Case No. D10/98

Additional tax – late filing of tax return – submission of parties – reasonable excuse – automatic block extension – Departmental Code – sections 18D, 51(1), 80(2)(d) and 82A(1) and (4) of the Inland Revenue Ordinance.

Panel: Christopher Chan Cheuk (chairman), Edward Chow Kam Wah and Mathew Ho Chi ming.

Date of hearing: 24 January 1998.
Date of decision: 8 April 1998.

The taxpayer, a partnership, commenced business in Hong Kong in 1990. Its account was closed on the 31 July in each year. On 1 April 1996 the Commissioner issued a profits tax return for the year of assessment 1995/96 under section 51(1) of the Inland Revenue Ordinance requiring the taxpayer to complete and return it within one month.

On 13 June 1996 the Commissioner wrote to the taxpayer advising that it had committed an offence under section 80(2)(d) for failing to comply with the provision of the IRO within the specified time and the Commissioner offered to compound the offence if the taxpayer agreed to pay the penalty of $1,200 when required and to submit a completed return within the next 14 days.

On 19 August 1996 the taxpayer applied for extension until October 1996 (without specifying a date) on the ground that the business had ceased operation and that there were still payments to be made in February and March 1996.

On 2 October 1996 the taxpayer's representative made further request for extension of time. The application was rejected. The taxpayer lodged the profits tax return together with the report and financial statements computed up to 31 December 1995, the date of cessation.

On 7 November 1996 the assessor made the profits tax assessments which the taxpayer did not dispute. In compliance with section 82A(4) the Commissioner gave notice to the taxpayer and stated that the tax which had been undercharged or would have been undercharged was $87,686. The taxpayer did not dispute the amount but made representation as to why it needed more time.

On 18 June 1997 the Commissioner assessed the taxpayer to an additional tax of $8,000 for the year of assessment 1995/96. The taxpayer appealed against both liability and quantum.

Held:

(1) The submission by the parties is meant to assist the Board in its reasoning and they are not facts or evidence of facts. Had the taxpayer's representative wanted to show the Board that money had not been collected or expenses not paid he should have produced the accounts and identified the different items. Otherwise the Board is left with no evidence except bare statements unless the other side has agreed as facts.

(2) It is wrong to suggest that because of contingencies a company is not able to produce true and fair accounts … even if the contingencies were of an immense magnitude, full provision could have still been made and there was no excuse not to file tax returns.

(3) The dispute or difference between the taxpayer and other parties in any event is a civil matter; it should not take precedence over the statutory obligation.

(4) For enforcement of any provision, statutory or otherwise an arbitrary cut off date has to be established. It is bound to have cases marginally falling outside the relief period and those taxpayers not applicable will feel aggrieved because of not being qualified for the relief. The taxpayer should realise that such extension is a matter of discretion or a matter of grace. There is no rule that the Commissioner is obligated to exercise it.

(5) One may query whether the taxpayer had been treated fairly and whether the taxpayer's special circumstances constitute reasonable excuse under section 82A(1). The taxpayer was first asked to file its return on 31 April 1996 and was given a chance to file within 14 days from 13 June 1996. The taxpayer took no action until 9 August 1996; it was the first time the taxpayer informed the Revenue of the cessation of its business and its difficulty. Such dilatory attitude gained no sympathy and should not be excused.

(6) It has been held in many cases that the Revenue had suffered no financial loss was not a ground for appeal against liability. It is a factor that the Board will take into consideration when deciding the quantum.

(7) Various decisions in the past have indicated that the penalty starting point for late filing of return is 10% of the tax undercharged or tax would have been undercharged if the taxpayer is a first offender, it is unintentional mistake and the Revenue has suffered no loss. There are neither aggravating factors nor mitigating ones in this case. The Commissioner's assessment of additional tax of $8,000 which is equivalent to 9.12% is slightly edged on the lenient side. The taxpayer should find itself fortunate that with the evidence before us the Revenue did not request for increase and we have decided not to interfere with the Commissioner's assessment.

Appeal dismissed.

Cases referred to:

D48/89, IRBRD, vol 5, 512
D104/96, IRBRD, vol 12, 74

Leung Man Keung for the Commissioner of Inland Revenue.
Keung Ping Yin, Certified Public Accountant for the taxpayer.

Decision:

1. This is an appeal by the Taxpayer, a private education enterprise owned by several partners against the assessment made by the Commissioner of Inland Revenue on 18 June 1997 on the Taxpayer for additional tax in the sum of $8,000 for the year of assessment 1995/96 as a penalty for late filing of the return.

Proceedings

2. The Taxpayer was represented by Mr KEUNG Ping-yin, Raymond, certified public accountant ('the Tax Representative') at the hearing. A bundle of documents consisting of 32 pages was agreed by the parties and produced by consent as exhibit 'R-1'. The Tax Representative called no witness and relied on the agreed bundle for his submission.

Facts of the Case

3. Facts of the case are relatively simple and can be summarised as follows:

(a) The Taxpayer commenced business in Hong Kong in 1990 and engaged in the business of kindergarten and child care centre. Its account was closed on the 31 July in each year.

(b) On 1 April 1996 the Commissioner issued a profits tax return for the year of assessment 1995/96 under section 51(1) of the Inland Revenue Ordinance (the IRO) requiring the Taxpayer to complete and return it within one month.

(c) On 13 June 1996 the Commissioner wrote to the Taxpayer advising that it had committed an offence under section 80(2)(d) for failing to comply with the provision of the IRO within the specified time and the Commissioner offered to compound the offence if the Taxpayer agreed to pay the penalty of $1,200 when required and to submit a completed return within the next fourteen days.

(d) On 19 August 1996 it applied for extension on the ground that the business had ceased operation and that there were still payments to be made in February and March 1996. It requested for extension of time for filing the tax return until October 1996 without specifying a date (Exhibit 'R-1' page 11).

(e) On 2 October 1996 a certain Ms X wrote on behalf of the Taxpayer claiming to be its representative, made further request for extension of time and stated (Exhibit 'R-1' page 13) : *'Due to the reshuffling of our company, the business registration of the former company has been cancelled and a new name has replaced the old one. But as the unsettled payments in the accounts have yet to be figured out, we would like to apply for deferring filing the tax return to the end of this month.'*

(f) The application for extension was rejected and the Taxpayer lodged the profits tax return together with the report and financial statements prepared by Mr Raymond KEUNG and computed up to 31 December 1995, the date of cessation.

(g) On 7 November 1996 the assessor made the profits tax assessments which the Taxpayer did not dispute.

(h) In compliance with section 82A(4) the Commissioner gave notice to the Taxpayer and stated that the tax which had been undercharged or would have been undercharged was $87,686. The Taxpayer did not dispute the amount but made representation which states:

> *'the above company has ceased its operation and transferred the whole business to a new limited company on 31 December 1995. (Actually some income were received on January 1996 and some expenses were paid on April 1996). Since there are new shareholders in the new limited company, we have to separate the income and expenses between the two companies. It is very difficult for all the partners of the old company and all the shareholders of the new company to agree the value. It needs more time.'* (Exhibit 'R-1' page 29)

(i) On 18 June 1997 the Commissioner assessed the Taxpayer to an additional tax of $8,000 for the year of assessment 1995/96. It is against such assessment the Taxpayer instituted this appeal.

Appeal

4. The Taxpayer appealed against the assessment in respect of both its liability and the quantum of penalty.

Ground of Appeal

5. Mr KEUNG for the Taxpayer did not clearly formulate the grounds of appeal but Mr LEUNG for the Revenue did summarise them in his response to Mr KEUNG's submission against liability.

6. The Taxpayer's representative submitted that it ceased business on 31 December 1995 and that some of the income was not received until January 1996 and some of the expenditures were settled only in late April 1996. We have no evidence before us except the verbal submission by Mr KEUNG who argued that if his submission was not contradicted then it should be taken as true by the Board. We are not aware of such rule of evidence. Mr KEUNG has confused between the two concepts 'evidence' and 'submission'. It is our duty to consider all evidence before us and to draw such conclusion as we consider appropriate. The submission by the parties is meant to assist us in our reasoning and they are not facts or evidence of facts. Had Mr KEUNG wanted to show us that money had not been collected or expenses not paid he should have produced the accounts and identified the different items. Otherwise, we are left with no evidence except bare statements unless the other side has agreed as facts. In this case we do not think that the Revenue has agreed and we find three pieces of information which are conflicting with each other:

(a) As stated in paragraph 3(d) above the Taxpayer in August 1996 claimed that there were still payments to be made in February and March 1996;

(b) On 2 October 1996 a certain Ms X claimed there were still unsettled payments as set out in paragraph 3(e) above;

and (c) The Tax Representative asserted that some expenses were paid in April 1996.

The Board wants to know the facts and the truth. Further, we are not told the difficulty the Taxpayer was facing. Even if we are to accept what Mr KEUNG submitted was true, he was unable to resist the strong submission by Mr LEUNG on point of law. Mr LEUNG for the Revenue referred us to the decision by another Board in D48/89, IRBRD, vol 5, 512 at 516, which has held that; *'it is wrong to suggest that because of contingencies a company is not able to produce true and fair accounts … even if the contingencies were of an immense magnitude, full provision could have still been made and there was no excuse not to file tax returns.'* In our present case Mr KEUNG for the Taxpayer had failed to demonstrate to us how difficult it was to prepare the accounts and why provisions could not be made in the accounts for the return.

7. The second ground of appeal as formulated by Mr LEUNG was that because a new company was going to take over the business, the new shareholders were unable to agree with the former partners as to the value of the transfer so it needed time to sort out the differences between the parties. As on the previous point, Mr KEUNG for the Taxpayer did not produce any evidence or demonstrate to us what was the difficulty that caused the delay. Mr LEUNG for the Revenue submitted that even if what Mr KEUNG submitted was true it

did not constitute reasonable excuse for the purpose of section 82A(1) of the IRO. In a recent case B/R 104/96, IRBRD, vol 12, 74 decided by a differently constituted Board, it was held that the deadlock between the only two shareholders in the taxpayer's company which was the main cause for its failure to comply with its statutory obligation of filing the return within time was not regarded as reasonable excuse. The taxpayer in that case failed to show to the Board that it had taken any step to resolve the impasse or to comply with the statutory obligation. The Taxpayer in the present case was in similar situation. We see no reason why we should not follow such decision. The dispute or difference between the parties in any event is a civil matter; it should not take precedence over the statutory obligation.

8. The third ground of appeal involves an interesting, long established filing practice of allowing tax representatives to have automatic block extension for different classes of cases to file return in each year. Each class was given special alphabetical codes by the Department. Departmental Code 'N' was for cases with accounting date within the period of 1 April 1995 to 30 November 1995. These Code 'N' cases did not have extension. For cases with accounting date falling within the period of 1 December 1995 to 31 December 1995 they were known as Departmental Code 'D' cases which had the extension up to 31 July 1996. In the present case the Taxpayer ceased business on 31 December 1995 and according to section 18D of the IRO the accounts had to be computated up to the date of cessation. For this reason the subject case coincided with the last day of the applicable period of Code 'D' cases and the Taxpayer had to file its return on or before 31 July 1996. Mr KEUNG for the Revenue argued that the Taxpayer felt aggrieved : had the business ceased its operation a day later that is, 1 January 1996, the relief of Departmental Code 'M' cases that is, those cases having accounting date within the period from 1 January 1996 to 31 March 1996 would have applied and the time for filing of the return would have been extended to 15 November 1996 as stated in the circular letter dated 9 April 1996 from the Commissioner. First, we doubt whether such filing practice had any binding effect on the Board but definitely the Board cannot ignore such practice. For enforcement of any provision, statutory or otherwise an arbitrary cutoff date has to be established. It is bound to have cases marginally falling outside the relief period and those taxpayers not applicable will feel aggrieved because of not being qualified for the relief. The Taxpayer should realise that such extension is a matter of discretion or a matter of grace. There is no rule that the Commissioner is obliged to exercise it. The invariable fact of this case was that the Taxpayer ceased business on 31 December 1995; we cannot extend the applicable period to cover it. Nor can we treat the cessation date to be a different date, a date other than 31 December 1995. The Commissioner refused to grant relief or to extend the period; we cannot force him to change the practice or exercise his discretion in any other manner. One may query whether the Taxpayer had been treated fairly and whether the Taxpayer's special circumstances constitute reasonable excuse under section 82A(1). The Taxpayer was first asked to file its return on 31 April 1996 and was given a chance to file within 14 days from 13 June 1996. The Taxpayer took no action until 9 August 1996, which was after the extended period for Code 'D' cases; it was the first time the Taxpayer informed the Revenue of the cessation of its business and its difficulty. Such dilatory attitude gained no sympathy and should not be excused.

9. The last ground was that the Revenue had suffered no financial loss. It has been held in many cases that it was not a ground for appeal against liability. It is a factor that the Board will take into consideration when deciding the quantum.

Quantum

10. Various decisions in the past have indicated that the penalty starting point for late filing of return is 10% of the tax undercharged or tax that would have been undercharged if the taxpayer is a first offender, it is an unintentional mistake and the Revenue has suffered no loss. We find neither aggravating factors nor mitigating ones in this case. The Commissioner's assessment of additional tax of $8,000 which is equivalent to 9.12% is slightly edged on the lenient side. The Taxpayer should find itself fortunate that with the evidence before us Mr LEUNG for the Revenue did not request for increase and we have decided not to interfere with the Commissioner's assessment.

Decision

11. For reasons stated above the appeal by the Taxpayer must fail. Accordingly, the Board dismisses the appeal and upholds the assessment by the Commissioner on 18 June 1996 on the Taxpayer for additional tax in the sum of $8,000 for the year of assessment 1995/96.