

**Case No. D15/09**

**Penalty tax** – late in submitting tax return – duty to perform the Board’s ultimate function – sections 51(1), 51C, 59(3), 68, 80(2), 82(1), 82A and 82B of the Inland Revenue Ordinance (‘IRO’).

**Costs** – frivolous and vexatious – sections 82B(3) and 68(9) of the Inland Revenue Ordinance (‘IRO’).

Panel: Kenneth Kwok Hing Wai SC (chairman), D’ ALMADA REMEDIOS Ng, Lisa Wei Min and Fong Ho Yin.

Date of hearing: 8 May 2009.

Date of decision: 25 May 2009.

The appellant was late in submitting its profits tax return for the year of assessment 2004/05 in relation to which the Commissioner, apart from issuing a letter to the appellant stating that any further offence of this nature would not be treated so leniently, took no action against the appellant. The appellant was again late in submitting its profits tax return for the 2007/08 year of assessment. The Commissioner assessed the appellant to additional (or penalty) tax in the sum of \$20,000 which was equivalent to 0.018% of the tax which would have been undercharged if the failure to submit the profits tax return by the due date had not been detected. The appellant appealed. The grounds of appeal of the appellant was that the account team of their [a named country] office just started to handle the set of account of [a named] business in mid-2007 and it took the appellant extra time to co-ordinate and obtain all necessary information for issuance of audited financial statement for 2007. The appellant had no intention to delay the return filing or tax payment and given their clean past record and that they settled the tax payment on-time, it was hoped that the penalty of \$20,000 for the late submission of their return for the year of assessment 2007/08 could be waived. No evidence was adduced by the appellant to substantiate any of the factual assertions in the grounds of appeal.

**Held:**

1. The asserted factual basis in the grounds of appeal, even if established, did not constitute any reasonable excuse. The appellant had a statutory duty under section 51C to keep sufficient records in the English or Chinese language of its income and expenditure to enable the assessable profits of its business *to be readily*

(2009-10) VOLUME 24 INLAND REVENUE BOARD OF REVIEW DECISIONS

*ascertained.* The appellant knew as early as mid-2007 that its overseas accounting team was new. If it had any or any real intention to file its profits tax return on time, it should have taken proper and effective steps since mid-2007 to put its house in order. The Board concludes that the appellant had no reasonable excuse and was liable to be assessed to additional tax.

2. None of the points raised in the grounds of appeal is a mitigating factor having regard to the circumstances in this case: the appellant had plainly not exercised due diligence and its attitude was clearly cavalier; no intention to delay tax payment and payment of tax on time are different duties; 'Clean past record' is an *untrue* assertion. Whether to assess a taxpayer to additional tax and, if the answer is in the affirmative, the amount of additional tax to be assessed, are matters for the Commissioner. However, if the taxpayer chooses to appeal, the Board must perform its 'ultimate function' to 'confirm, reduce, increase or annul the assessment' appealed against. It is a basic sentencing principle that repeat offenders should, in general, receive a higher penalty than first offenders. For the 2004/05 year of assessment, the Commissioner let the taxpayer off with a warning. This has proved to be ineffective in encouraging the appellant to comply with its reporting duties. For the additional tax under appeal, the Commissioner saw her way to be exceptionally lenient. This has also proved ineffective, whether as a punishment or a deterrent. The appellant responded by choosing to waste the resources of the Revenue and of the Board in pursuing this wholly unmeritorious appeal to its conclusion. Neither the Chairman nor the members of the panel hearing this appeal recalls having come across a penalty as exceptionally lenient as the 0.018% in this case. The Board has not been told of any system put in place by the appellant to ensure compliance in future. The apology from the appellant's finance and accounting senior supervisor to the Revenue sounded insincere and had a hollow ring. She insisted that she had a right of appeal. This the Board agrees. However, the right of appeal brings with it the Board's duty to perform its ultimate function and its discretion to order costs. In the circumstances of this case, the Board would not have considered it excessive if the Commissioner had imposed a penalty in the 10% - 20% range. For reasons given above, the Board considers the 0.018% to be woefully inadequate. In view of the exceptional leniency on the part of the Commissioner, the Board's decision is that the additional tax should be **increased from \$20,000 to \$1,000,000** under sections 82B(3) and 68(8)(a), which is slightly less than 1%.
3. The Board considers this appeal to be frivolous and vexatious. It sees no reason why the compliant taxpayers should bear the costs of such a waste of public resources. Pursuant to sections 82B(3) and 68(9), the Board **orders** the appellant to pay the sum of **\$5,000 as costs** of the Board.

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

Cases referred to:

- D25/97, IRBRD, vol 12, 204
- D134/00, IRBRD, vol 16, 10
- D118/02, IRBRD, vol 18, 90
- D10/03, IRBRD, vol 18, 351
- D67/03, IRBRD, vol 18, 681
- D94/03, IRBRD, vol 18, 886
- D63/04, IRBRD, vol 19, 512
- D77/04, IRBRD, vol 19, 597
- D50/06, (2006-07) IRBRD, vol 21, 888
- D57/06, (2006-07) IRBRD, vol 21, 1061
- D34/07, (2007-08) IRBRD, vol 22, 797
- Commissioner of Inland Revenue v Nina T H Wang [1993] 1 HKLR 7

Taxpayer represented by its finance and accounting senior supervisor, tax manager and tax supervisor.

Lam Wai Hing and Ong Wai Man for the Commissioner of Inland Revenue.

**Decision:**

**Introduction**

1. The appellant was late in submitting its profits tax return for the 2004/05 year of assessment. The Commissioner of Inland Revenue ('the Commissioner') issued a notice under section 82A(4) of the Inland Revenue Ordinance, Chapter 112, ('the Ordinance'). After considering the appellant's representations, the Commissioner wrote to the appellant by letter dated 4 July 2006 stating that she had decided that no action would be taken on that occasion and that any further offence of that nature would not be treated so leniently.

2. 2 years later, the appellant was again late in submitting its profits tax return. After considering the appellant's representations, the Commissioner assessed the appellant to additional (or penalty) tax in the sum of \$20,000 which was equivalent to 0.018% of the tax which would have been undercharged if the failure to submit the profits tax return by the due date had not been detected. The appellant reported assessable profits of over \$625,000,000 which was accepted by the assessor to be correct and the appellant was assessed to profits tax as per return in a sum in excess of \$109,000,000.

(2009-10) VOLUME 24 INLAND REVENUE BOARD OF REVIEW DECISIONS

3. After the appellant's finance and accounting senior supervisor had concluded her submissions, we asked her to address us on whether we should:

- (1) increase the additional tax appealed against; and
- (2) order the appellant to pay the costs of the Board of Review.

After she had finished addressing us, we told the parties that we were not calling on the respondent and that we would give our Decision in writing which we now do.

**The agreed facts**

4. The parties agreed with the facts in the 'Statement of Facts' and we find them as facts.

5. The appellant has appealed against the imposition of additional tax by way of penalty assessed upon it on 4 February 2009 under section 82A of the Ordinance for the failure to comply with the requirement of a notice under section 51(1) of the Ordinance to furnish a profits tax return ('the Return') for the year of assessment 2007/08 within the prescribed time allowed.

6. Particulars of the appellant's delay in filing the Return and the additional tax by way of penalty are as follows:

Year of assessment	2007/08
Date of issue of Return	1 April 2008
Extended due date for filing Return	25 August 2008
Date of receipt of Return	3 October 2008
Period of delay in filing Return	39 days
Tax undercharged	\$109,368,898
Additional tax by way of penalty	\$20,000
Percentage of additional tax on tax undercharged	0.018%

7. The appellant is a private company incorporated in Hong Kong on 12 December 1986. It closes its accounts annually on 31 December.

8. The appellant's principal business activities as reported in its profits tax returns for the years of assessment 2004/05 to 2007/08 were as set out in the agreed Statement of Facts:

Year of assessment 2004/05

'[Details set out in the agreed Statement of Facts]'

Years of assessment 2005/06 to 2007/08

(2009-10) VOLUME 24 INLAND REVENUE BOARD OF REVIEW DECISIONS

‘[Details set out in the agreed Statement of Facts]’

9. (a) On 1 April 2008, the Commissioner issued a notice for filing profits tax return for the year of assessment 2007/08 to the appellant. The appellant was required to complete and submit the return within one month from 1 April 2008.
- (b) By reason of a Block Extension Scheme for lodgement of 2007/08 profits tax returns, which applied to the appellant, the due date for filing the tax return was extended to 22 August 2008 (Friday). As a gale warning was in force on 22 and 23 August 2008, the due date was further extended to 25 August 2008 (Monday) (‘extended due date’).
- (c) By a letter dated 22 August 2008, a leading firm of certified public accountants who audited the appellant’s financial statements submitted a request for extension of time to file the profits tax return for the year of assessment 2007/08 on behalf of the appellant. The assessor rejected the request on 28 August 2008.
- (d) The appellant did not submit its profits tax return by the extended due date.

10. On 5 September 2008, the assessor raised on the appellant an estimated assessment for the year of assessment 2007/08 pursuant to section 59(3) of the Ordinance as follows:

Estimated assessable profits	\$897,150,000
Tax thereon	\$156,976,250

11. On 3 October 2008, the appellant objected against the estimated assessment and submitted its profits tax return for the year of assessment 2007/08 together with the tax computation and financial statements for the year ended 31 December 2007, reporting assessable profits of \$625,107,992. The Auditor’s Report was signed on 3 October 2008. The financial statements were approved and authorised for issue by the appellant’s Board of Directors on the same day (i.e. on 3 October 2008).

12. On 17 October 2008, the assessor accepted the appellant’s objection and issued a revised assessment for the year of assessment 2007/08 as follows:

Revised assessable profits	\$625,107,992
Tax thereon	\$109,368,898

(2009-10) VOLUME 24 INLAND REVENUE BOARD OF REVIEW DECISIONS

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

14. On 31 December 2008, the Commissioner issued a notice of intention to assess additional tax given under section 82A(4) of the Ordinance ('the Notice') to the appellant in respect of its failure to furnish a profits tax return for the year of assessment 2007/08 within the prescribed time allowed. If the Department had not detected the failure, tax amounting to \$109,368,898 would have been undercharged. The Notice stated that a penalty by way of additional tax up to three times the amount of tax that would have been undercharged might be imposed. The appellant was invited to submit written representations to the Commissioner.

15. By a letter dated 14 January 2009, the appellant made representations to the Commissioner in response to the Notice.

16. On 4 February 2009, the Commissioner, having considered the representations, assessed the appellant to additional tax by way of penalty under section 82A of the Ordinance in the amount of \$20,000.

17. By a letter dated 25 February 2009, the appellant filed a notice of appeal to the Clerk to the Board of Review ('the Clerk') against the assessment to additional tax by way of penalty.

18. (a) The appellant had previously failed to submit its profits tax return for the year of assessment 2004/05 within the time stipulated and details are as follows:

Date of issue of 2004/05 tax return	1 April 2005
Extended due date for filing the return	15 August 2005
Date of receipt of the return	6 September 2005
Period of delay in filing the return	22 days
Tax undercharged	\$18,483,180

(b) In relation to the appellant's late filing of its profits tax return for the year of assessment 2004/05, the Commissioner issued a notice under section 82A(4) of the Ordinance to it on 13 April 2006. By two letters dated 27 April 2006 and 9 June 2006, the appellant submitted representations to the Commissioner.

(c) Having considered the representations, the Commissioner decided not to take penalty action against the appellant on that occasion. A letter was issued to the appellant on 4 July 2006 warning that any further offence of this nature would not be treated so leniently.

(2009-10) VOLUME 24 INLAND REVENUE BOARD OF REVIEW DECISIONS

19. The appellant has subsequently filed its profits tax returns for the years of assessment 2005/06 and 2006/07 on the respective due dates.

**Grounds of appeal**

20. By letter dated 25 February 2009, the appellant's finance manager gave notice of appeal on behalf of the appellant on the following grounds:

‘As mentioned in our letter dated 14 January 2009 (enclosed for your easy reference), the accounting team of our [a named country] office just started to handle the set of account of [a named] business in mid-2007. As the new team is new to our [named] business, it took us extra time to co-ordinate and obtain all necessary information for issuance of audited financial statements for 2007. Please be advised that we did the return filing immediately after the issuance of audited financial statements for 2007 and we have no intention to delay the return filing or tax payment. Given our clean past record and we settled the tax payment on-time, we sincerely hope that the penalty of HK\$20,000 for late submission of the [appellant's] return for the year of assessment 2007/08 could be waived.’

**Bundle of authorities sent by the Revenue**

21. Under cover of her letter dated 21 April 2009, the assessor sent a bundle of the following authorities to the Clerk and to the appellant:

1. Inland Revenue Ordinance, Chapter 112, sections 51, 51C, 68, 82A, 82B and Schedule 5 Part I;
2. D25/97, IRBRD, vol 12, 204;
3. D134/00, IRBRD, vol 16, 10;
4. D118/02, IRBRD, vol 18, 90;
5. D10/03, IRBRD, vol 18, 351;
6. D67/03, IRBRD, vol 18, 681;
7. D94/03, IRBRD, vol 18, 886;
8. D63/04, IRBRD, vol 19, 512;
9. D77/04, IRBRD, vol 19, 597;
10. D50/06, (2006-07) IRBRD, vol 21, 888;
11. D57/06, (2006-07) IRBRD, vol 21, 1061; and
12. D34/07, (2007-08) IRBRD, vol 22, 797.

**The hearing**

22. The appellant sent 3 relatively junior staff in its accounting and tax departments to attend the hearing on its behalf. They were the appellant's finance and accounting senior supervisor,

(2009-10) VOLUME 24 INLAND REVENUE BOARD OF REVIEW DECISIONS

tax manager and tax supervisor. No witness was called and no legal authority was furnished or cited and no reference was made to any of the authorities included in the assessor's bundle of authorities. The finance and accounting senior supervisor argued the case along the lines of the grounds of appeal.

23. The respondent was represented by a senior assessor and an assessor. As we said in paragraph 3 above, we did not call on the respondent.

**The relevant statutory provisions**

24. Section 51(1) of the Ordinance provides that:

*'An assessor may give notice in writing to any person requiring him within a reasonable time stated in such notice to furnish any return which may be specified by the Board of Inland Revenue for ... profits tax ... under Parts ... IV ...'*

25. Section 51C(1) provides that:

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

26. Section 59(3) provides that:

*'Where a person has not furnished a return and the assessor is of the opinion that such person is chargeable with tax, he may estimate the sum in respect of which such person is chargeable to tax and make an assessment accordingly, but such assessment shall not affect the liability of such person to a penalty by reason of his failure or neglect to deliver a return.'*

27. Section 68(4) provides that:

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

28. Section 68(8)(a) provides that:



(2009-10) VOLUME 24 INLAND REVENUE BOARD OF REVIEW DECISIONS

*'After hearing the appeal, the Board shall confirm, reduce, increase or annul the assessment appealed against or may remit the case to the Commissioner with the opinion of the Board thereon.'*

29. Section 68(9) provides that:

*'Where under subsection (8), the Board does not reduce or annul such assessment, the Board may order the appellant to pay as costs of the Board a sum not exceeding the amount specified in Part I of Schedule 5, which shall be added to the tax charged and recovered therewith.'*

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

30. Section 82A(1)(d) provides that:

*'Any person who without reasonable excuse ... fails to comply with the requirements of a notice given to him under section 51(1) ... shall, if no prosecution under section 80(2) or 82(1) has been instituted in respect of the same facts, be liable to be assessed under this section to additional tax of an amount not exceeding treble the amount of tax which ... (ii) has been undercharged in consequence of the failure to comply with a notice under section 51(1) ... or which would have been undercharged if such failure had not been detected.'*

31. Section 82B(2) and section 82B(3) provide that:

*'(2) On an appeal against assessment to additional tax, it shall be open to the appellant to argue that-*

- (a) he is not liable to additional tax;*
- (b) the amount of additional tax assessed on him exceeds the amount for which he is liable under section 82A;*
- (c) the amount of additional tax, although not in excess of that for which he is liable under section 82A, is excessive having regard to the circumstances.'*

*'(3) Sections 66(2) and (3), 68, 69 and 70 shall, so far as they are applicable, have effect with respect to appeals against additional tax as if such appeals were against assessments to tax other than additional tax.'*

**Liability for additional tax**

32. On the admitted facts, the appellant had failed to file its profits tax return by the extended due date.

33. The appellant's finance and accounting senior supervisor adduced no evidence to substantiate any of the factual assertions in the grounds of appeal. There is thus no factual basis for any reasonable excuse.

34. Further and in any event, the asserted factual basis, even if established, did not constitute any reasonable excuse. The appellant had a statutory duty under section 51C to keep sufficient records in the English or Chinese language of its income and expenditure to enable the assessable profits of its business *to be readily ascertained*. The appellant knew as early as mid-2007 that its overseas accounting team was new. If it had any or any real intention to file its profits tax return on time, it should have taken proper and effective steps since mid-2007 to put its house in order. The appellant had December year ends and by the extended due date, it had more than 7 ½ months since 31 December 2007 to finalise its audited financial statements and tax computations and to submit the profits tax return. Failure to do so evidences its disrespect for statutory duties and disregard of the Commissioner's advice or warning.

35. We conclude that the appellant had no reasonable excuse and was liable to be assessed to additional tax.

**Maximum amount of additional tax**

36. It is an agreed fact that the tax which would have been undercharged was over \$109,000,000. 3 times that is over \$327,000,000.

37. The additional tax of \$20,000 as assessed by the Commissioner did not exceed the amount for which the appellant was liable under section 82A.

**Whether additional tax excessive**

38. None of the points raised in the grounds of appeal<sup>1</sup> is a mitigating factor having regard to the circumstances in this case:

- (1) New accounting team – We repeat paragraph 34 above.
- (2) No intention to delay the return filing – The relevant issue is whether the appellant intended to file its profits tax return on time and whether it had exercised due diligence in complying with its reporting duties. In the

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<sup>1</sup> See paragraph 20 above.

circumstances of this case, the appellant had plainly not exercised due diligence and its attitude was clearly cavalier.

- (3) No intention to delay tax payment and payment of tax on time – Payment of tax is a different duty. If the appellant should default in payment of tax, it would be dealt with by the Revenue's enforcement section.
- (4) Clean past record – This is an *untrue* assertion. The appellant's finance and accounting senior supervisor offered no explanation why the appellant had made an untrue assertion in its grounds of appeal.
- (5) Waiver of penalty – We reject this request. The Revenue issued an estimated assessment in view of the failure of the appellant to file its profits tax return on time and revised it as per return which was submitted out of time. We see no reason why compliant taxpayers should bear the administrative costs. We shall return to this in paragraph 41 below.

### **Increasing the additional tax**

39. Whether to assess a taxpayer to additional tax and, if the answer is in the affirmative, the amount of additional tax to be assessed, are matters for the Commissioner. It is entirely up to the Commissioner if she should consider it appropriate to be exceptionally lenient in the punishment of a taxpayer who has failed to comply with its reporting duties. If the taxpayer has the wisdom and judgment to recognise an exceptionally lenient treatment by the Commissioner and pays up without further ado, that is the end of the matter and the Board does not come in at all.

40. However, if the taxpayer chooses to appeal, the Board must perform its 'ultimate function' to 'confirm, reduce, increase or annul the assessment' appealed against<sup>2</sup>.

41. It is a basic sentencing principle that repeat offenders should, in general, receive a higher penalty than first offenders. For the 2004/05 year of assessment, the Commissioner let the appellant off with a warning. This has proved to be ineffective in encouraging the appellant to comply with its reporting duties. For the additional tax under appeal, the Commissioner saw her way to be exceptionally lenient. This has also proved ineffective, whether as a punishment or a deterrent. The appellant responded by choosing to waste the resources of the Revenue and of the Board in pursuing this wholly unmeritorious appeal to its conclusion. Neither the Chairman nor the members of the panel hearing this appeal recalls having come across a penalty as exceptionally lenient as the 0.018% in this case. We have not been told of any system put in place by the appellant to ensure compliance in future. The apology from the appellant's finance and accounting senior supervisor to the Revenue sounded insincere and had a hollow ring. She insisted that she had

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<sup>2</sup> See Commissioner of Inland Revenue v Nina T H Wang [1993] 1 HKLR 7, per Fuad VP at page 23.

(2009-10) VOLUME 24 INLAND REVENUE BOARD OF REVIEW DECISIONS

a right of appeal. This we agree. However, the right of appeal brings with it the Board's duty to perform its ultimate function and its discretion to order costs.

42. In the circumstances of this case, we would not have considered it excessive if the Commissioner had imposed a penalty in the 10% - 20% range. For reasons given above, we consider the 0.018% to be woefully inadequate. In view of the exceptional leniency on the part of the Commissioner, our decision is that the additional tax should be increased from \$20,000 to \$1,000,000 which is slightly less than 1%.

**Disposition and costs**

43. We **increase** the additional tax assessment appealed against **from \$20,000 to \$1,000,000** under sections 82B(3) and 68(8)(a).

44. For reasons given above, we consider this appeal to be frivolous and vexatious. We see no reason why the compliant taxpayers should bear the costs of such a waste of public resources. Pursuant to sections 82B(3) and 68(9), we **order** the appellant to pay the sum of **\$5,000 as costs** of the Board, which \$5,000 shall be added to the additional tax as increased by us to \$1,000,000 and recovered therewith.