
1999/2000	($3,803,183)

9. On 30 July 1998, the 2nd Appellant signed, in the capacity of director, the Profits Tax Return of NT Trading for the year of assessment 1997/98 [Item 3] and declared NT Trading's Assessable Profits as follows:

Year of assessment	Assessable profits
1997/98	$8,667,488

10. The Profits Tax Return of NT Trading for the year of assessment 1998/99 [Item 3] was signed by a Mr Francis LI, in the capacity of financial controller, who declared NT Trading's Assessable Profits as follows:

Year of assessment	Assessable profits
1998/99	$2,071,402

11. The Assessor issued to NT Trading the following Profits Tax Assessments and statement of loss, as the case might be, in accordance with the profits or loss returned [paragraphs 8 to 10 above]:

	1996/97	1997/98	1998/99	1999/2000
Profit/(loss) per returns	$9,889,250	$8,667,488	$2,071,402	($3,803,183)
Date of assessment/ statement of loss	8 August 1997	27 August 1998	6 October 1999	24 October 2000
Tax payable	$,.631,726	$1,287,121	$331,424	-

Tax Audit

12. In December 2002, the Assessor commenced an audit on the tax returns and accounts filed by NT Trading.

13. The Assistant Commissioner, having examined the facts, applied the provisions in sections 16, 17, 61 and 61A of the Ordinance and raised on NT Trading Additional Profits Tax Assessments for the years of assessment 1996/97 to 1998/99 and Profits Tax Assessment for the year of assessment 1999/2000 to disallow certain expenses including management fees paid to NTEI:

	1996/97	1997/98	1998/99	1999/2000
Date of assessment/ additional assessment	28 February 2003	31 March 2004	31 March 2005	31 March 2006
Profits/(loss) per return [Paragraph 11]	$9,889,250	$8,667,488	$2,071,402	($3,803,183)
Add: Management fee paid/payable to NTEI	32,313,540	34,790,641	25,622,804	35,873,789
Legal and professional fee paid/payable to NTE1 and NTSZ	4,429,290	–	–	–
Cost of sales adjustment	24,388,988	–	–	–
Salaries and allowances	4,800,000	–	–	–
Assessable profits	75,821,068	43,458,129	27,694,206	32,070,606
Less: Profits already assessed	9,889,250	8,667,488	2,071,402	–
Assessable Profits/ Additional Assessable Profits	$65,931,818	$34,790,641	$25,622,804	$32,070,606
Tax payable	$10.878.151	51166.411	14.099,642	55.131,296

14. After consideration of the seven matters set out in section 61A of the Ordinance, the Assistant Commissioner came to the conclusion that the entering into of the service agreements between NT Trading and NTEI and the purported payment of management fees to NTEI were transactions entered into or carried out for the sole or dominant purpose of enabling NT Trading to obtain tax benefits.

Objection and Appeal

15. By letters of 20 March 2003, 23 April 2004, 8 April 2005 and 19 April 2006 from Grant Thornton, NT Trading's then tax representative, the company raised objections against the assessment and additional assessments listed out in paragraph 13.

16. By the Determination [Item 5], the Deputy Commissioner revised or confirmed the assessments concerned. The amounts of assessable profits and tax payable as revised or confirmed were as follows:

	1996/97	1997/98	1998/99	1999/2000
Profits/(loss) per return [Paragraphs 8 to 10]	$9,889,250	$8,667,488	$2,071,402	($3,803,183)
Add: Management fee paid/ payable to NTEI	32,313,540	34,790,641	25,622,804	35,873,789
Legal and professional fee paid/payable to NTEI and NTSZ	4,429,290	–	–	–
Cost of sales adjustment (no adjustment)	–	–	–	–
Salaries and allowances (no adjustment)	–	–	–	–
Legal and professional fees	–	–	–	4,624,023
Management fee written off	–	–	3,955,874	–
Assessable profits	46,632,080	43,458,129	31,650,080	36,694,629

	1996/97	1997/98	1998/99	1999/2000
Less: Profits already assessed	9,889,250	8,667,488	2,071,402	–
Assessable Profits/Additional Assessable Profits	$36,742,830	$34,790,641	$29,578,678	$36,694,629
Tax payable	$6,062,567	$5,166,411	$4,732,588	$5,871,140

Having considered the facts of the case, the Deputy Commissioner accepted that no adjustments for cost of sales and salaries and allowances for the year of assessment 1996/97 were required. The Deputy Commissioner also considered that the following expenses were not deductible under sections 16(1) and 17(1)(b) of the Ordinance:

- management fees to NTEI for the years of assessment 1996/97 to 1999/2000;

- legal and professional fees of $4,429,290 to NTEI and NTSZ for the year of assessment 1996/97;

- legal and professional fees of $4,624,023 for the year of assessment 1999/2000;

- management fees of $3,955,874 written off in the year of assessment 1998/99.

The Deputy Commissioner further determined that section 61A of the Ordinance was applicable in relation to the first two items stated above.

17. By a Notice of Appeal dated 29 November 2007, the representative of NT Trading appealed to the Board against the Determination.

18. By a decision dated 9 December 2008 ("**Board Decision**"), the Board dismissed NT Trading's appeal and upheld the Determination under sections 16(1), 17(1)(b) and 61A of the Ordinance [Item 6].

19. NT Trading then sought to appeal by way of case stated pursuant to section 69 of the Ordinance. On 16 January 2009, the Board replied that the questions formulated by NT Trading were unparticularised and did not identify questions of law that at that stage the Board was prepared to state. By a letter dated 30 March 2009, the legal representative of NT Trading asked the Board to confirm whether or not it was willing to state any questions for the opinion of the Court of First Instance. On 15 April 2009, before receiving the Board's reply, NT Trading applied to the Court of First Instance in HCAL 40/2009 for leave to apply for judicial review of the Board's "de facto refusal" to state a case.

20. On 22 April 2009, the Board issued its decision and declined to state a case on the ground that the questions formulated by NT Trading were not proper questions of law [Item 7].

21. Leave to apply for judicial review in HCAL 40/2009 was refused by the Court of First Instance on 23 April 2009 without a hearing. NT Trading then appealed to the Court of Appeal (CACV *114/2009*). The appeal was dismissed by the Court of Appeal's judgment of 14 October 2009. No further appeal was lodged by NT Trading.

Winding-up of NT Trading (HCCW 193/2011)

22. According to NT Trading's audited accounts for the year ended 31 December 2003, the company disposed its entire interest in NTSZ to a fellow subsidiary during the year and then ceased its trading business. Regarding the Profits Tax payable as determined by the Deputy Commissioner and upheld by the Board Decision (paragraph 16 above), NT Trading failed to pay any of the tax payable as stated in paragraph 16 above despite repeated demands and enforcement actions.

23. In or around June 2011, the Commissioner petitioned for the winding-up of NT Trading by reason of the unpaid tax. The petition was heard on 13 March 2012, and judgment of the Court was handed down on 4 June 2012 ordering NT Trading be wound up.

Discrepancies

24. The discrepancies between the profits or loss as stated in the returns signed by the Appellants (paragraphs 8 and 9 above), and the assessable profits for each relevant year of assessment as determined in the Determination and upheld by the Board Decision and tax undercharged are tabulated as follows:

Discrepancies

Year of Assessment	Total Assessable Profits $	Assessable Profits (Loss) reported $	Amount of Discrepancy S	% of profits understated to total Assessable Profits
1996/97	46,632,080	9,889,250	36,742,830	78.79%
1997/98	43,458,129	8,667,488	34,790,641	80.06%
1999/2000	36,694.629	(3,803,183)	40,497,812*	110.36%
Total	126,784,838	14,751,555	1 12,031,283	

*For the year of assessment 1999/2000, the amount of discrepancy comprises of profits understated $36,694,629 and loss over-claimed $3,803,183

Tax Undercharged

Year of Assessment	Total Tax Payable $ $	Tax already charged $ $	Tax Undercharged $ S	% of tax undercharged to total tax payable
1996/97	7,694,293	1,631,726	6,062,567	78.79%

Year of Assessment	Total Tax Payable $	Tax already charged $	Tax Undercharged $	% of tax undercharged to total tax payable
	$	$	S	
1997/98	6,453,532	1,287,121	5,166,411	80.06%
1999/2000	5,871,140	0	5,871,140	100%
Total	20,018,965	2,918,847	17,100,118	

Additional Tax under section 82A

25. On 17 January 2011, the Commissioner gave notices ("**the Notices**") [Item 8] to the 1st Appellant and 2nd Appellant respectively under section 82A(4) of the Ordinance that he intended to assess the 1st Appellant to Additional Tax for making incorrect returns in respect of NT Trading by understating its profits and overclaiming its losses for the years of assessment 1996/97 and 1999/2000 and to assess the 2nd Appellant to Additional Tax for making incorrect return in respect of NT Trading by understating its profits for the year of assessment 1997/98.

26. No prosecution under sections 80(2) or 82(1) of the Ordinance has been instituted in respect of the incorrect returns filed by NT Trading.

27. On 16 February 2011, the Appellants, via their former tax representative, BDO Tax Limited ("**BDO**"), submitted written representations to the Commissioner [Item 12]. Further representations for the 1st Appellant were made in 13DO's letters of 25 February 2011 [Item 13], 13 May 2011 [Item 15] and 30 June 2011 [Item 16], and for the 1st Appellant, or the Appellants, in the letters of the new tax representative, ECOVIS David Yeung Hong Kong ("**ECOVIS**") of 3 September 2012 [Item 28], 1 February 2013 [Item 40], 18 February 2013 [Item 41] and 8 March 2013 [Item 42].

28. On 14 April 2011, the Appellants filed a notice of application for leave to apply for judicial review *(HCAL 24/2011)* to challenge the Commissioner's decision to issue the Notices to the Appellants.

29. Before the application was considered by the Court, the Appellants filed a notice of discontinuance of the application for leave to apply for judicial review on 27 June 2011.

30. Having considered all the written representations and submissions, the Commissioner made the Additional Tax assessments referred to in paragraph 1 above which were issued to the Appellants on 26 April 2013 [Item 47].

31. On 24 May 2013, Wilkinson & Grist, on behalf of the Appellants, appealed to the Board against the assessments to Additional Tax.

32. On 22 July 2013, the Appellants filed a Notice of Application for Leave to Apply for Judicial Review in relation to the Commissioner's decision to issue the said assessments of Additional Tax *(HCAL 112/2013).* The said application for leave was

refused by the High Court on 21 August 2013 after an oral *ex parte* hearing.

33. On 2 September 2013, the Appellants issued Notice of Appeal appealing against the refusal *(CACV 182/2013).* The appeal was heard by the Court of Appeal on 30 May 2014, and the appeal was dismissed on the same day after the hearing (the attendance by the Commissioner was excused). Written Reasons for Judgment were handed down by the Court of Appeal on 9 June 2014.

Dated this 15th day of December 2014.

Government Counsel for the Commissioner of Inland Revenue	Messrs Baker & McKenzie, Solicitors for the 1st and 2nd Appellants