Case No. D11/93

Penalty tax – profits tax – late filing of tax return after estimated assessment – quantum of penalty – section 82A of the Inland Revenue Ordinance.

Panel: William Turnbull (chairman), Rowdget W Young and Jack Samuel Yuen.

Date of hearing: 4 March 1993.
Date of decision: 7 June 1993.

The taxpayer was a limited liability company which was late in filing its profits tax return for the year of assessment 1990/91. The assessor on 29 November 1991 issued an estimated assessment. The taxpayer lodged its profits tax return in March 1992. The amount of the tax disclosed in the return was a little more than the estimated assessment. Subsequently the Commissioner imposed a penalty of approximately 20% of the amount of tax involved. The taxpayer appealed to the Board of Review on the ground that the amount of the penalty was excessive. The reason given for the delay was that the managing director of the taxpayer had been away from Hong Kong on business on behalf of the taxpayer and it had not been possible to finalise the accounts. It was pointed out that the amount of the profits returned by the taxpayer was not very much higher than the estimated assessment.

Held:

The issuance of an estimated assessment does not mitigate the circumstances of the filing of a late tax return and it is not material to take into account the quantum of the estimated assessment. The managing director of the taxpayer had made a decision that the business affairs of the taxpayer were more important than its taxation affairs. A penalty of 20% of the amount of tax involved was at the top end of the range for a case of this nature but was not excessive.

Appeal dismissed.

Cases referred to:

D61/90, IRBRD, vol 5, 444
D2/88, IRBRD, vol 3, 125
D1/82, IRBRD, vol 1, 407
D53/88, IRBRD, vol 4, 10
D33/89, IRBRD, vol 4, 359

Woo Sai Hong for the Commissioner of Inland Revenue.

Rayson Wong of Messrs H M Ng & Co for the taxpayer.

Decision:

This is an appeal by a private limited company against an additional tax assessment made under section 82A of the Inland Revenue Ordinance by the Commissioner. The facts are as follows:

1. The Taxpayer was incorporated in Hong Kong in late 1982.

2. In default of receiving a duly completed profits tax return for the year of assessment 1990/91, the assessor on 29 November 1991 issued an estimated assessment on the Taxpayer in the sum of $4,030,000. No objection was lodged against this assessment.

3. On 9 March 1992 the tax representative for the Taxpayer lodged a profits tax return dated 18 February 1992 showing assessable profits of $4,166,172 for the year of assessment 1990/91.

4. On 14 April 1992 the assessor raised an additional assessment on the Taxpayer in the sum of $136,172 being the difference between the returned profits and the estimated profits in respect of the year of assessment 1990/91. No objection was lodged against this additional assessment.

5. On 27 August 1992 the Commissioner gave notice to the Taxpayer under section 82A that he proposed to assess the Taxpayer to additional tax by way of penalty in respect of the year of assessment 1990/91 because the Taxpayer had failed to file its tax return on time.

6. On 18 September 1992 the tax representative made a submission on behalf of the Taxpayer to the Commissioner.

7. On 18 November 1992 the Commissioner after having considered and taken into account the representations issued a notice of assessment for additional tax under section 82A in respect of the year of assessment 1990/91 in the sum of $140,000.

8. On 11 December 1992 the Taxpayer gave notice of appeal to the Board of Review against the assessment for additional tax issued under section 82A of the Inland Revenue Ordinance.

At the hearing of the appeal the tax representative for the Taxpayer duly appeared and submitted that this was not a tax evasion case. He said that the delay was only a few months and had been caused by extraordinary circumstances. He submitted that the penalty was excessive in the circumstances. He said that the delay had been caused by the managing director of the Taxpayer who had spent most of his time away from Hong Kong because he was very busy visiting customers, clients, and vendors of the Taxpayer. He submitted copies of the relevant pages of the passport of the managing director showing that he had travelled very frequently through the period August 1991 to February 1992 inclusive. The representative said that during the absence of the managing director the accounting and auditing matters of the Taxpayer could not be solved. He said that the profits tax return had been filed in early March 1992 and so was only about three months late. He pointed out that the difference between the profits returned by the Taxpayer and the estimated assessment was only approximately $140,000. He said that in the light of the foregoing facts the penalty was excessive. He said that the accounting records of the Taxpayer had been given to the auditors in October 1991 and that it took a few months to audit the accounts of a company of this size. He said that most of the customers of the Taxpayer were in China and that is why the managing director had to travel frequently to China. He said that the turnover of the Taxpayer had increased from $9,000,000 in its first year of business to a current turnover of $78,000,000.

The representative for the Commissioner submitted that the penalty was not excessive in the circumstances and was just over 20% of the amount of tax involved. He referred us to the following Board of Review decisions:

D61/90, IRBRD, vol 5, 444
D2/88, IRBRD, vol 3, 125
Dl/82, IRBRD, vol 1, 407
D53/88, IRBRD, vol 4, 10
D33/89, IRBRD, vol 4, 359

The Inland Revenue Ordinance imposes clear obligations upon taxpayers regarding the filing of returns. It also imposes severe penalties upon those who fail to fulfil their obligations.

A penalty of just over 20% of the amount of tax involved is quite high but we are not able to say that it is excessive when the circumstances are taken into account.

First of all we would like to make it quite clear that the issuing by the Inland Revenue Department of an estimated assessment does not mitigate the circumstances of a taxpayer being late in filing a tax return. Furthermore the amount of the estimated assessment is not material and not to be taken into account when assessing penalties. The Inland Revenue Ordinance makes it quite clear that penalties are to be assessed on the full amount of the tax involved. The tax involved is defined as being the amount of tax which would have been undercharged if the failure to file the tax return had not been detected (section 82A(l)(ii)). The fact that the assessor did find out that the tax return had not been duly filed and decided to impose an estimated assessment is not material.

Turning now to the quantum of the penalty in the circumstances of the case before us it is clear to us that the managing director made a business decision. He decided that it was more important to spend time visiting customers, clients, and vendors of his company than it was in filing the tax return for the company. We have no doubt that the managing director could have caused his company to file its tax return without delay had he so wished. Those who decide that their obligations under the Inland Revenue Ordinance are of a low priority must recognise that the consequence of their action or inaction may lead to very substantial financial penalties being imposed upon them or their company.

A penalty of 20% of the amount of tax involved is a substantial penalty and is probably at the top end of the range for a case of this nature but we cannot say that in the circumstances the amount is excessive. Accordingly we dismiss this appeal and confirm the assessment which the Taxpayer has appealed.