Case No. D17/08

Penalty tax – incorrect return – Commissioner's determination – whether involving determination of criminal charge – whether there was fair and public hearing by competent, impartial and independent tribunal established by law – access to appellate body with full jurisdiction – whether application of reverse persuasive burden on taxpayer justified derogation of presumption of innocence – finality of underlying profits tax assessment – whether return in fact incorrect – whether there was reasonable excuse – whether additional assessments excessive – participation in tax avoidance scheme

Panel: Kenneth Kwok Hing Wai SC (chairman), James Julius Bertram and Albert T da Rosa, Jr.

Dates of hearing: 24, 25, 26 January 2007 and 26, 27, 28 May 2008
Date of decision: 29 July 2008

Following an audit of the appellant's tax return and an investigation into its tax affair, the Commissioner decided to raise on the appellant profits tax assessments for the years of assessment between 1994 and 2001 after disallowing the deductions of interest expenses, bank charges and legal fees relating to a bank loan. The purported deductions were related to a tax avoidance scheme that the appellant and others had entered into. The appellant appealed to the Board against the assessments of the Commissioner. The Board dismissed the appeal in 2005 (see D84/04). The appellant appealed by way of case stated but abandoned the appeal in late 2005. The assessments thereby became final and conclusive under section 70 of the Inland Revenue Ordinance (Chapter 112).

The Commissioner made in 2006 additional tax assessments under section 82A of the Inland Revenue Ordinance for the years of assessment between 1994 and 2001 against the appellant for making incorrect returns. The additional tax assessments represented between 39% and 60% of the tax undercharged for the respective year of assessment. The appellant appealed to the Board against the additional tax assessments on the grounds that the appellant did not make an incorrect return; that the appellant had a reasonable excuse for filing the profits tax returns for the years of assessment between 1994 and 2001 on the basis it did; and that the amounts of additional tax assessed were incorrect and/or excessive having regard to the circumstances. The Board heard the appeal in January 2007.

While the Board was deliberating, the Court of Appeal handed down its judgment in Koon Wing Yee & Anor v Insider Dealing Tribunal & Anor (CACV 358, 360/2005) on 30 May 2007. The Board asked the parties to the appeal if they wished the Board to reconvene to hear any

submission as a result of the Court of Appeal judgment. The parties indicated that further submissions were necessary but preferred to await the result of the final appeal of the Koon Wing Yee case. The appellant then filed a new ground of appeal. The Board decided to schedule hearings to hear the parties on the application to amend the grounds of appeal and, if thought fit, arguments under the additional ground. The appellant then substituted its proposed additional ground of appeal, which now contended that in the light of the principles set out in the Koon Wing Yee case, the Commissioner should have treated the assessment of additional tax under section 82A of the Inland Revenue Ordinance as involving the determination of a "criminal charge" within the meaning of Article 11 of the Hong Kong Bill of Rights and Article 39 of the Basic Law of the HKSAR and therefore applied a "criminal" burden and standard of proof and, for such purposes, was not entitled to rely upon the earlier decision of the Board in 2005 or upon section 70 of the Inland Revenue Ordinance. The appellant also contended that section 82A of the Inland Revenue Ordinance was invalid by reason of breaches of Articles 10 and 11 of the Hong Kong Bill of Rights. The Commissioner objected to the proposed additional ground. The Board allowed after argument that submissions be made on human rights issues raised by the proposed additional ground and consented to the appellant relying on that ground. The Board also allowed additional evidence to be adduced on behalf of the Commissioner.

Held:

1. The Commissioner was an administrative authority and discharged administrative and not judicial functions in assessing additional tax. While the Commissioner could not be considered to satisfy the requirement of Article 10 of the Hong Kong Bill of Rights, the system in Hong Kong on additional tax was not incompatible with Article 10 so long as a taxpayer could bring any such decision affecting him or her before a judicial body that had full jurisdiction including the power to quash, in all respects, on questions of fact and law, the challenged decision. The Board was a competent, independent and impartial tribunal established by law to perform the ultimate function of deciding under the Inland Revenue Ordinance, having such full jurisdiction regarding appeals against additional tax assessment. It was not challenged that the Board or the Court of First Instance was not a tribunal offering the guarantees of Article 10; Commissioner of Inland Revenue v Loganathan [2000] 1 HKLRD 914 followed; Janosevic v Sweden (2004) 38 EHRR 473 applied. (paragraphs 118, 121, 123)

2. Proceedings under section 82A of the Inland Revenue Ordinance (Chapter 112) involved the determination of a "criminal charge" within the meaning of Article 11 of the Hong Kong Bill of Rights and Article 39 of the Basic Law of the HKSAR. However, the fact that additional tax proceedings involved a "criminal charge" for human rights purposes did not necessarily mean that all the consequences of a criminal trial applied in relation to the substance of the matter. Section 68(4) of the Inland

Revenue Ordinance applied to an appeal against an additional tax assessment under section 82B of the same and imposed on the taxpayer a reverse persuasive burden, derogating from the presumption of innocence under Article 87 of the Basic Law and Article 11(1) of the Hong Kong Bill of Rights. The derogation was justified. The HKSAR enjoys financial autonomy under Article 106 of the Basic Law but is constrained by Articles 107 and 108 to adopt a low tax policy and exercise fiscal prudence. An efficient system of taxation is important, if not crucial, to the HKSAR's financial interests. Imposing an administrative penalty with a reverse onus on appeal was a rational means of enforcing compliance with the duties to submit timely and correct tax returns and information to the Commissioner. Weight must be given to the decision of the Legislative Council to impose a reverse onus on the taxpayer, taking into account the nature of the problem addressed in the statute, and in particular, whether it involved adoption of a policy which the legislature was better placed than the court to assess. Defaults in submitting timely and correct tax returns, if not deterred and punished, put the HKSAR's fiscal system at risk. There was no contention that the burden of proving that the additional tax assessment was difficult to rebut. Even if it was, the statute provided certain means of defence based on subjective elements and it was open to the taxpayer to put forward grounds for a reduction under the excessiveness element. The reverse onus was confined within reasonable limits; Koon Wing Yee v Insider Dealing Tribunal [2008] 3 HKLRD 372; Han v Customs & Excise Commissioner [2001] 1 WLR 2253; Ferrazini v Italy [2001] STC 1314; Janosevic v Sweden (2004) 38 EHRR 473 applied; D17/72 IRBRD 97; D57/06 (2006) 21 IRBRD 1061; Mok Tsze Fung v Commissioner of Inland Revenue [1962] HKLR 258; Commissioner of Inland Revenue v Board of Review ex p Herald International Ltd [1964] HKLR 224; All Best Wishes Ltd v Commissioner of Inland Revenue (1992) 3 HKTC 750; Cheung Wah Keung v Commissioner of Inland Revenue [2002] 3 HKLRD 773; HKSAR v Lam Kwong Wai (2006) 9 HKCFAR 574; HKSAR v Ng Po On (unrep., 7 March 2008, FACC 6/2007) considered. (paragraphs 170, 171, 193, 195, 201, 208, 211)

3. Section 70 of the Inland Revenue Ordinance applied to an appeal against a penalty tax assessment. Section 70 was the provision dealing with the correctness and quantum of the underlying profits (or salaries or property) tax assessment. The necessity and rationality of enacting a provision governing the finality of a profits, salaries or property tax assessment was obvious; the HKSAR should be in a position to budget and use its financial resources without fear that profits (or salaries or property) tax assessments may be re-opened years down the line. In the present case, the question whether section 70 applied was academic and if it was not, the section applied and it was not open to the appellant to re-open the issues on the correctness and quantum of the underlying profits tax assessment; Weson Investment Ltd v Commissioner of Inland Revenue [2007] 2 HKLRD 568; D5/07 (2007-08) 22

IRBRD 245; Khan v Customs and Excise Commissioners [2006] STC 1167 followed. (paragraphs 216, 220, 225)

4. The appellant had filed incorrect returns of profits tax in the years of assessment in question. The previous decision of the Board had decided against the appellant on the question of whether the deductions were allowable and that decision was final and conclusive under section 69 of the Inland Revenue Ordinance. Whether a return was incorrect was a question of fact, not a question of belief or opinion. Common belief, even if established, was irrelevant. By virtue of the Board's previous decision and the agreed facts in the present appeal, the appellant had clearly not reported correct amounts of assessable profits. Section 51(1) of the Ordinance did not and does not provide for the filing of a profits tax return by a taxpayer "in accordance with the provisions of Part IV"; Newton v Commissioner of Taxation [1958] AC 450; D40/88 3 IRBRD 377 considered. (paragraphs 236, 237, 245, 246, 247)

5. In deciding whether a taxpayer had a reasonable excuse for filing an incorrect return, the approach was not to decide what a reasonable person would do or would omit to do. Rather, the taxpayer must identify and prove an excuse on the actual facts of the case and the Board must be satisfied that that excuse was reasonable. (paragraphs 263, 264, 268)

6. The appellant failed to establish a reasonable excuse for filing incorrect returns. In so far as it was suggested that the appellant relied on the advices of an accounting firm, the advices given were in fact non-committal and somewhat wishy-washy, with the accounting firm refraining from expressing any view on the applicability of section 61A of the Inland Revenue Ordinance. There was no evidence of reliance. Even if the appellant did rely on the advices of the accounting firm, such excuse of reliance was not a reasonable excuse. The least the appellant should have done was to seek an advance ruling, which was premised upon full and frank disclosure to the Commissioner. Acting on advices on the tax scheme which depended on concealment, or not giving the Commissioner full and frank disclosure, for its success did not constitute a reasonable excuse. (paragraphs 275, 289, 292, 293, 295, 298, 299)

7. If tax avoidance schemes fail, there is no reason why taxpayers should not pay a price. They must be punished and other taxpayers deterred from incorrect reporting without reasonable excuse. Where the amounts of tax involved are high, the maximum amount of additional tax will correspondingly be high in dollars. Taxpayers who chose to play with high stakes must be prepared to pay a penalty in terms of a percentage of the stack which they chose to play with. (paragraphs 313, 317)

8. The additional tax assessments were not excessive in the circumstances. The appellant entered into the tax scheme for the sole or dominant purpose of tax avoidance as a matter of choice, doing so knowingly and deliberately and in spite of warnings. The tax scheme was a complex one. By extending the repayment date by five years, the appellant deliberately continued its omission or understatement for five more years. By increasing the interest rate, the appellant deliberately increased the amounts of omission or understatement. The appellant's returns omitted or understated its assessable profits by 99.91%. Lack of intention to evade tax was not a mitigating factor. Payment of tax was not a mitigating factor. On the contrary, the Commissioner erred in being too lenient with the appellant. The present case was not a case of disclosure with full information promptly on challenge. There was some obstruction. Prevalence of a breach of statutory reporting duty calls for a deterrent penalty. Taxpayers in failed tax avoidance schemes should not have unrealistic hope for sympathy. (paragraphs 319, 320, 321, 322, 327, 328, 330, 336, 337, 338, 339)

Appeal dismissed.

Cases referred to:

D94/04, (2005-06) IRBRD, vol 20, 47
BR 80/76, IRBRD, 259
D13/85, IRBRD, vol 2, 173
D18/91, IRBRD, vol 6, 36
D14/98, IRBRD, vol 13, 153
D129/02, IRBRD, vol 18, 216
CIR v Tai Hing Cotton Mill (Development) Limited (2006) CACV 343/2005
D60/05, (2005-06) IRBRD, vol 20, 828
D52/86, IRBRD, vol 2, 314
D4/06, (2006-07) IRBRD, vol 21, 139
CIR v Howe (1977) 1 HKTC 936
Inland Revenue Commissioners v Duke of Westminster [1936] AC 1
Mullens v FC of T (1976) 135 CLR 290
Patcorp Investments Ltd v Federal Commissioner of Taxation (1976) 140 CLR 247
Lau v Federal Commissioner of Taxation (1984) 54 ALR 167
Stubart Investments Ltd v the Queen (1984) 10 DLR (4^{th}) 1
Hutchings v The Commissioners of Customs and Excise [1987] VATTR 58
The Clean Car Company Ltd v The Commissioners of Customs and Excise [1991] VATTR 234
D40/88, (1988) IRBRD, vol 3, 377
D42/89, (1989) IRBRD, vol 4, 479
D96/97, (1998) IRBRD, vol 12, 520

D26/99, (1999) IRBRD, vol 14, 288
D17/01, (2001) IRBRD, vol 16, 178
D90/01, (2001) IRBRD, vol 16, 757
D115/01, (2001) IRBRD, vol 16, 893
D118/02, (2003) IRBRD, vol 18, 90
D40/03, (2003) IRBRD, vol 18, 526
D96/03, (2004) IRBRD, vol 18, 905
D59/05, (2005-06) IRBRD, vol 20, 821
Newton v Commissioner of Taxation of the Commonwealth of Australia [1958] AC 450
Koon Wing Yee and another v Insider Dealing Tribunal and another, CACV 358 and 360 of 2005
Commissioner of Inland Revenue v HIT Finance Limited FACV No 8 & 16 of 2007
BR17/72, IRBRD, 97
Koon Wing Yee v Insider Dealing Tribunal and Another FACV No 19 of 2007
HIT Finance Limtied v CIR HCIA 14 & 15/2005
CIR v HIT Finance Limited FACV Nos. 8 & 16 of 2007
Insider Dealing Tribunal v Shek Mei-ling [1999] 2 HKCFAR 205
HKSAR v Lam Kwong Wai (2006) 9 HKCFAR 574
Leung Kwok Hung v HKSAR (2005) 8 HKCFAR 229
HKSAR v Hung Chan Wa FACC 1/2006
HKSAR v Ng Po On FACC 6/2007
R v Edwards [1975] QB 27
Han v Customs & Excise Commissioner [2001] 1 WLR 2253 (CA)
R (McCann) v Manchester Crown Court [2003] 1 AC 787 (HL)
Janosevic v Sweden (2004) 38 EHRR 473
Tse Wai Chun Paul v Solicitors Disciplinary Tribunal CACV 3174/2001
Ngai Few Fung v Cheung Kwai Heung CACV 147/2007
Medical Council of Hong Kong v Chow Siu Shek (2000) 3 HKCFAR 144
Commissioner of Inland Revenue v Loganathan [2000] 1 HKLRD 914
D57/06, (2006) IRBRD, vol 21, 1061
Tsang Yiu Kai v Insider Dealing Tribunal [2008] 1 HKC 376
R v Johnstone [2003] 1 WLR 1736
Sheldrake v DPP [2005] 1 AC 264
R v Ng Wing Keung Paul (1996) 6 HKPLR 299; [1997] HKLRD 142
D115/01, (2001) IRBRD, vol 16, 893
Khan v Customs and Excise Commissioners [2006] STC 1167
R (Federation of Technological Industries and others) v Customs and Excise Commissioners [2004] STC 1008
Wilson v First County Trust Ltd (No 2) [2004] 1 AC 816
Ozturk v Germany (1984) 6 EHRR 409
Mok Tsze Fung v The Commissioner of Inland Revenue [1962] HKLR 258
Hakansson v Sweden (1990) 13 EHRR 1

Tse Wai Chun v Solicitors Disciplinary Tribunal [2002] 3 HKLRD 712
Bryan v United Kingdom (1995) 21 EHRR 342
Attorney General of Hong Kong v Lee Kwong-kut [1993] AC 951
Ferrazzini v Italy [2001] STC 1314
R v Benjafield [2003] 1 AC 1099
Weson Investment Ltd v Commissioner of Inland Revenue [2007] 2 HKLRD 567
BR 23/75, IRBRD, 187
Yau Wah Yau v Commissioner of Inland Revenue [2006] 3 HKLR 586
China Map Limited and others v Commissioner of Inland Revenue, FACV 28-31 of 2007, 28 April 2008
Nina T H Wang v Commissioner of Inland Revenue, CACV 106 of 1991
Ing Baring Securities (Hong Kong) Limited v Commissioner of Inland Revenue [2008] 1 HKLRD 412
Commissioner of Inland Revenue v The Board of Review, exparte Herald International Ltd [1964] HKLR 224
All Best Wishes Limited v Commissioner of Inland Revenue (1992) 3 HKTC 750
Cheung Wah Keung v Commissioner of Inland Revenue [2002] 1 HKLRD 172
Cheung Wah Keung v Commissioner of Inland Revenue [2002] 3 HKLRD 773
D5/07, (2007-08) IRBRD, vol 22, 245
Chu Ru Ying v Commissioner of Inland Revenue, HCIA 7/2007
CIR v Secan Limited & another (2000) 3 HKCFAR 411
D62/96, IRBRD, vol 11, 633
D3/02, IRBRD, vol 17, 396
Chau Min Ching v Commissioner of Inland Revenue [1999] 2 HKLRD 586
D41/89, IRBRD, vol 4, 472
D53/92, IRBRD, vol 7, 446
D37/94, IRBRD, vol 9, 254
D65/00, IRBRD, vol 15, 610

For the taxpayer:
24, 25 & 26 January 2007 – Steven Rudolf Sieker of Messrs Baker & McKenzie, solicitors
26, 27 & 28 May 2008 – Johnny Mok, senior counsel, instructed by Messrs Baker & McKenzie.

For the Commissioner of Inland Revenue:
24, 25 & 26 January 2007 – Gladys Li, senior counsel, leading Stewart Wong, counsel, instructed by Winnie W Y Ho, senior Government counsel of the Department of Justice
26, 27 & 28 May 2008 – David Pannick, Queen' s counsel, leading Stewart Wong, instructed by Richard Fawls, senior assistant law officer (civil law) and Winnie W Y Ho, senior Government counsel of the Department of Justice.

Decision:

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INTRODUCTION

1. In October and November 1992, the appellant and other participants entered into a tax scheme. The appellant did so for the sole or dominant purpose of avoiding its liability to pay profits tax on the rental income or reducing the amount of tax payable on such rental income.

2. The appellant deducted interest expenses, bank charges and legal fees incurred in respect of a loan from Bank A and reported the following profits/losses in its tax returns:

Year of assessment	Date of receipt by the Revenue	Assessable profits/ (adjusted loss)
		$
1992/93	17-8-1993	(13,356,822)
1993/94	22-7-1994	828,427[1]
1994/95	31-7-1995	490,892
1995/96	31-7-1996	(18,120,874)
1996/97	31-7-1997	(17,962,154)
1997/98	30-7-1998	(25,562,646)
1998/99	21-3-2001	(52,683,453)
1999/2000	21-3-2001	(68,483,142)
2000/01	30-8-2001	(67,992,935)

3. On 15 February 2001, the assessor commenced an audit on the appellant's tax return for the year of assessment 1997/98 and also an investigation into the tax affairs of the appellant.

4. The Assistant Commissioner of Inland Revenue, having examined the facts, applied sections 16, 17, 61 and/or 61A of the Inland Revenue Ordinance, Chapter 112 ('the Ordinance'), and raised on the appellant the following profits tax assessments after disallowing the interest expenses, bank charges and legal fees in relation to the bank loan:

Year of assessment	Date of assessment	Assessable profits
		$
1994/95	30-3-2001	106,684,272
1995/96	13-3-2002	88,032,798
1996/97	19-7-2002	88,191,218
1997/98	19-7-2002	86,889,467
1998/99	19-7-2002	85,310,519
1999/2000	19-7-2002	69,475,699
2000/01	19-7-2002	69,966,325

[1] In the profits tax computation, $320,229, being the amount of industrial building allowance overclaimed for 1993/94, was added to arrive at a revised assessable profits of $1,148,656.

5. The appellant objected against the assessments. By a Determination dated 15 January 2004, the Commissioner determined against the appellant as follows:

Year of assessment	Assessable profits	Tax payable
	$	$
1994/95	106,683,672	17,602,805
1995/96	88,032,498	14,525,362
1996/97	88,191,218	14,551,550
1997/98	86,889,467	12,903,085
1998/99	85,310,519	13,649,683
1999/2000	69,475,699	11,116,111
2000/01	72,064,262	11,530,281
Total	596,647,335	95,878,877

6. The appellant appealed to the Board of Review against the Determination. By a decision dated 16 March 2005, D94/04, (2005-06) IRBRD, vol 20, 47, the Board [Colin Cohen, Mabel Lui Fung Mei Yee and Anthony So Chun Kung] dismissed the appeal.

7. The appellant lodged an appeal by way of case stated to the Court of First Instance but abandoned its appeal by notice dated 29 November 2005.

8. On 18 September 2006, after considering the appellant's representations, the Commissioner made the following additional tax assessments ('the Assessments') for making incorrect returns:

Year of assessment	Tax undercharged	Additional tax under section 82A	Percentage of additional tax to tax undercharged
	$	$	
1994/95	17,602,805	10,560,000	60%
1995/96	14,525,362	8,720,000	60%
1996/97	14,551,550	8,730,000	60%
1997/98	12,903,085	7,740,000	60%
1998/99	13,649,683	7,470,000	55%
1999/2000	11,116,111	5,190,000	47%
2000/01	11,530,281	4,510,000	39%
Total	95,878,877	52,920,000	55%

9. This is the appellant's appeal against the Assessments.

THE AGREED FACTS

10. The appellant and the respondent agreed the following facts set out in a Statement of Agreed Facts and we find them as facts.

11. This is an appeal by the appellant against the following assessments, all dated 18 September 2006, by the Commissioner assessing the appellant to additional tax under section 82A of the Ordinance for making incorrect profits tax returns:

Year of assessment	Charge no	Additional tax
		$
1994/95	1-6008584-95-1	10,560,000
1995/96	1-6008566-96-1	8,720,000
1996/97	1-1159275-97-A	8,730,000
1997/98	1-2916464-98-9	7,740,000
1998/99	1-1128926-99-5	7,470,000
1999/2000	1-1123452-00-6	5,190,000
2000/01	1-1124482-01-4	4,510,000
Total		52,920,000

12. The additional tax was assessed following the dismissal of the appellant's appeal to the Board of Review ('the Board') from the assessments referred to in paragraphs 75 and 77 below, whereby the appellant was disallowed deductions for interest expenses, bank charges and legal fees it incurred in respect of a loan ('the Bank Loan') of HK$1,060 million borrowed from Bank A. An appeal from the decision of the Board was abandoned (see paragraph 81 below).

13. The appellant was incorporated in Hong Kong on 26 November 1991 with an authorised share capital of $1,000 divided into 100 ordinary shares of $10 each. Two shares were issued and fully paid-up. The principal activity of the appellant, as described in its 1994/95 to 2000/01 profits tax returns, was 'property investment'.

14. At all relevant times, Company B, a company incorporated in Hong Kong and listed on the Hong Kong Stock Exchange was the ultimate holding company of the appellant and Company B indirectly held all the equity in the following companies:

	Interest in equity held by subsidiary
Company C	100%
Company D	100%
The appellant	100%
Company E [City X]	100%

15. From the date of incorporation up to 31 December 2000, the following individuals were the directors of the appellant:

(a)	Mr F	(Appointed on 24 March 1992 and resigned on 1 January 1994)
(b)	Mr G	(Appointed on 24 March 1992 and resigned on 2 August 1994)
(c)	Mr H	(Appointed on 24 March 1992 and resigned on 2 August 1994)
(d)	Mr I	(Appointed on 1 July 1993 and resigned on 2 August 1994)
(e)	Mr J	(Appointed on 1 January 1994 and resigned on 10 June 1994)
(f)	Mr K	(Appointed on 1 July 1994 and resigned on 2 August 1994)
(g)	Mr L	(Appointed on 2 August 1994)
(h)	Mr M	(Appointed on 2 August 1994)
(i)	Mr N	(Appointed on 2 August 1994)

16. Company O was incorporated in Country P on 20 October 1992 with an authorised capital of HK$1,060,000,002 divided into 2 ordinary shares of HK$1 each and 1,060,000,000 cumulative redeemable preference shares of HK$1 each. Throughout the relevant period under dispute, all the ordinary shares were issued to Bank Q and all the cumulative redeemable preference shares were subscribed by Company E.

17. Company O has not applied for a business registration in Hong Kong.

18. The object or purpose for which Company O was established, as laid down in its Memorandum of Association, was to enter into a sub-participation agreement with Bank Q which was to be made on or about 26 October 1992. Clause 8 of Company O's Memorandum of Association and Articles 86 to 90 of Company O's Articles of Association also provided for the conditions upon which dividends were payable to Company O's shareholders.

19. Throughout the relevant period, the 2 ordinary shares of Company O were held by Bank Q.

20. Company E was incorporated in Country P on 7 August 1992 with an authorised share capital of US$5,000 divided into 5,000 ordinary shares of US$1 each with one vote for each share. Company E is a wholly owned subsidiary of Company B.

21. Company E has not applied for a business registration in Hong Kong.

22. From date of incorporation to 31 December 2000, the following individuals were directors of Company E:

(a) Mr F (Appointed on 7-8-1992 and resigned on 1-1-1994)
(b) Mr G (Appointed on 7-8-1992 and resigned on 2-8-1994)
(c) Mr H (Appointed on 7-8-1992 and resigned on 2-8-1994)
(d) Mr I (Appointed on 1-11-1993 and resigned on 2-8-1994)
(e) Mr J (Appointed on 22-2-1994 and resigned on 10-6-1994)
(f) Mr M (Appointed on 2-8-1994)
(g) Mr R (Appointed on 2-8-1994)
(h) Mr S (Appointed on 2-8-1994)
(i) Mr T (Appointed on 2-8-1994)
(j) Ms U (Appointed on 2-8-1994)

23. In the minutes dated 29 September 1992 of a meeting of the directors of Company E, it was recorded that the directors resolved that a Hong Kong dollar current account in name of Company E would be opened with Bank Q.

Sale and Purchase of Property

24. In the written resolutions dated 18 September 1992 passed by the board of directors of Company D, it was resolved that:

(a) Company D should procure Company C to transfer the property at Address AY ('the Property') to the appellant. Any one director of Company D should be authorised on behalf of Company D to sign any documents to signify Company D's consent to the transfer;

(b) the purchase consideration of $1,060 million should be provided to the appellant by an inter-company unsecured loan from Company D. After referring to the prevailing interest rate charged on the unsecured advance of similar size with no fixed repayment terms; Company D should accept the recommendation to charge the inter-company loan at the interest rate of 11 per cent per annum;

(c) the statutory declaration for claiming relief from the Collector of Stamp Revenue under section 45 of the Stamp Duty Ordinance as regards the assignment of the Property should be approved; and

(d) any one director of Company D should be authorised to make the statutory declaration and to sign any other documents on behalf of Company D in connection therewith.

25. In the written resolutions dated 19 September 1992 passed by the board of directors of the appellant, it was recorded that the directors resolved:

(a) The appellant should acquire the Property from Company C at a consideration of $1,060 million. The Property should be held as a long term investment for rentals and should continue to be leased to Company AW;

(b) the acquisition of the Property by the appellant should be financed by an inter-company unsecured loan from Company D. After referring to the prevailing interest rate charged on the unsecured advance of similar size with no fixed repayment terms, the appellant should accept the recommendation of the interest rate of 11 per cent per annum regarding the proposed inter-company loan;

(c) the sale and purchase agreement to be entered into between Company C as the vendor and the appellant as the purchaser ('the Agreement') should be approved. Any one director of the appellant should be authorised for and on behalf of the appellant to execute the same and to agree to such modifications or alterations to be made thereto as he may think fit;

(d) the assignment to be entered into between Company C as the assignor and the appellant as the assignee in respect of assigning all the beneficial interests and title of the Property to the appellant ('the Assignment') should be approved. Any two directors of the appellant should be authorised for and on behalf of the appellant to execute the same and to agree to such modifications or alternations to be made thereto as he may think fit and to affix the Seal of the appellant thereon in his presence;

(e) the statutory declaration for claiming relief from the Collector of Stamp Revenue under section 45 of the Stamp Duty Ordinance as regards the assignment of the Property by Company C to the appellant ('the Statutory Declaration') should be approved. Any one director of the appellant should be authorised for and on behalf of the appellant to make the Statutory Declaration; and

(f) any one director of the appellant should be authorised for and on behalf of the appellant to sign any other documents in connection with the Agreement, the Assignment, and the Statutory Declaration, and to do such acts and things as may be necessary to give effect to the acquisition of the Property.

26. By a sale and purchase agreement dated 21 September 1992, Company C agreed to sell the Property to the appellant at $1,060 million.

27. By a deed of assignment dated 21 September 1992, Company C assigned the Property to the appellant.

28. The appellant recorded the below accounting entries in respect of the transfer of Property in its books on 21 September 1992:

Debit	Leasehold land and building	1,060 million
Credit	Current account with Company D	1,060 million

29. On 23 September 1992, Mr H made a declaration for the purposes of section 45 of the Stamp Duty Ordinance.

Bank Loan from Bank A

30. In the written resolutions dated 21 October 1992 passed by the board of directors of the appellant, it was recorded that the directors resolved:

(a) The appellant should accept the terms and conditions set out in a facility letter to be entered into between the appellant and Bank A ('the Facility Letter') regarding the proposed loan, which includes the following:

- the loan should be repayable by the appellant in one instalment on the repayment date as defined in the Facility Letter;

- the interest rate for the loan should be at 10% per annum; and

- Company D should execute a guarantee ('the Guarantee') in favour of Bank A under which Company D should guarantee to pay to Bank A on demand any of the following amounts as defined in the Guarantee as the Guaranteed Moneys which were defined as all moneys owing by the appellant to Bank A at any time, interest on such moneys and all reasonable expenses of Bank A in enforcing the Guarantee.

(b) any one of the directors of the appellant should be authorised to execute the Loan Agreement and any other documents in connection with the Loan Agreement.

31. In a Loan Agreement dated 28 October 1992, Bank A confirmed that it would place at the disposal of the appellant the Bank Loan of $1,060 million according to the terms and conditions set out in the Loan Agreement.

32. By a guarantee dated 28 October 1992, Company D guaranteed to pay to Bank A on demand any of the Guaranteed Moneys as defined in the Guarantee which have fallen due by the appellant and that have not been paid at the time such demand is made.

33. By a letter dated 2 October 1992, Bank A confirmed with the appellant that the fees payable under the Bank Loan included an arrangement fee of $3,500,000, an annual management fee of $100,000, and the legal fees incurred by the solicitors of Bank A regarding the Bank Loan.

Loan Participation and Sub-Participation

34. By a participation agreement dated 28 October 1992, Bank Q agreed with Bank A to participate in the loan of $1,060 million on the terms thereof.

35. By a sub-participation agreement dated 28 October 1992, Company O agreed with Bank Q to sub-participate in the loan of $1,060 million.

36. Mr V of Bank A, Hong Kong signed the sub-participation agreement on 28 October, 1992 pursuant to authority approved at a board resolution passed by the board of directors of Company O on 26 October, 1992.

37. (a) According to an internal fax from Mr V to Bank A [City X, Country P] dated 26 October 1992, the sub-participation agreement would be signed on 28 October 1992 in City W as per an action list attached to the fax.

(b) There exists a copy of an agenda for, inter alia, the signing of the sub-participation agreement on 28 October 1992 in City W together with copies of 6 sets of used return jetfoil tickets between Hong Kong and City W for 28 October 1992 with departure times from Hong Kong to City W and from City W to Hong Kong coinciding with those set out in the agenda.

(c) According to an internal memo of Bank A dated 30 October 1992, Mr V gave instruction to credit Bank A [City W]'s HKD Account with the sum of HK$15,000 being the signing fee for the sub-participation agreement.

Subscriptions for Preference Shares in Company O by Company E

38. In the written resolution dated 26 October 1992 passed by the board of directors and signed by Mr Y and Ms Z as directors of Company O, it was recorded that the director resolved among other things that:

(a) two ordinary shares would be issued to Bank Q on 27 October 1992 with payment in cash of the par value to be made by Bank Q on or before 2 November 1992;

(b) 1,060,000,000 cumulative redeemable preference shares would be issued to Company E on 27 October 1992 with payment in cash of the par value by Company E on or before 2 November 1992;

(c) a sub-participation agreement entered into between Company O and Bank Q would be approved and that Mr V of Bank A would be authorised on behalf of Company O to execute the sub-participation agreement;

(d) that the amount received in respect of the cumulative redeemable preference shares was to be deposited by Company O with Bank A in City X branch overnight on 2 November 1992 and, pursuant to Article 87, the one-day interest thereon would be declared dividend in favour of the holder of the cumulative redeemable preference shares;

(e) pursuant to Article 88, each amount received by Company O from time to time under the sub-participation agreement would constitute surplus and that payment of interim cumulative preference dividends to the holder of the cumulative redeemable preference shares from each such amount upon receipt be authorised; and

(f) that any one director, or any person authorised by the directors, should do such act and execute such documents as might be required or otherwise regarded by him as necessary or desirable in connection with the resolution, including to sign and deliver irrevocable payment instructions to Company O's bank to effect payments of the cumulative preference dividends.

39. In the minutes of a meeting of the directors of Company E dated on 21 October 1992, it was recorded the directors resolved that Company E should subscribe at par for all the 1,060,000,000 cumulative redeemable preference shares of $1 each in the capital of Company O.

40. In the minutes of a meeting of the directors of Company E dated 21 October 1992, it was recorded that:

(a) the 2 ordinary shares ('the Shares') and 1,060,000,000 cumulative redeemable preference shares in Company O were to be respectively held by Bank Q and Company E;

(b) an option agreement should be executed between Company E and Bank Q under which Company E should grant to Bank Q an option to require Company E to purchase and Bank Q should grant to Company E an option to require Bank Q to sell the Shares; and

(c) the directors resolved that the option agreement should be approved and that any one director should be authorised to execute the option agreement.

41. By an option agreement dated 28 October 1992, Company E granted to Bank Q an option to require Company E to purchase the Shares in Company O and Bank Q granted to Company E an option to require Bank Q to sell the Shares in Company O on the terms set out therein. Neither option has been exercised in the periods covered by the assessment in this case. In the option agreement, Bank Q gave the following undertakings:

(a) Clause 7.01

Bank Q shall not vote in favour of any resolution to:

(i) amend or vary the memorandum or articles, or amend or waive any terms of the sub-participation agreement;

(ii) alter the share capital of Company O;

(iii) incur any indebtedness on the part of Company O; and

(iv) wind up Company O.

(b) Clause 7.02

Bank Q agrees to procure and to pass such resolutions as may be necessary to ensure, that the profits of Company O in each of its financial year should be distributed in full semi-annually by way of cumulative preference dividends promptly upon receipt of such profits. Bank Q acknowledges and agrees that any payment received by Company O pursuant to the terms of the sub-participation agreement shall constitute profits of Company O and would use reasonable endeavours to procure that such profits will be distributed in full.

The Fund Flow

42. By a letter dated 9 October 1992, the appellant instructed Bank A to transfer out of its account on the draw down date and the anniversaries thereof the fees referred to in paragraph 33 above.

43. (a) By a letter dated 28 October 1992, the appellant gave notice to Bank A to draw down the loan of $1,060 million for value on 2 November 1992 and credit the sum to the account it maintained with Bank A.

(b) By a letter dated 28 October 1992, the appellant instructed Bank A to transfer out of its account $1,060 million for value on 2 November 1992 to the account Company D maintained with Bank A. The transfer was recorded in the bank statement of the appellant.

44. On 2 November 1992, Bank Q paid the sum of $1,060 million to Bank A under the Participation Agreement.

45. On 2 November 1992, Bank A paid the sum of $1,060 million to the appellant under the Loan Agreement.

46. On 2 November 1992, the appellant paid the sum of $1,060 million to Company D.

47. On 2 November 1992, Company D paid the sum of $1,060 million to Company E as an unsecured inter-company loan.

48. On 2 November 1992, Company E paid the sum of $1,060 million to Company O as the subscription money for the allotment of 1,060,000,000 redeemable preference shares.

49. On 3 November 1992, Company O paid the sum of $1,060 million to Bank Q under the Sub-Participation Agreement, thereby completing the flow of funds. Accordingly, between 2 and 3 November 1992 the relevant funds were placed by Company O on an overnight deposit with the City X branch of Bank Q.

Interest/Dividend Payments

50. With the exception of the 1st interest/dividend payment, the amount and date of the each interest payment under the Loan Agreement/Participation Agreement/Sub-Participation Agreement coincided with the amount and date of each dividend payment in respect of the redeemable preference shares in Company O. The 1st interest/dividend payment was exceptional because of the one day' s interest payable to Company O by bank A [City X].

51. For example, with respect to the interest/dividend payment which took place on 3 May 1993:

(a) On 28 April 1993, Company D gave an irrevocable instruction to Bank A to debit the amount of HK$52,807,186.17 from its account and pay the same to the appellant' s account on 3 May 1993 (in order to put the appellant in funds to make the interest payment);

(b) On 28 April 1993, the appellant gave an irrevocable instruction to Bank A to debit the amount of HK$52,807,186.17 from its account on 3 May 1993 to settle the 1st interest payment due to Bank A under the Loan Agreement;

(c) On 28 April 1993, Company E gave an irrevocable instruction to Bank Q to debit the amount of HK$52,807,186.17 (representing the 1st dividend payment expected to receive from Company O) from its account and pay the same to Company D on 3 May 1993 (in order to cover the outflow of funds from Company D under (a) above);

(d) According to a document dated 30 April 1993, Bank A informed Bank Q of the details of the payment of HK$52,807,186.17 (made up of HK$52,517,568.68 and HK$289,617.49, the latter being the overnight interest on the principal amount of HK$1,060,000,000 on 2 November 1992) to take place on 3 May 1993 amongst various accounts and the accounting entries which were required to be made.

(e) According to a document dated 30 April 1993, Mr V gave instructions to the OIC Loans Section of Bank A in respect of the accounting entries to be made on 3 May 1993 in the accounts of Company D, the appellant and Bank Q.

(f) On 3 May 1993, the following fund flow in respect of the interest/dividend payment took place:

(i) Company D paid the sum of HK$52,807,186.17 to the appellant;

(ii) the appellant paid the sum of HK$52,807,186.17 to Bank A as the 1st interest payment;

(iii) Bank A paid the sum of HK$52,807,186.17 to Bank Q pursuant to the Participation Agreement;

(iv) Bank Q paid the sum of HK$52,517,568.68 to Company O pursuant to the Sub-Participation Agreement, and Bank A (City X Branch) paid the sum HK$289,617.49 [to] Company O (being the overnight interest on the principal amount of HK$1,060 million on 2 November 1992);

(v) Company O paid the sum of HK$52,807,186.17 to Company E as the 1st dividend in respect of the redeemable preference shares;

(vi) Company E paid sum of HK$52,807,186.17 to Company D pursuant to the irrevocable instruction dated 28 April 1993.

52. All subsequent interest/dividend payments were effected in manner similar to that of the 3 May 1993 payments.

Group Re-organisation and Amendment of Guarantee

53. In the minutes of a meeting of the board of directors of the appellant dated 29 July 1994, it was recorded that Company B would substitute for Company D as the guarantor to the Bank Loan of $1,060 million provided by Bank A to the appellant.

54. In the written resolutions of Company B dated 29 July 1994, it was recorded that the ultimate holding company Company B should substitute Company D as the guarantor to the Bank Loan of $1,060 million provided by Bank A.

55. By an amendment agreement dated 1 August 1994, Bank A agreed to release Company D from its obligations under the Guarantee, subject to the conditions, inter alia, that Company B should enter into a guarantee with Bank A substantially in the same form as the Guarantee.

56. By a guarantee dated 1 August 1994, Company B guaranteed to pay to Bank A on demand any of the Guaranteed Moneys as defined in the guarantee which have fallen due by the appellant and that have not been paid at the time such demand is made. Guaranteed Moneys were defined as all moneys owing by the appellant to Bank A at any time, interest on such moneys and all reasonable expenses of Bank A in enforcing the guarantee.

57. By a letter dated 28 July 1994, Bank A gave notice to Bank Q of an amendment agreement relating to the Loan Agreement to be made between Bank A, the appellant and Company D asking Bank Q to confirm its agreement to the terms of the agreement and changes in the participation agreement between Bank A and Bank Q dated 28 October 1992 consequent upon the amendment agreement which Bank Q did by signing the letter.

58. In the written resolutions of the board of directors of Company O dated 1 August 1994 in the Country P, it was recorded that the directors approved a letter agreement to be entered into between Bank Q and Company O [to approve] the terms of an amendment agreement between Bank Q and Bank A.

59. By a letter dated 1 August 1994, Bank Q gave notice to Company O of amendments to the participation agreement between Bank A and Bank Q to reflect the amendments pursuant to the Amendment Agreement whereby Company D was to be released from its obligations under the Company D Guarantee to Bank A and Company B was to be substituted as guarantor asking Company O to confirm its agreement to consequential amendments to the sub-participation agreement between Bank Q and Company O which Company O did by signing the letter.

60. In the minutes of a meeting of the board of directors of Company E dated 25 July 1994, it was resolved that Company E should give consent to a letter agreement to approve the proposed change of guarantor to the loan as defined in the sub-participation agreement.

61. By a letter agreement dated 25 July 1994, Company E gave consent to Bank Q to the amendment to the sub-participation agreement pursuant to a letter agreement to be made between Bank Q and Company O.

Extension of Loan Facility

62. In the written resolutions of the board of directors of the appellant dated 12 November 1997, it was recorded that the directors of the appellant approved a draft amendment agreement relating to the Loan Facility of $1,060 million to be executed between Bank A and the appellant under which the repayment date was extended for a period of 5 years.

63. By an amendment agreement dated 18 November 1997, Bank A and the appellant agreed to vary the terms in the loan agreement in order to extend the repayment date under the original agreement for a further period of 5 years and to increase the interest payable on the loan to the annual rate of 13 per cent per annum.

64. By a letter agreement dated 18 November 1997, Company O confirmed its agreement to the amendments to the sub-participation agreement as a result of the amendment to the participation agreement between Bank A and Bank Q caused by the changes.

65. In the written resolution of the board of directors of Company O dated 18 November 1997, it was recorded that the sole director of Company O approved the letter agreement in the form of the attached draft be entered into between Bank Q and Company O to approve the terms of the amendment agreement and other amendments to the sub-participation agreement.

66. In the minutes of a meeting of the board of directors of Company E dated 17 November 1997, it was resolved that Company E should approve the letter agreement to be entered into by Company E and Bank Q to approve the terms of the amendment agreement and certain amendments to the option agreement.

67. By a letter dated on 18 November 1997 to Bank Q, Company E gave consent to the amendment to the sub-participation agreement pursuant to a letter agreement to be made between Bank Q and Company O.

Returns and Accounts

68. On divers dates, the appellant filed its profits tax returns for the years of assessment 1994/95 to 2000/01.

69. The appellant makes up its accounts to 31 December each year. In its accounts for the years ended 31 December 1994 to 2000, the appellant recorded the following particulars:

(a) Profit and Loss Accounts

Year ended 31 December	1994	1995	1996	1997	1998	1999	2000
	$	$	$	$	$	$	$
Rental income	117,441,080	99,091,392	99,091,392	99,091,392	99,091,392	82,576,160	82,576,160
Bank interest	-	884	238	1,792	8,922	1,964	1,892
	117,441,080	99,092,276	99,091,630	99,093,184	99,100,314	82,578,124	82,578,052
Expenses							
Interest paid	106,000,000	106,000,000	106,000,000	111,314,521	137,800,000	137,800,000	137,800,000
Bank charges	100,600	100,300	100,300	1,138,512	159,312	160,149	159,260
General/sundry expenses	3,370	3,765	2,594	2,517	103,974	2,992	2,833
Insurance	237,202	457,637	412,661	225,424	181,304	130,748	97,590
Professional fee	13,333	2,120	-	-	-	-	-
Legal fee	39,409	-	-	-	35,070	-	-
Crown rent	2,000	-	-	1,551,366	3,042,000	2,322,450	1,975,950
Repairs & maintenance	-	62,135	41,100	-	108,500	210,436	91,759
Auditors' remuneration	16,500	24,000	26,820	28,800	28,800	20,680	25,000
Depreciation & Amortisation	8,196,023	8,196,024	22,465,254	22,465,254	22,465,254	22,465,253	22,465,254
	8,212,523	8,282,159	22,533,174	22,494,054	25,679,624	25,018,819	24,557,963
Profits/(Loss) before tax	2,832,643	(15,753,705)	(29,957,099)	(37,633,210)	(64,823,900)	(80,534,584)	(80,039,594)

(b) Balance Sheets

As at 31 December	1994	1995	1996	1997	1998	1999	2000
	$	$	$	$	$	$	$
Fixed Assets							
Leasehold land	742,000,000	742,000,000	742,000,000	742,000,000	742,000,000	742,000,000	742,000,000
Building	343,259,816	343,452,927	343,452,927	342,118,638	342,118,638	342,118,638	342,118,638
	1,085,259,816	1,085,452,927	1,085,452,927	1,084,118,638	1,084,118,638	1,084,118,638	1,084,118,638
Less: Aggregated Depreciation	(23,614,898)	(31,810,922)	(54,276,176)	(76,741,430)	(99,206,684)	(121,671,937)	(144,137,191)
	1,061,644,918	1,053,642,005	1,031,176,751	1,007,377,208	984,911,954	962,446,701	939,981,447
Amount due from Ultimate Holding Co.	17,616,635	10,027,457	1,849,199	-	-	-	-
Current Assets							
Amount due from immediate holding company	20	20	-	-	-	-	-
Prepayment	47,440	81,886	66,155	31,854	29,889	608,052	694,732
Cash at bank	6,984	8,485	26,626	51,831	99,498	46,318	29,055

	54,444	90,391	92,781	83,685	129,387	654,370	723,787
Current Liabilities							
Accruals and provisions	(19,127,486)	(19,325,047)	(18,641,024)	(23,904,809)	(23,418,855)	(22,792,891)	(22,615,164)
	1,060,188,511	1,044,434,806	1,014,477,707	983,556,084	961,622,486	940,308,180	918,090,070
Share capital	20	20	20	20	20	20	20
Retained profits/ (Accumulated Losses)	188,491	(15,565,214)	(45,522,313)	(83,155,523)	(147,979,423)	(228,514,007)	(308,553,601)
Shareholders' Fund/ (Deficit)	188,511	(15,565,194)	(45,522,293)	(83,155,503)	(147,979,403)	(228,513,987)	(308,553,581)
Bank loan	1,060,000,000	1,060,000,000	1,060,000,000	1,060,000,000	1,060,000,000	1,060,000,000	1,060,000,000
Amount due to Ultimate Holding Co.	-	-	-	6,711,587	49,601,889	108,822,167	166,643,651
	1,060,188,511	1,044,434,806	1,014,477,707	983,556,084	961,622,486	940,308,180	918,090,070

70. In the notes to the appellant's accounts for the years ended 31 December 1994 to 2000, the descriptions for the Bank Loan are summarised below:

Years ended 31 December 1994 to 1997

'BANK LOAN

The bank loan is secured by guarantee from the Company's ultimate holding company and is repayable after one year but within five years from the balance sheet date.'

Years ended 31 December 1998 to 2000

'BANK LOAN

The bank loan is secured by a guarantee from the Company's ultimate holding company and is repayable in full upon maturity in year 2002.'

71. The appellant computed its assessable profits/(adjusted losses) for the years of assessment 1994/95 to 2000/01 as follows:

Year of Assessment	1994/95	1995/96	1996/97	1997/98	1998/99	19992000	2000/01
	$	$	$	$	$	$	$
Profit/(Loss) before tax	2,832,643	(15,753,705)	(29,957,099)	(37,633,210)	(64,823,900)	(80,534,584)	(80,039,594)
Add: Depreciation	8,196,023	8,196,024	22,465,254	22,465,254	22,465,254	22,465,253	22,465,254
Other adjustments	25	47,440	81,886	66,155	133,254	29,889	19,032
	11,028,691	8,243,464	22,547,140	22,531,409	22,598,508	22,495,142	22,484,286
Less: Depreciation allowance	(10,433,568)	(10,475,375)	(10,432,668)	(10,428,991)	(10,425,682)	(10,422,704)	(10,420,023)
Other adjustments	(50,860)	(81,886)	(66,155)	(31,854)	(32,379)	(20,996)	(17,604)
Assessable profit/ (Adjusted loss)	544,263	(18,067,502)	(17,908,782)	(25,562,646)	(52,683,453)	(68,483,142)	(67,992,935)

Notes:

(a) The appellant revised its tax computations for the years 1994/95 to 1996/97. The assessable profits/(adjusted losses) for the 3 years of assessment represent the revised figures.

(b) An assessable profit of $1,148,656 was declared for the year 1993/94 after deduction of interest expenses of $106,000,000 and bank charges of $100,000. The loss brought forward from 1992/93 was $13,356,822. After setting off the assessable profit declared for the year 1993/94, a loss of $12,208,166 was carried forward to the year 1994/95.

72. In the schedules to the appellant's returns for the years of assessment 1994/95 to 2000/01, the descriptions for the interest expenses are summarised below:

'Interest on bank loan from [Bank A] of [Address AX].'

'The bank loan was used to finance the purchase of the property at [Address AY] which has been let out for taxable rental income. The loan is not secured by any non-taxable deposit. The interest is therefore deductible under Section 16(1)(a) and 16(2)(d) of the Inland Revenue Ordinance.'

Note:

In the schedule for the year of assessment 1994/95, the 'property' was described as the 'Company's property'.

73. On divers dates, the assessor issued to the appellant the following assessment/statements of loss for the years of assessment 1994/95 to 2000/01:

Year of assessment	Date of assessment/ statement of loss	Assessable profit/(loss) $	
1994/95	20 Aug 1998	544,263	(Revised)
1995/96	20 Aug 1998	(18,067,502)	(Revised)
1996/97	28 Aug 1998	(17,908,782)	(Revised)
1997/98	28 Aug 1998	(25,562,646)	(Revised)
1998/99	6 July 2001	(52,683,453)	
1999/2000	6 July 2001	(68,483,142)	
2000/01	25 Sept 2001	(67,992,935)	

Tax Audit

74. On 15 February 2001, the assessor commenced an audit on the appellant's tax return for the year of assessment 1997/98 and also an investigation into the tax affairs of the appellant.

75. On divers dates, the Assistant Commissioner, having examined the facts, applied the provisions in sections 16, 17, 61 and/or 61A of the Ordinance and raised on the appellant the following profits tax assessments to disallow the interest expenses, bank charges and legal fees in relation to the Bank Loan:

Year of Assessment	1994/95	1995/96	1996/97	1997/98	1998/99	1999/2000	2000/01
	$	$	$	$	$	$	$
Profit/(Loss) per return	544,263	(18,067,502)	(17,908,782)	(25,562,646)	(52,683,453)	(68,483,142)	(67,992,935)
Add: Interest expenses	106,000,000	106,000,000	106,000,000	111,314,521	137,800,000	137,800,000	137,800,000
Bank charges	100,600	100,300	100,000	1,137,592	158,902	158,841	159,260
Legal fees	39,409	-	-	-	35,070	-	-
Assessable profits	69,966,325	106,684,272	88,032,798	88,191,218	86,889,467	85,310,519	69,475,699
Tax payable	17,602,904	14,525,411	14,551,550	12,903,085	13,649,683	11,116,111	11,194,612

76. Accounting Firm AA on behalf of the appellant objected against the assessments.

77. By a determination dated 15 January 2004, the Commissioner determined the assessments as follows:

Year of assessment	Total assessable profits	Total tax payable
	$	$
1994/95	106,683,672	17,602,805
1995/96	88,032,498	14,525,362
1996/97	88,191,218	14,551,550
1997/98	86,889,467	12,903,085
1998/99	85,310,519	13,649,683
1999/2000	69,475,699	11,116,111
2000/01	72,064,262	11,530,281
Total	596,647,335	95,878,877

78. By a Notice of Appeal dated 13 February 2004, Messrs Baker & McKenzie on behalf of the appellant appealed to the Board.

79. The appellant purchased tax reserve certificates for the full amount of tax assessed.

The Board's Conclusions

80. By the Decision, the Board of Review upheld the Commissioner's determination. See D94/04, (2005-06) IRBRD, vol 20, 47.

Assessments Final and Conclusive

81. The appellant applied for a case to be stated for the opinion of the Court of First Instance under section 69 of the Ordinance. The Board stated the case on 3 November 2005 and the appellant transmitted the stated case to the Court of First Instance on 17 November 2005. By notice dated 29 November 2005, Messrs Baker & McKenzie on behalf of the appellant informed the Court of First Instance that the appellant would abandon the appeal. As such, the assessments as determined by the Commissioner in paragraph 77 have become final and conclusive under section 70 of the Ordinance. The amount of profits understated and tax undercharged are tabulated as follows:

Year of assessment	Total assessable profits	Assessable profits already reported	Profits understated	Percentage of profits understated to total assessable profits
	$	$	$	
1994/95	106,683,672	544,263	106,139,409	99%
1995/96	88,032,498	Nil	88,032,498	100%
1996/97	88,191,218	Nil	88,191,218	100%
1997/98	86,889,467	Nil	86,889,467	100%
1998/99	85,310,519	Nil	85,310,519	100%
1999/2000	69,475,699	Nil	69,475,699	100%
2000/01	72,064,262	Nil	72,064,262	100%
Total	596,647,335	544,263	596,103,072	

Year of assessment	Total tax payable	Tax already charged	Tax undercharged	Percentage of tax undercharged to total tax payable
	$	$	$	
1994/95	17,602,805	Nil	17,602,805	100%
1995/96	14,525,362	Nil	14,525,362	100%
1996/97	14,551,550	Nil	14,551,550	100%
1997/98	12,903,085	Nil	12,903,085	100%
1998/99	13,649,683	Nil	13,649,683	100%
1999/2000	11,116,111	Nil	11,116,111	100%
2000/01	11,530,281	Nil	11,530,281	100%
Total	95,878,877	Nil	95,878,877	

Additional Tax under section 82A

82. On 21 March 2006, the Commissioner gave notice to the appellant under section 82A(4) of the Ordinance, informing the appellant that she intended to assess the appellant to additional tax for making incorrect returns for the years of assessment 1994/95 to 2000/01.

83. On 20 April 2006, Messrs Baker & McKenzie submitted written representations on behalf of the appellant to the Commissioner.

84. On 18 September 2006, the Commissioner, having considered the representations, made the following additional tax assessments:

Year of assessment	Tax undercharged	Additional tax assessed under section 82A	Percentage of additional tax to tax undercharged
	$	$	
1994/95	17,602,805	10,560,000	60%
1995/96	14,525,362	8,720,000	60%
1996/97	14,551,550	8,730,000	60%
1997/98	12,903,085	7,740,000	60%
1998/99	13,649,683	7,470,000	55%
1999/2000	11,116,111	5,190,000	47%
2000/01	11,530,281	4,510,000	39%
Total	95,878,877	52,920,000	55%

85. On 16 October 2006, Messrs Baker & McKenzie on behalf of the appellant appealed to the Board against the Assessments.

ORIGINAL GROUNDS OF APPEAL

86. The appellant appealed on the following grounds:

> ' 1. The [appellant] did not make an incorrect return by omitting or understating anything in respect of which it is required by the IRO to make a return and therefore should not be liable to additional tax.
>
> 2. The [appellant] had a ' reasonable excuse' within the meaning of the IRO for filing the profits tax returns for the years of assessment 1994/95 to 2000/01 on the basis it did and therefore should not be liable to additional tax.
>
> 3. The amounts of the additional tax assessed are incorrect and/or excessive having regard to the circumstances.'

THE JANUARY 2007 HEARING

87. At the January 2007 hearing, the appellant was represented by Mr Steven Rudolf Sieker and the respondent by Ms Gladys Li SC, leading Mr Stewart Wong. We have had the benefit of helpful and able assistance by both teams.

88. Mr Sieker called one factual witness, Mr AB, a partner in Accounting Firm AA from 1 April 1987 to 30 June 2003, and one expert witness, Dr AC, a senior adviser for the Accounting Firm AD in Hong Kong/China. Both Dr AC and Mr AB were at all material times with accounting firms involved in devising and advising on tax avoidance schemes.

89. Ms Li called one factual witness, Mr AE, an assessor in the Field Audit and Investigation Unit of the Inland Revenue Department.

90. The appellant furnished us with a bundle of the following authorities:

1. Inland Revenue Ordinance (Chapter 112), table of contents, sections 16, 51, 61, 61A and 82A
2. BR 80/76, IRBRD, 259
3. D13/85, IRBRD, vol 2, 173
4. D18/91, IRBRD, vol 6, 36
5. D14/98, IRBRD, vol 13, 153
6. D129/02, IRBRD, vol 18, 216
7. CIR v Tai Hing Cotton Mill (Development) Limited (2006) CACV 343/2005
8. D60/05, (2005-06) IRBRD, vol 20, 828
9. Inland Revenue Ordinance (Chapter 112), section 51C
10. D52/86, IRBRD, vol 2, 314
11. D4/06, (2006-07) IRBRD, vol 21, 139
12. CIR v Howe (1977) 1 HKTC 936
13. Inland Revenue Commissioners v Duke of Westminster [1936] AC 1
14. Mullens v FC of T (1976) 135 CLR 290
15. Patcorp Investments Ltd v Federal Commissioner of Taxation (1976) 140 CLR 247
16. Lau v Federal Commissioner of Taxation (1984) 54 ALR 167
17. Stubart Investments Ltd v the Queen (1984) 10 DLR (4^{th}) 1
18. UK Finance Act 1985 Chapter 54, sections 14, 15 and 33
19. Hutchings v The Commissioners of Customs and Excise [1987] VATTR 58
20. The Clean Car Company Ltd v The Commissioners of Customs and Excise [1991] VATTR 234
21. Extracts of 'The 1985-86 Budget: Speech by the Financial Secretary', pages 50-53
22. Extracts of 'Hong Kong Legislative Council Hansard 29 January 1986', pages 553-555

23. Extracts of 'Legislative Council Brief, Inland Revenue (Amendment) Bill 2000', 29 September 2000, pages 1-5 [File Ref.: FIN CR 1/2306/00]
24. Extracts of 'Bills Committee on Inland Revenue (Amendment) Bill 2000, Administration's Response to Comments relating to Exemption from "tax symmetry" Rule for Internal Borrowings by Associated Corporations', April 2004, pages 1-7 [Ref.: CB(1)1654/03-04 (03)]
25. Extracts of 'Paper for the House Committee meeting on 28 May 2004, Report of the Bills Committee on Inland Revenue (Amendment) Bill 2000', 27 May 2004, pages 1-12 [Ref.: CB1/BC/1/00]
26. Bill Committee on Inland Revenue (Amendment) Bill 2000, Follow-up actions arising from the discussion at the meeting on 29 April 2004, May 2004 [Ref.: CB(1)1753/03-04 (01)]
27. Departmental Interpretation & Practice Note No 15, 1 May 1986
28. Extracts of minutes of the 2005 annual meeting between the Revenue and the Hong Kong Institute of Certified Public Accountants, November 2005, pages 35-38
29. Extracts of minutes of the 2006 annual meeting between the Revenue and the Hong Kong Institute of Certified Public Accountants, July 2006, pages 33-35
30. Extracts of Peter Willoughby, 'Revenue Law Roundabout' in Law Lectures for Practitioners 1985 Libra Press Limited, pages 100-102
31. Extracts of Peter Willoughby, 'Revenue Law Roundabout' in Law Lectures for Practitioners 1986 Libra Press Limited, pages 209-212
32. Extracts of Andrew Halkyard, 'Revenue Law Roundabout' in Law Lectures for Practitioners 1987 Libra Press Limited, pages 139-142
33. Extracts of Michael Olesnicky, 'Revenue Law Up-To-Date' in Law Lectures for Practitioners 1988 Libra Press Limited, pages 291-300
34. Extracts of Michael Olesnicky, 'Revenue Law Up-To-Date' in Law Lectures for Practitioners 1992 Libra Press Limited, pages 1-5
35. Extracts of 'Hong Kong Taxation Law & Practice', 1986/87 edition to 2005/06 edition

91. The respondent furnished us with a bundle of the following authorities:

1. Inland Revenue Ordinance (Chapter 112), sections 16, 51, 61, 61A, 68, 70, 82A, 82B
2. D40/88, (1988) IRBRD, vol 3, 377
3. D42/89, (1989) IRBRD, vol 4, 479
4. D96/97, (1998) IRBRD, vol 12, 520
5. D26/99, (1999) IRBRD, vol 14, 288
6. D17/01, (2001) IRBRD, vol 16, 178
7. D90/01, (2001) IRBRD, vol 16, 757
8. D115/01, (2001) IRBRD, vol 16, 893

9. D118/02, (2003) IRBRD, vol 18, 90
10. D40/03, (2003) IRBRD, vol 18, 526
11. D96/03, (2004) IRBRD, vol 18, 905
12. D59/05, (2005-06) IRBRD, vol 20, 821
13. Newton v Commissioner of Taxation of the Commonwealth of Australia [1958] AC 450

THE MAY 2008 HEARING

Correspondence between the Clerk and the parties

92. The January 2007 hearing concluded on 26 January 2007.

93. On 30 May 2007, the Court of Appeal handed down its judgment in Koon Wing Yee and another v Insider Dealing Tribunal and another, CACV 358 and 360 of 2005.

94. In early July 2007, we were considering our decision in draft. By letter dated 4 July 2007, the Clerk wrote to the parties asking whether the parties would wish the Board to reconvene to hear any submission as a result of the Court of Appeal judgment, failing which the Board would finalise its decision and transmit it to the parties.

95. By letter dated 10 July 2007, the Department of Justice sought clarifications from the Board and suggested that any further submissions should wait until after the disposal of the Financial Secretary' s intended appeal to the Court of Final Appeal. By letter dated 16 July 2007, Messrs Baker & McKenzie indicated the appellant' s wish to make further submissions and agreed with the respondent' s suggestion to await the outcome of the intended appeal to the Court of Final Appeal.

96. By letter dated 18 July 2007, the Clerk wrote advising the parties that:

> 'apart from forming the view that the parties should be offered an opportunity to be heard if they so wish, the Board has not formed any view on *Koon Wing Yee*' and
>
> the suggestion to await the outcome of intended appeal to the Court of Final Appeal did not find favour with the Board.

97. By letter dated 25 July 2007, Messrs Baker & McKenzie asked for 'a little bit more time' before responding further as they were performing a preliminary evaluation of the appellant' s position and taking instructions from the appellant.

98. The appellant took more than 'a little bit more time' and by letter dated 6 September 2007, the Clerk informed it that the Board intended to deliver its decision in about 10 days' time unless persuaded to do otherwise by the appellant. This prompted another holding reply indicating

its desire to make further submissions. By letter dated 17 October 2007, the Clerk informed the appellant that unless the Clerk received a written application by the appellant to amend the grounds of appeal setting out the proposed new grounds and a written submission, the Board intended to deliver its decision by the end of October 2007.

99. By a joint letter dated 24 October 2007, the appellant and the respondent informed the Board that the appeal in Koon Wing Yee was scheduled to be heard in the Court of Final Appeal on 25 & 26 February 2008.

100. By letter dated 29 October 2007, Messrs Baker & McKenzie set out a proposed new ground of appeal and enclosed a written submission.

101. As the Financial Secretary' s appeal to the Court of Final Appeal was scheduled to be heard in 2 months' time and bearing in mind the time estimate of 1 day by Messrs Baker & McKenzie, and in consultation with both parties, the Clerk fixed 3 evening sessions (26 – 28 May 2008) for the Board to hear the parties on the application to amend the grounds of appeal and, if thought fit, arguments under the additional ground.

102. By letter dated 28 April 2008, the Clerk reiterated that the Board intended to restrict further submissions to points arising from Koon Wing Yee and stated that the Board would have to be persuaded before it would hear submissions on the Court of Final Appeal' s judgment on section 61A in Commissioner of Inland Revenue v HIT Finance Limited.

Additional ground of appeal

103. By letter dated 16 May 2008, Messrs Baker & McKenzie contended that the points arising from Koon Wing Yee were covered by 1st and 3rd grounds of appeal, but went on to ask for leave to amend by adding the following ground of appeal:

> '1A. In the light of the principles set out in *Koon Wing Yee v Insider Dealing Tribunal* (CACV 358 & 360/2005 & FACV No. 19 of 2007), the Commissioner should have treated the assessment of additional tax under section 82A of the IRO as involving the determination of a "criminal charge" within the meaning of Article 11 of the Hong Kong Bill of Rights ["BOR"] and Article 39 of the Basic Law and therefore applied a burden and standard of proof appropriate for such a determination and, for such purposes, was not entitled to rely upon the earlier decision of this Board dated 16 March 2005 or upon section 70 of the IRO. The consequence of section 82A being "criminal" in nature is that both BOR 10 and 11 are triggered and that such section is invalid by reason of breaches of BOR 11 and/or 10.'

The May 2008 hearing

104. At the May 2008 hearing, the appellant was represented by Mr Johnny Mok SC and the respondent by Mr David Pannick QC, leading Mr Stewart Wong.

105. In answer to a question asked more than once by the Chairman, Mr Mok told the Board that ground 1A set out in paragraph 103 above was the only proposed additional ground that he was seeking the Board's permission under section 66(3) to rely on.

106. The appellant submitted a total of 5 written submissions:

(1) 'Appellant's submissions on Koon Wing Yee v Insider Dealing Tribunal' dated 29 October 2007;

(2) 'Appellant's supplemental submissions on Koon Wing Yee v Insider Dealing Tribunal' dated 16 May 2008;

(3) 'CFA's Principles relating to Presumption of Innocence', undated, handed by Mr Mok to us on 26 May 2008;

(4) 'Why the Proportionality Test is Not Satisfied', undated, handed by Mr Mok to us on 27 May 2008; and

(5) 'Appellant's reply submissions', also undated, handed by Mr Mok to us on 28 May 2008.

107. Mr Pannick submitted that the Board should not allow the appellant to raise human rights issues so late in the appeal. Without prejudice to that objection, he sought leave to adduce further evidence. His submissions on human rights issues were concise, pertinent and helpful.

108. By consent of both parties, the statement dated 7 May 2008 of Ms AF, Assistant Commissioner of the Field Audit and Investigation Unit of the Revenue, was admitted as sworn evidence without calling the maker.

109. The appellant furnished us with a copy of the following authorities:

1. Inland Revenue Ordinance, Chapter 112, ss. 51, 51A, 51B, 52, 59, 60, 68, 70, 80, 82A & 82B
2. Hong Kong Bill of Rights Ordinance, Chapter 383, sections 6 & 8 – Hong Kong Bill of Rights, articles 10 & 11
3. Basic Law, articles 39 & 87
4. Criminal Procedure Ordinance, Chapter 221, section 94A
5. Securities (Insider Dealing) Ordinance, Chapter 395, sections 17, 23

6. Securities and Futures Commission Ordinance, Chapter 24, section 33
7. Article 14(2) of the International Covenant on Civil Political Rights
8. D17/72, IRBRD, vol 2, 97[2]
9. D94/04, IRBRD, vol 20, 18
10. Koon Wing Yee v Insider Dealing Tribunal CACV 358 & 360/2005
11. Koon Wing Yee v Insider Dealing Tribunal and Another FACV No. 19 of 2007
12. HIT Finance Limited v CIR HCIA 14 & 15/2005
13. CIR v HIT Finance Limited FACV Nos. 8 & 16 of 2007
14. Insider Dealing Tribunal v Shek Mei-ling [1999] 2 HKCFAR 205
15. HKSAR v Lam Kwong Wai (2006) 9 HKCFAR 574
16. Leung Kwok Hung v HKSAR (2005) 8 HKCFAR 229
17. HKSAR v Hung Chan Wa FACC 1/2006
18. HKSAR v Ng Po On FACC 6/2007
19. R v Edwards [1975] QB 27
20. Han v Customs & Excise Commissioner [2001] 1 WLR 2253 (CA)
21. R (McCann) v Manchester Crown Court [2003] 1 AC 787 (HL)
22. Janosevic v Sweden (2004) 38 EHRR 473
23. Halkyard, Vanderwolk & Chow, Hong Kong Tax Law, Cases and Materials (3rd Edn: 2001) page 325
24. Tse Wai Chun Paul v Solicitors Disciplinary Tribunal CACV 3174/2001
25. Ngai Few Fung v Cheung Kwai Heung CACV 147/2007

110. The respondent furnished us with a copy of the following authorities:

1. Inland Revenue Ordinance, Chapter 112, section 66
2. Medical Council of Hong Kong v Chow Siu Shek (2000) 3 HKCFAR 144
3. Commissioner of Inland Revenue v Loganathan [2000] 1 HKLRD 914
4. BR 17/72, IRBRD, 97
5. D57/06, (2006) IRBRD, vol 21, 1061
6. Tsang Yiu Kai v Insider Dealing Tribunal [2008] 1 HKC 376
7. R v Johnstone [2003] 1 WLR 1736
8. Sheldrake v DPP [2005] 1 AC 264
9. R v Ng Wing Keung Paul (1996) 6 HKPLR 299; [1997] HKLRD 142
10. D115/01, (2001) IRBRD, vol 16, 893
11. Khan v Customs and Excise Commissioners [2006] STC 1167
12. R (Federation of Technological Industries and others) v Customs and Excise Commissioners [2004] STC 1008
13. Wilson v First County Trust Ltd (No 2) [2004] 1 AC 816
14. Ozturk v Germany (1984) 6 EHRR 409
15. Mok Tsze Fung v The Commissioner of Inland Revenue [1962] HKLR 258

[2] This is an incorrect citation for BR17/72 IRBRD 97.

16. Hakansson v Sweden (1990) 13 EHRR 1
17. Tse Wai Chun v Solicitors Disciplinary Tribunal [2002] 3 HKLRD 712
18. Bryan v United Kingdom (1995) 21 EHRR 342
19. Attorney General of Hong Kong v Lee Kwong-kut [1993] AC 951
20. Willoughby and Halkyard, Encyclopaedia of Hong Kong Taxation, para II[20836]
21. Ferrazzini v Italy [2001] STC 1314
22. R v Benjafield [2003] 1 AC 1099
23. Weson Investment Ltd v Commissioner of Inland Revenue [2007] 2 HKLRD 567
24. BR 23/75, IRBRD, 187
25. Inland Revenue (Amendment) Ordinance 1969, Ord No 26/69
26. Legislative Council Hansard on the Inland Revenue (Amendment) (No 2) Bill 1975 – 2 April 1975, 18 June 1975 & 2 July 1975
27. Inland Revenue (Amendment) (No 4) Ordinance, Ord No 43/75

BOARD' S DECISION ON WHETHER TO ALLOW SUBMISSIONS ON HUMAN RIGHTS ISSUES

111. Mr Pannick submitted that it is well established that, other than in exceptional circumstances, it is wrong in principle to allow an extension of time for an appeal on the ground that a subsequent judgment has shown the previous understanding of the law to be wrong, citing Tsang Yiu Kai and others v Insider Dealing Tribunal [2008] 1 HKC 376, and argued that it must similarly follow that the appellant, whose appeal had already been heard, could not rely on Koon Wing Yee in an attempt to raise new human rights points out of time.

112. Mr Mok also referred to Tsang Yiu Kai and HKSAR v Hung Chan Wa FACC 1/2006 and argued that the principle there was only a recognition by the court of 'the practical necessity for finality in criminal process' and distinguishable from the present case. He cited Ngai Few Fung v Cheung Kwai Heung CACV 147/2007 and contended that a party was not permitted in subsequent proceedings to raise a matter which could have been raised in previous proceedings which had been determined only if it amounted to abuse of process, but there would 'rarely be a finding of abuse unless the later proceeding involves what the Court regards as unjust harassment of a party'. As the Chairman pointed out to Mr Mok during his submission, Ngai Few Fung was a case on *res judicata* in its wider sense with which we are not concerned.

113. There is some force in the respondent' s objections. Cases such as Han v Customs & Excise Commissioner [2001] 1 WLR 2253 (CA) and Janosevic v Sweden (2004) 38 EHRR 473 were decided a few years before the January 2007 hearing.

114. However, what is at stake here is the Board' s jurisdiction and the correct approach for penalty cases generally. Following what the Court of Appeal did in Yau Wah Yau v

Commissioner of Inland Revenue and HIT Finance Limited v Commissioner of Inland Revenue, we allow submissions to be made on human rights issues raised by ground 1A.

In Yau Wah Yau v Commissioner of Inland Revenue [2006] 3 HKLR 586, the Court of Appeal allowed the appeal but remitted the case back to be heard *de novo* by a differently constituted Board. However, prior to the order being drawn up, on 19 June 2006, the Commissioner filed a notice of motion for an order that the direction be rescinded or set aside and that the appeal be allowed. On 22 June 2006 it was ordered that no further steps be taken to draw up an order or enter judgment or otherwise perfecting the terms of the judgment of 30 May 2006 until final determination by the Court of Appeal of the notice of motion. After hearing further arguments, in a judgment handed down on 8 December 2006, the Court of Appeal held that remitting the case for a hearing *de novo* was not an option open to it and there would be no rehearing, see (2006-07) IRBRD, vol 21, 942.

However, in HIT Finance Limited v Commissioner of Inland Revenue (2006-07) IRBRD, vol 21, 972, the Court of Appeal made an order *nisi* that the matter be remitted to the Board with the questions that had been posed answered as per the judgments. The taxpayers applied to vary the order *nisi*. After hearing further arguments, the Court of Appeal ordered that the matter be remitted to the Board; that it was a matter for the Board to be masters of their own procedure within the context of their having held a hearing and issued a decision which was final subject to the case stated; that it must be left to the Board to decide whether to permit further evidence that might be considered essential in the light of the fact that the composition of the Board might have changed; and that it seemed clear that the parties were not entitled to call evidence which would in effect constitute a new case, see (2007-08) IRBRD, vol 22, 357.

115. No human rights issues are raised by the original grounds of appeal given in accordance with section 66(1) and it is not permissible for the appellant to raise them under the original grounds. However, we give our consent under section 66(3) to allow the appellant to rely on additional ground 1A. We admit the fresh evidence from the assistant commissioner. We note the requirement in China Map Limited and others v Commissioner of Inland Revenue, FACV 28-31 of 2007, 28 April 2008, at paragraph 9 – 10, which we will return in paragraph 126 below that 'if and whenever s.66(3) consent is sought, it should be sought fairly, squarely and unambiguously':

> '***Grounds of appeal : section 66(3) consent***
>
> *9. By its representative, each of the Taxpayers put forward the grounds of appeal that the profits in question "were capital in nature and were not assessable to Profits Tax or alternatively that the assessment was excessive". None of the Taxpayers pursued its alternative ground that the assessments were excessive. That left only one question raised by the grounds of appeal given in accordance with s.66(1). Did the profits in*

question arise from the sale of capital assets? But at the hearing before us, Mr Patrick Fung SC for the Taxpayers contended that there was an antecedent question. Were the profits in question from the carrying on of a trade, profession or business?

10. No such question is raised by the Taxpayers' grounds of appeal given in accordance with s.66(1). But Mr Fung contended that the Board is to be treated as having consented under s.66(3) to the Taxpayers relying on a fresh ground which raised such a question. For this contention, Mr Fung relied on an exchange between the Board's chairman and the Taxpayers' counsel (not Mr Fung or his junior Ms Catrina Lam). That exchange took place after the close of the evidence and during final speech. By its nature, such a question is fact-sensitive and its answer inherently dependent on evidence. For a tribunal of fact to entertain such a question after the close of the evidence would be unusual and plainly inappropriate if done without offering the party against whom the question is raised an opportunity to call further evidence. No such opportunity was offered to the Revenue. We do not think that the Board is to be treated as having consented under s.66(3) to the Taxpayers relying on a fresh ground which raised the antecedent question for which Mr Fung now contends. If and whenever s.66(3) consent is sought, it should be sought fairly, squarely and unambiguously. Nothing of that kind occurred in this case.'

BOARD' S DECISION ON GROUND 1A

116. We turn now to consider ground 1A. Significantly, the contention stops at the Commissioner level. The contention is that the Commissioner should have treated the assessment of additional tax under section 82A of the Ordinance as involving the determination of a 'criminal charge' within the meaning of Article 11 of the Hong Kong Bill of Rights and Article 39 of the Basic Law.

117. This contention is misconceived.

118. In Commissioner of Inland Revenue v Loganathan [2000] 1 HKLRD 914 at pages 918 – 919, Cheung J, as he then was, held that the Commissioner is an 'administrative authority', discharging administrative and not judicial functions in assessing additional tax:

*'**Administrative and not judicial functions***

One begins the task by asking what is the role of the Commissioner or Deputy Commissioner in assessing additional tax. Although a comparison had been

made to judicial proceedings in which the judge who hears the evidence will also give the verdict, in my view, it is inappropriate to compare the role of the Commissioner or the Deputy Commissioner to that of a judge. The Commissioner or Deputy Commissioner's role is an administrative one, namely, to assess the additional tax. There is no difference in principle between the Commissioner or Deputy Commissioner in assessing additional tax and that of the Commissioner in dealing with objections raised by a taxpayer against the assessment of tax by an assessor. The role is still an administrative one. This was the position in Mok Tsze Fung v CIR [1962] 1 HKTC 166[3] *which was concerned with s.64 of the Inland Revenue Ordinance of 1950 which provided for an appeal to the (p.919) Commissioner against the assessment by an assessor. Section 64 had since been replaced by provisions for making objections to the Commissioner. It was held by Mills-Owens J that during the hearing before the Commissioner under s.64, his role was an administrative one and not a judicial one, see also CIR v Board of Review, ex p Herald International Ltd*[4] *[1964] HKLR 224 and Encyclopaedia of Hong Kong Taxation, Vol.4, para.20299.*

The power to assess additional tax by the Commissioner or Deputy Commissioner does not make their function a judicial one. The Commissioner or the Deputy Commissioner in assessing additional tax does not hold a hearing. They are not required to hear evidence or observe the demeanour of witnesses. There are no opposing parties. In considering whether additional tax should be levied, they consider whether there was any incorrect return and the written representation made by the taxpayer. The task can be performed by more than one person so long as they are holders of the same rank. If a taxpayer is dissatisfied with the assessment of additional tax, he may appeal to the Board under s.82B of the Ordinance. The Board holds hearings to determine the appeal.'

119. Moreover, as Mr Pannick rightly pointed out, conferring the prosecution and punishment of minor offences on administrative authorities is not inconsistent with the Convention provided that the person concerned is enabled to take any decision thus made against before a tribunal that does offer the guarantees of the equivalent of Article 10 of the Bill of Rights, see Ozturk v Germany (1984) 6 EHRR 409 at paragraph 56:

'Article 6(3)(e) was thus applicable in the instant case. It in no wise follows from this, the Court would want to make clear, that the very principle of the system

[3] In Nina T H Wang v Commissioner of Inland Revenue, CACV 106 of 1991, Fuad VP pointed out that Mok Tsze Fung and Herald International Ltd were decided when section 64 of the Ordinance was in a somewhat different form, and warned that it would be dangerous to apply what was said in those cases to interpret section 64 in its amended form. It is clear from the passage cited that Cheung J was well aware of the amendments to section 64.

[4] See Footnote 3 above.

> *adopted in the matter by the German legislature is being put in question. Having regard to the large number of minor offences, notably in the sphere of road traffic, a Contracting State may have good cause for relieving its courts of the tasks of their prosecution and punishment. Conferring on the prosecution and punishment of minor offences on administrative authorities is not inconsistent with the Convention provided that the person concerned is enabled to take any decision thus made against him before a tribunal that does offer the guarantees of Article 6.'*

120. Ozturk was applied in Janosevic at paragraph 81 where it was held that Contracting States must be free to impose sanctions like tax surcharges even if they come to large amount:

> *'The tax authorities are administrative bodies which cannot be considered to satisfy the requirements of Art. 6(1) of the Convention. The Court considers, however, that Contracting States must be free to impose sanctions like tax surcharges even if they come to large amounts. Such a system is not incompatible with Art. 6(1) so long as the taxpayer can bring any such decision affecting him before a judicial body that has full jurisdiction including the power to quash in all respects, on questions of fact and law, the challenged decision.'*

121. The Commissioner is an administrator who cannot be considered to satisfy the requirements of our Article 10. However, the SAR Government must be free to impose additional tax which may come to large amounts. The Hong Kong system on additional tax is not incompatible with Article 10 of the BOR so long as a taxpayer can bring any such decision affecting him or her before a judicial body that has full jurisdiction including the power to quash in all respects, on questions of fact and law, the challenged decision.

122. An appeal from the Commissioner' s assessment of additional tax lies to the Board of Review.

123. Mr Pannick cited Ozturk in his written submission. Janosevic was cited by both parties and Mr Pannick placed heavy reliance on Janosevic. In the absence of any contention by Mr Mok that the Board is not a judicial body, we assume in favour of the respondent that it is. The Board is, and there is no contention by Mr Mok to the contrary, a competent[5], independent and impartial tribunal established by law to perform the ultimate function of deciding under section 68(8) of the Ordinance, incorporated by 82B(3) by reference, whether to confirm, reduce, increase or annul the additional tax assessment appealed against or to remit the case to the Commissioner with

[5] Suggestions were made by the Court of Final Appeal in Ing Baring Securities (Hong Kong) Limited v Commissioner of Inland Revenue [2008] 1 HKLRD 412 at paragraphs 4, 17, 113, 115 and 179 to re-consider the composition and operation of the Board. Bokhary PJ made it plain that 'this involves no criticism of those willing to take time out of their busy schedules to serve on the Board. What it does perhaps involve is whether it is fair to expect them to do so under present conditions.'

the opinion of the Board thereon. On remission, 'the Commissioner shall revise the assessment as the opinion of the Board may require and in accordance with such directions (if any) as the Board, at the request at any time of the Commissioner, may give concerning the revision required in order to give effect to such opinion'. The Board has full jurisdiction including the power to quash in all respects, on questions of fact and law, the challenged decision to assess the taxpayer to additional tax.

124. We heard no submission on whether section 67 applies to additional tax appeal. We say nothing about its applicability. If it does, there is no question about the competence of the Court of First Instance in the event of a 'leapfrog' appeal to the Court of First Instance. It is clearly a judicial body.

125. Ground 1A contains no challenge against the Board. There is no contention in ground 1A on how an appeal to the Board or to the Court of First Instance (if section 67 is applicable) is said to fall short of the Janosevic requirements. Nor is there any contention on how an appeal from the Board to the Court of First Instance under section 69 is said to fall short. Section 68(7) operates in favour of both the taxpayer and the Revenue.

126. If the appellant wishes to seek the Board's consent under section 66(3) to argue against the Board or the Court of First Instance as a tribunal offering the guarantees of Article 10 of the Bill of Rights, it should have sought the Board's consent 'fairly, squarely and unambiguously'. Like China Map Limited, 'nothing of that kind occurred in this case'. As stated in paragraph 105 above, Mr Mok had told the Board more than once that ground 1A was the only proposed additional ground that he was seeking the Board's permission under section 66(3) to rely on. Thus, it is not open to the appellant to argue against the Board or the Court of First Instance as a tribunal having full jurisdiction over the challenged additional tax assessment. Nor does ground 1A, as formulated, entitle the appellant to put forward such argument, whether on human rights or otherwise, as the appellant's legal advisers may feel able to. The Court of Final Appeal has ruled in China Map Limited that sections 66 (1) and (3) are there to be observed.

127. The further contention in ground 1A is that the consequence of section 82A being 'criminal' in nature is that both Articles 10 and 11 are triggered and that 'such' section is invalid by reason of breaches of Articles 11 and/or 10.

128. If section 82A is the section said to invalid, the contention is *non sequitur*. Invalidity does not follow from the mere fact of its being 'criminal' in nature.

129. If section 70 is the section referred to, the short answer is that the amount of profits understated and tax undercharged are agreed by the appellant as facts, see paragraph 81 above.

130. It is not open to the appellant to repudiate an agreed fact and it has not attempted to do so.

131. Ground 1A, as formulated, fails.

BOARD' S VIEWS ON ADDITIONAL TAX PROCEEDINGS AND APPEALS TO THE BOARD

132. Having disposed of ground 1A as formulated, it is not necessary for us to consider further human rights issues in respect of additional tax proceedings. We will discuss some of the issues briefly but do not propose to deal with all the points canvassed.

Reasons for enactment of administrative penalty

133. We start with the evidence given by the assistant commissioner, how additional tax came to be enacted as an administrative penalty and how the maximum penalty came to be increased to 3 times the size of the tax undercharged.

The assistant commissioner' s evidence

134. Ms AF states in her statement that:

> ' 2. The IRD is the government department responsible for the assessment and collection of profits tax, salaries tax and property tax levied under the Ordinance; that the effective operation of the HKSAR' s simple tax system with relatively low tax rates requires a high degree of compliance by taxpayers. It is also the primary duty of every taxpayer under the law to file timely and accurate tax returns to the IRD. The filing of incorrect returns causes loss in government revenue and is unfair to the community at large.
>
> 3. Revenue raised through profits tax, salaries tax and property tax by the IRD forms a significant portion of the HKSAR Government' s general revenue. I now attach at Annex 1 a table showing the percentage of profits tax, salaries tax, property tax and tax under personal assessment to the HKSAR Government' s general revenue for the years 1994/95 to 2006/07. The data are extracted from the IRD' s Annual Reports for the aforesaid years.
>
> 4. For tax assessment and collection purposes, tax returns are issued to the taxpayers to report assessable profits or losses (for profits tax), assessable income (for salaries tax) and assessable value (for property tax) based on which assessments are made. I now attach at Annex 2 a table showing the

number of assessments issued during the years 1994/95 to 2006/07. The data are extracted from Annual Estimates published by the HKSAR Government.

...

6. The tax reporting system in Hong Kong is an honour system. The IRD relies on the taxpayers to furnish true and correct returns.

7. To ensure compliance and to deter tax avoidance and evasion, tax returns will be selected for audit and investigation. If the returns are found to be incorrect, the Commissioner may initiate penal actions under Part XIV of the IRO, which includes the imposition of additional tax under section 82A.

8. Section 82A was first introduced in 1969 pursuant to the recommendation in Part II of the Report of the Inland Revenue Ordinance Review Committee.'

'**Annex 1**

Revenue collected by Inland Revenue Department

(Data extracted from Annual Reports of Inland Revenue Department)

Year	Total earnings & profits tax (1) ($ billion) (a)	Total government general revenue ($ billion) (b)	Total earnings & profits tax to government general revenue (a) / (b)
1994/95	74	151	49%
1995/96	77	153	50%
1996/97	84	174	48%
1997/98	92	229	40%
1998/99	76	179	42%
1999/00	67	162	41%
2000/01	74	179	41%
2001/02	78	157	50%
2002/03	73	148	49%
2003/04	80	175 (2)	46%
2004/05	97	230	42%
2005/06	112	205	55%
2006/07	115	229	50%

Notes:

(1) Total earnings & profits tax includes profits tax, salaries tax, interest tax, property tax and personal assessment.
(2) Total government revenue for 2003/04 excludes a transfer of $120 billion from the Land Fund.'

' **Annex 2**

Number of assessments made by Inland Revenue Department

(Data extracted from the Controlling Officer's Reports of the Inland Revenue Department in the Annual Estimates published by the HKSAR government)

Year	Profits tax ('000)	Salaries tax ('000)	Property tax ('000)	Personal assessment ('000)	Total ('000)
1994/95	382	2,084	326	192	2,984
1995/96	463	2,214	392	322	3,391
1996/97	477	2,288	436	384	3,585
1997/98	472	2,277	494	384	3,627
1998/99	427	2,250	471	367	3,515
1999/00	407	2,165	473	341	3,386
2000/01	398	2,120	487	355	3,360
2001/02	379	2,092	472	363	3,306
2002/03	375	2,108	476	342	3,301
2003/04	370	2,021	471	324	3,186
2004/05	390	2,021	480	328	3,219
2005/06	381	2,051	494	307	3,233
2006/07	408	2,127	506	328	3,369'

Part II of the Report of the Inland Revenue Ordinance Review Committee

135. The Inland Revenue Ordinance Review Committee was chaired by the Financial Secretary. Members included the Commissioner of Inland Revenue, Crown Counsel and prominent professional accountant and lawyer. The Committee was appointed by the Governor to consider and advise on certain matters connected with the Ordinance which had been raised by the Commissioner, the Hong Kong General Chamber of Commerce and certain other bodies.

136. In Part II of its Report dated 14 March 1968, the Committee reported that:

'**OFFENCES & PENALTIES**

394. The Commissioner asked us to review Part XIV of the Ordinance in the light of certain proposals he wished to submit. The proposals were—

(1) To provide an administrative penalty for certain offences under the Ordinance as an alternative to Court prosecution for the offences.

(2) The correction of an anomaly in the penalty which may be imposed under Section 82 on summary conviction or on indictment. The section provides that the Court may impose, in addition to a fine, a penalty of "treble the amount of tax for which the person who evaded or attempted to evade tax is liable under the Ordinance for the year of assessment in respect of which the offence was committed." The penalty should be treble the amount of tax undercharged as a consequence of the offence or which would have been undercharged if the offence had not been detected before assessment.

(3) The modification of the penalty provisions in both Section 80(2) and Section 82(1) so that the additional penalty which a court is empowered to impose on conviction—the amount of tax undercharged in Section 80(2) and treble the amount of tax in Section 82(1)—shall on an order of the Court be made payable to the Commissioner.

395. In giving his reasons for the first proposal the Commissioner said that the offences for which he sought an administrative penalty—i.e. a penalty which he would be empowered to impose in certain circumstances—were—

(*a*) the making of any incorrect return, incorrect statement or the giving of incorrect information which, if accepted by the Department, would result in the person being undercharged to tax,

(*b*) any failure to lodge a return which successfully defers the payment of tax, and

(*c*) any failure to notify chargeability to tax which enables the person to avoid paying tax.

The Commissioner did not seek such a penalty in respect of offences under Section 82 which he proposed should be dealt with by Court prosecution or by compounding the offence.

396. Our attention was directed to the views expressed by the Royal Commission on The Taxation of Profits and Income, 1955 Cmd. 9474. We attach at Appendix K an extract of the relevant paragraphs of the Commission' s Final Report and it will be noted in paragraph 1070 thereof that the Commission favoured the imposition by an appropriate tribunal of penalties for all offences, except those which depend upon the presence of fraud.

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. He envisaged that the full penalty equal to 100% of the tax undercharged would only be imposed for aggravated offences such as might be considered as borderline cases for prosecution under Section 82(1).

399. The Ordinance provides in Section 54 that proceedings under Part XIV may not be taken against the executor in respect of any act or default of the deceased person. As a consequence the offences for which a person would be punishable under Section 80(2) and Section 82(1) if he is apprehended during his lifetime, go unpunished if they are only uncovered after he dies. The introduction of an administrative penalty which may be recovered by civil proceedings would remedy this situation and the penalty could be made a

charge on the deceased's estate as is the law in the U.K. (see Section 56(5) U.K. Finance Act 1960).

400. Whilst we were in general agreement on the principle of providing an administrative penalty as an alternative to Court proceedings for at least certain offences which at present are punishable under Part XIV, we considered that the administration should not be empowered to impose a heavier monetary penalty for an offence than the maximum penalty which the Court could impose for the same offence. It appeared to us that if a person failed to notify the Department that he was chargeable to tax and the tax found to be due by him for any year exceeded $2,000 the administrative penalty as proposed could exceed the maximum fine ($2,000) which the Court may impose on conviction for the offence under Section 80(1). Consequently, whilst we considered that, subject to the reservation which follows, an administrative penalty should be provided as an alternative to prosecution for the offences described in sub-paragraph (*a*) of paragraph 395 above, we did not think such a penalty was suitable for application to offences under sub-paragraphs (*b*) and (*c*).

401. Our reservation on the views expressed above is that a taxpayer on whom an administrative penalty is imposed should be given a right of appeal to some independent tribunal. The Board of Review appeared to us to be particularly suited to consider such appeals as it may well have to hear appeals by taxpayers on assessments or additional assessments to which administrative penalties have been added. Whilst an appellant may appeal to the Court from a decision of the Board where his case involves some question of law, we considered that the Board should, in the case of a penalty, be the final arbiter on the question of quantum as it is already in the case of an assessment.

402. We agreed with both of the proposals in (2) and (3) of paragraph 394. The first of these corrects an anomaly. The second, which requires the payment to the Department of the additional or special penalties related to the quantum of tax undercharged is, in our opinion, appropriate. The Department's revenue collections will then reflect its efforts in recovering back duty from taxpayers so convicted whilst the Court collects the fine.

403. WE RECOMMEND—

(1) (a) that, as an alternative to prosecution or compounding the offences described in subsection (2) of Section 80, the Commissioner be empowered to impose a penalty not exceeding an amount equal to the tax which has been

undercharged in consequence of the incorrect return, statement or information or which would have been undercharged if the return, statement or information had been accepted as correct. The penalty is to be additional to the tax payable on any assessment under Section 60 and should be recoverable by the same process as if it were tax due on an assessment made under the provisions of Part X;

(b) that, if the Commissioner imposes an administrative penalty for any offence under Section 80(2), he be precluded from initiating any prosecution for the same offence;

(c) that there be a right of appeal to the Board of Review on the question of the penalty apart from the normal right of appeal on the correctness of the assessment;

(d) that the Board of Review be authorized to review the penalty in the same way as if it were an assessment against which a taxpayer has appealed and to increase, reduce or annul the penalty after considering it in relation to the circumstances of the taxpayer's incorrect return, statement or information which resulted in an undercharge of tax and the excuse offered by the offender;

(2) the correction of the anomaly in Section 82 which at present provides a fine of two thousand dollars and treble the amount of tax for which the person is liable for the year of assessment by making it treble the amount of tax undercharged as a consequence of the evasion or which would have been undercharged if the evasion had not been detected before assessment;

(3) the modification of the penalty provisions in both Section 80(2) and Section 82(1) so that the additional penalty which a court is empowered to impose on conviction—the amount of tax undercharged in Section 80(2) and treble the amount of tax in Section 82(1)—shall be ordered by the Court to be paid to the Commissioner.'

Introduction of additional tax in 1969

137. The recommendations to introduce an administrative penalty were implemented by section 38 of the Inland Revenue (Amendment) Ordinance 1969, Ord No 26/69. The maximum

penalty was the amount of the tax undercharged. In paragraph 11 of the appellant' s second written submission, Mr Mok referred to the Commissioner' s submission (see paragraph 398 of the Report) and stated that:

> 'The legislature, however, did not accept this but vastly raised the level of penalty up to 300% of the tax undercharged, ie up to the level of penalty to be imposed for conviction under section 80(2) of the IRO.'

This statement is factually incorrect in two respects. The maximum under the 1969 amendment ordinance was the amount of the tax undercharged, see paragraph 138 below. Secondly, the maximum penalty under section 80(2) as at 1969 was the amount of the tax undercharged, not 3 times, see paragraph 403(3) of the Report. The maximum amounts under section 80(2) and 82A were trebled in 1975, see paragraph 145 below.

138. Sections 82A and 82B, as added by section 38 of Ord No 26/69, provided as follows:

> *'82A. (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 a partnership; or*
>
> *(b) makes an incorrect statement in connexion 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 to tax or the liability of any other person or of a partnership,*
>
> *shall, if no prosecution under subsection (2) of section 80 or subsection (1) of section 82 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 the amount of tax which has been undercharged in consequence of the incorrect return, statement or information, or which would have been so undercharged if the return, statement, or information had been accepted as correct.*

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

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

(a) cause notice to be given to the person he proposes so to assess which shall—

(i) inform such person of the alleged incorrect return, incorrect statement or incorrect information in respect of which the Commissioner or the deputy commissioner intends to assess additional tax under subsection (1);

(ii) include a statement that such person has the right to submit written representations to him with regard to the proposed assessment on him of additional tax;

(iii) specify the date, which shall not be earlier than twenty-one days from the date of service of the notice, by which representations which such person may wish to make under sub-paragraph (ii) must be received;

(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.

(5) Notice of intention to assess additional tax and notice of an assessment to additional tax shall be given in the same manner as is provided in subsection (2) of section 58 in respect of a notice of assessment under section 62.

(6) where a person who is liable to be assessed to additional tax has died, an assessment to additional tax may be made on his executor, and the additional tax shall be recovered as a debt due from and payable out of the deceased person's estate.

(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 subsection (2) of section 80 or subsection (1) of section 82.

82B. (1) Any person who has been assessed to additional tax may, within one month after notice of assessment is given to him, 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 a copy of the notice of assessment and a statement of the grounds of appeal therefrom.

(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) Subsections (2) and (3) of section 66 and sections 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.'

Increase of the administrative penalty in 1975

139. In BR23/75, IRBRD, 187 at page 188, the Board [L J D' Almada Remedios, Ressel Fok, D A Graham & C H Wong] made a passing comment on an amendment of section 82A increasing the maximum from double to treble the amount of tax undercharged:

'Under section 82A of the Inland Revenue Ordinance, the Appellant is liable to a penalty of double the amount of tax which has been undercharged. (This

> *section has since been amended to increase the penalty to treble the amount but the amendment has no application to the case under review).'*

We were unable to find any amendment ordinance between 1969 and 1975 increasing the amount of additional tax from the amount of the tax undercharged to double the amount of tax undercharged.

140. By letter dated 23 May 2008, the Clerk wrote to both parties to ask for assistance at the hearing on:

(a) whether the reference to double the amount was erroneous; and

(b) how section 8 of the Inland Revenue (Amendment) (No 4) Ordinance 1975, Ord 43/75, came to be enacted.

141. The appellant did not respond to the Clerk' s letter.

142. Mr Pannick helpfully confirmed that the reference was erroneous and provided us with a copy of the Legislative Council Hansard on Ord 43/75 and a copy of that amendment Ordinance.

143. The Hansard recorded what the Financial Secretary said when he moved the second reading of the amendment bill on 2 April 1975:

> 'THE FINANCIAL SECRETARY moved the second reading of:—"A bill to amend the Inland Revenue Ordinance."
>
> He said:—Sir, during the course of my 1974 budget speech I said that the present investigation powers and penalty provisions in Parts IX and XIV of the Inland Revenue Ordinance needed strengthening. The bill at present before Council is intended to achieve just this. Honourable Members will no doubt recall that in 1969, following the recommendations of the last Inland Revenue Ordinance Review Committee, extended powers, which included the right to impose an administrative penalty in cases of tax evasion, were given to the Commissioner of Inland Revenue. These amendments, coupled with the establishment of a special Investigation Section in the Inland Revenue Department, have certainly had their effect—the total amount of tax and penalties imposed in the five years since 31st March 1969 amounted to $35 million, which, of course, excludes the unquantifiable, but nevertheless known, effect that action of this sort has on the accuracy of current returns. Nevertheless, it is the view of the Commissioner that there is still a lot that can be done in this field but he is hindered by the fact that first this is proving an expensive and time-consuming operation and that secondly the penalties are not sufficiently high to act as a deterrent

to some would-be evaders. As recently as the year ended 31st March 1974, the average understatement of earnings and profits in the cases finalized by the Investigation Section was as high as 79 per cent. This is a frightening figure, particularly at a time when we need every cent we can lay our hands on—legitimately lay our hands on—to meet the ever increasing demands on General Revenue.

Whilst some of the amendments are of a comparatively minor nature—some of the amendments proposed in this bill—and are adequately explained in the explanatory memorandum, there are two which do call for particular comment.

...

The other amendment or really group of amendments which merits elaboration is the increase in the penalties which the courts may impose from $2,000 plus a fine equal to the amount of tax undercharged, to $2,000 plus treble the amount of the tax undercharged. This is provided for in clause 6 and it should also be noted that by clause 7 the Commissioner is empowered, subject to a right of appeal by the taxpayer, to impose an administrative penalty known as "additional tax". These amendments also bring into the net for the first time the case where the taxpayer just sits back and quietly fails to submit a return at all.

Clearly these amendments are intended as a deterrent and also as a punishment to the guilty. It will be evident from the figures I have already given to honourable Members that the existing penalty is simply not sufficient as a deterrent. As regards punishment, it will I hope be readily appreciated that, because of high interest rates and inflation, even where the maximum penalty of 100 *per cent* is imposed as it is in the worst type of case, the taxpayer is often no worse off than if he had paid the tax in due time. Furthermore, it must be remembered that with a standard rate of 15 *per cent*, except for corporations where the rate is now happily 16½ *per cent*, the worst that can happen to an offender if he is caught is to pay tax at 30 or 33 *per cent*—to put it at its lowest level it is worth taking a sporting chance, although let me say at once that I consider there is nothing sporting about the tax evader (*laughter*). His action, if undetected, simply shifts the burden of the tax on to those who are honest enough to contribute according to law. He deserves no sympathy from this Council and I trust he will get none. I would also remind honourable Members that, in some neighbouring countries, the penalties when added to the tax are confiscatory in that in some cases they can exceed the amount of income on which they are levied. Even the maximum 300 *per cent* penalty now proposed will still not be anywhere near confiscatory in Hong Kong.

An additional motive behind the increase in the penalty is to give the Commissioner a greater degree of flexibility in fixing the amount of the penalty. At present, as I have

already indicated, if one does no more than recover what one should have paid to the Exchequer in the first instance, the penalty would very often have to be close to the 100 *per cent* margin. There is very little therefore that the Commissioner can offer by way of inducement to a taxpayer to make a clean breast of things and submit corrected returns. Furthermore, it has been the Commissioner' s experience that once having been caught out, the taxpayer often sits back and leaves it to the department to build up the necessary statements from which his true profits can be ascertained. This is a laborious, painstaking task and it is ironic that this should be done at Government' s expense when the fault lies entirely with the taxpayer. There is however an insufficient range of penalties for the Commissioner to hold out some inducement to the taxpayer at this stage to pay his own accountant to do his own work at his own expense.

In this connection, I should like to place on record what the Commissioner' s practice in relation to the full voluntary disclosure of tax evasion is. Where offences under the Inland Revenue Ordinance have been committed, the Commissioner may institute prosecution under Part XIV of the ordinance. He is, however, also given power to compound these offences, that is to say, to accept a monetary settlement instead of sanctioning the institution of a prosecution. Alternatively, he is given the power to impose additional tax in lieu of prosecution. Although no undertaking can be given as to whether or not the Commissioner will refrain from prosecution in the case of any particular person, it is the practice of the Commissioner to be influenced by the fact that a person has made a full confession of any offence to which he has been a party and has given full facilities for investigation and has provided corrected returns accompanied by detailed statements in support of these returns. These facts will also have a favourable bearing on the amount of the penalty or where applicable, additional tax, in settlement.'

144. At the resumption of debate on second reading, the Financial Secretary said on 18 June 1975 that:

'I of course welcome [honourable Members'] support of the Government' s objective of reducing the incidence of tax evasion, not only to protect the revenue – and if the revenue is not protected our low and narrowly based fiscal system is put at risk – but also to re-assure honest taxpayers that they alone are not expected to carry the burden of public expenditure.'

145. Sections 6, 8 and 9 of Ord No 43/75 provided that:

'6. Section 80 of the principal Ordinance is amended—

(a) in subsection (1) —

(i) by deleting, in paragraph (a), "section 51(1) or (3)" and substituting the following—

"section 51(3)"; and

(ii) by deleting, in paragraph (c), "51(2), (6)," and substituting the following—

"51(6),";

(b) by deleting subsection (1A);

(c) by deleting subsection (2) and substituting the following—

"(2) 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 a partnership;

(b) makes an incorrect statement in connexion with a claim for any deduction or allowance under this Ordinance;

(c) gives any incorrect information in relation to any matter or thing affecting his own liability to tax or the liability of any other person or of a partnership;

(d) fails to comply with the requirements of a notice given to him under section 51(1); or

(e) fails to comply with section 51(2),

shall be guilty of an offence: Penalty a fine of two thousand dollars and a further fine of treble the amount of tax which 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 which has been undercharged in consequence of the failure to comply with a notice under section 51(1) or a failure to comply with

section 51(2), or which would have been undercharged if such failure had not been detected."; and

(d) by inserting, after subsection (2), the following new subsections—

"(2A) In the case of an offence under paragraph (d) of subsection (2), the court may order the person convicted to comply with the requirements of the notice given to him under section 51(1) within such time as may be specified in the order.

(2B) Any person who does not comply with an order of the court under subsection (1) or (2A) or under section 51(4B)(b) shall be guilty of an offence: Penalty a fine of five thousand dollars".'

'8. Section 82A of the principal Ordinance is amended—

(a) in subsection (1) —

(i) by deleting the comma at the end of paragraph (c) and substituting the following—

"; or";

(ii) by inserting, after paragraph (c), the following new paragraphs—

"(d) fails to comply with the requirements of a notice given to him under section 51(1); or

(e) fails to comply with section 51(2),"; and

(iii) by deleting "the amount of tax which has been undercharged in consequence of the incorrect return, statement or information, or which would have been so undercharged if the return, statement, or information had been accepted as correct" and substituting the following—

"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 a failure to comply with section 51(2), or which would have been undercharged if such failure had not been detected".

(b) in subsection (4) by deleting sub-paragraph (i) of paragraph (a) and substituting the following—

"(i) inform such person of the alleged incorrect return, incorrect statement or incorrect information or alleged failure to comply with the requirements of the notice given to him under section 51(1) or the alleged failure to comply with section 51(2) in respect of which the Commissioner or deputy commissioner intends to assess additional tax under subsection (1);"; and

(c) by inserting, after subsection (4), the following new subsection—

"(4A) Notwithstanding subsection (4), if the Commissioner or deputy commissioner is of the opinion that the person he proposes to assess to additional tax under subsection (1) is about to leave the Colony, he need not serve a notice under paragraph (a) of subsection (4), but may assess that person to additional tax under subsection (1).".

9. Section 82B of the principal Ordinance is amended by deleting subsection (1) and substituting the following—

"(1) Any person who has been assessed to additional tax under section 82A may, within one month after notice of assessment is given to him, 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—

(a) a copy of the notice of assessment;

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

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

(d) a copy of any written representations made under subsection (4) of section 82A.".'

Basic Law

146. We turn now to the constitutional provisions and the relevant provisions in the Ordinance (including provisions relevant to the other grounds of appeal).

147. The following articles in the Basic Law are relevant:

Article 6 - *The Hong Kong Special Administrative Region shall protect the right of private ownership of property in accordance with law.*

Article 8 - *The laws previously in force in Hong Kong, that is, the common law, rules of equity, ordinances, subordinate legislation and customary law shall be maintained, except for any that contravene this Law, and subject to any amendment by the legislature of the Hong Kong Special Administrative Region.*

Article 18 - *The laws in force in the Hong Kong Special Administrative Region shall be this Law, the laws previously in force in Hong Kong as provided for in Article 8 of this Law, and the laws enacted by the legislature of the Region ...*

Article 39 - *The provisions of the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social and Cultural Rights, and international labour conventions as applied to Hong Kong shall remain in force and shall be implemented through the laws of the Hong Kong Special Administrative Region.*

The rights and freedoms enjoyed by Hong Kong residents shall not be restricted unless as prescribed by law. Such restrictions shall not contravene the provisions of the preceding paragraph of this Article.

Article 64 - *The Government of the Hong Kong Special Administrative Region must abide by the law and be accountable to the Legislative Council of the Region: it shall implement laws passed by the Council and already in force; it shall present regular policy addresses to the Council; it shall answer questions raised by members of the Council; and it shall obtain approval from the Council for taxation and public expenditure.*

Article 73 - *The Legislative Council of the Hong Kong Special Administrative Region shall exercise the following powers and functions ... (a) To approve taxation and public expenditure ...*

Article 105 - *The Hong Kong Special Administrative Region shall, in accordance with law, protect the right of individuals and legal persons to the acquisition, use, disposal and inheritance of property and their right to compensation for lawful deprivation of their property.*

Such compensation shall correspond to the real value of the property concerned at the time and shall be freely convertible and paid without undue delay.

The ownership of enterprises and the investments from outside the Region shall be protected by law.

Article 106 - *The Hong Kong Special Administrative Region shall have independent finances.*

The Hong Kong Special Administrative Region shall use its financial revenues exclusively for its own purposes, and they shall not be handed over to the Central People's Government.

The Central People's Government shall not levy taxes in the Hong Kong Special Administrative Region.

Article 107 - *The Hong Kong Special Administrative Region shall follow the principle of keeping the expenditure within the limits of revenues in drawing up its budget, and strive to achieve a fiscal balance, avoid deficits and keep the budget commensurate with the growth rate of its gross domestic product.*

Article 108 - *The Hong Kong Special Administrative Region shall practise an independent taxation system.*

The Hong Kong Special Administrative Region shall, taking the low tax policy previously pursued in Hong Kong as reference, enact laws on its own concerning types of taxes, tax rates, tax reductions, allowances and exemptions, and other matters of taxation.

Hong Kong Bill of Rights Ordinance

148. Section 6(1) of the Hong Kong Bill of Rights Ordinance, Chapter 383, ('BORO') is relevant:

Section 6(1) - *A court or tribunal ... (b) in other proceedings within its jurisdiction in which a violation or threatened violation of the Bill of Rights is relevant, may grant such remedy or relief, or make such order, in respect of such a breach, violation or threatened violation as it has power to grant or make in those proceedings and as it considers appropriate and just in the circumstances.*

149. The following articles in the Hong Kong Bill of Rights ('BOR') under the BORO are relevant:

Article 10 - *Equality before courts and right to fair and public hearing*

All persons shall be equal before the courts and tribunals. In the determination of any criminal charge against him, or of his rights and obligations in a suit at law, everyone shall be entitled to a fair and public hearing by a competent, independent and impartial tribunal established by law. The press and the public may be excluded from all or part of a trial for reasons of morals, public order (ordre public) or national security in a democratic society, or when the interest of the private lives of the parties so requires, or to the extent strictly necessary in the opinion of the court in special circumstances where publicity would prejudice the interests of justice; but any judgment rendered in a criminal case or in a suit at law shall be made public except where the interest of juvenile persons otherwise requires or the proceedings concern matrimonial disputes or the guardianship of children. [cf. ICCPR Art. 14.1]

Article 11 - *Rights of persons charged with or convicted of criminal offence*

(1) Everyone charged with a criminal offence shall have the right to be presumed innocent until proved guilty according to law ... [cf. ICCPR Art. 14.2 to 7]

Convention for the Protection of Human Rights and Fundamental Freedoms (1950)

150. The following articles in the Convention for the Protection of Human Rights and Fundamental Freedoms (1950) ('the Convention') are relevant:

Article 1 of Protocol 1 - *Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law. The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties.*

Article 6

1. In the determination of his civil rights and obligations or of any criminal charge against him, every one is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law. Judgment shall be pronounced publicly but the press and public may be excluded from all or part of the trial in the interests of morals, public order or national security in a democratic society, where the interests of juveniles or the protection of the private life of the parties so require, or to the extent strictly necessary in the opinion of the court in special circumstances where publicity would prejudice the interest of justice.

2. Everyone charged with a criminal offence shall be presumed innocent until proved guilty according to law ...

The Ordinance

151. The 1986 version of sections 16(1)(a) and 16(2)(d) provided that:

'(1) In ascertaining the profits in respect of which a person is chargeable to tax under this Part for any year of assessment there shall be deducted all outgoings and expenses to the extent to which they are incurred during the basis period for that year of assessment by such person in the production of profits in respect of which he is chargeable to tax under this Part for any period, including-

(a) where the conditions set out in subsection (2) are satisfied, sums payable by such person by way of interest upon any money borrowed by him for the purpose of producing such profits, and sums payable by such person by way of legal fees, procuration fees, stamp duties and other expenses in connection with such borrowing; (Replaced 2 of 1971 s. 11. Amended 36 of 1984 s. 4)

...

(2) The conditions referred to in subsection (1)(a) are that-

...

(d) the money has been borrowed from a financial institution or an overseas financial institution and the repayment of the principal or interest is not secured or guaranteed either in whole or in part, and whether directly or indirectly, by any instrument executed or any undertaking given by or on behalf of the borrower or an associate of the borrower against a deposit made with that or any other financial institution or overseas financial institution where any sums payable by way of interest on the deposit are not chargeable to tax under this Ordinance; (Amended 7 of 1986 s. 4; 63 of 1997 s. 2)'

152. The 1993 version of section 51(1) provided 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 –

(a) property tax, salaries tax or profits tax; or

(b) property tax, salaries tax and profits tax,

under Parts II, III, IV, XA, XB, and XC, containing such particulars and in such form as may be specified by the Board of Inland Revenue. (Replaced 52 of 1993 s. 5).'

Section 51(1) was amended in 2003 and the current version 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 –

(a) property tax, salaries tax or profits tax; or

(b) property tax, salaries tax and profits tax,

under Parts II, III, IV, XA, XB, and XC. (Replaced 52 of 1993 s. 5. Amended 5 of 2003 s. 7).'

153. Sections 51(2), (2A) and (5) provide that:

'(2) Every person chargeable to tax for any year of assessment shall inform the Commissioner in writing that he is so chargeable not later than 4 months after the end of the basis period for that year of assessment unless he has already been required to furnish a return under the provisions of subsection (1). (Replaced 49 of 1956 s. 37)'

'(2A) An assessor shall give notice to any individual who has elected to be personally assessed under Part VII requiring that individual within a reasonable time stated in the notice to furnish a return in the specified form of his total income assessable under this Ordinance. (Added 43 of 1989 s. 16)'

'(5) 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 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.'

154. Section 60(1) provides that:

'Where it appears to an assessor that for any year of assessment any person chargeable with tax has not been assessed or has been assessed at less than the

proper amount, the assessor may, within the year of assessment or within 6 years after the expiration thereof, assess such person at the amount or additional amount at which according to his judgment such person ought to have been assessed, and the provisions of this Ordinance as to notice of assessment, appeal and other proceedings shall apply to such assessment or additional assessment and to the tax charged thereunder: (Amended 16 of 1951 s. 10; 49 of 1956 s. 44)

Provided that-

(a) (Repealed 2 of 1971 s. 39)

(b) where the non-assessment or under-assessment of any person for any year of assessment is due to fraud or wilful evasion, such assessment or additional assessment may be made at any time within 10 years after the expiration of that year of assessment. (Amended 49 of 1956 s. 44).'

155. Section 66(1) & (3) provide that:

'(1) Any person (hereinafter referred to as the appellant) who has validly objected to an assessment but with whom the Commissioner in considering the objection has failed to agree may within-

(a) 1 month after the transmission to him under section 64(4) of the Commissioner's written determination together with the reasons therefor and the statement of facts; or

(b) such further period as the Board 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 a copy of the Commissioner's written determination together with a copy of the reasons therefor and of the statement of facts and a statement of the grounds of appeal. (Replaced 2 of 1971 s. 42)'

'(3) Save with the consent of the Board and on such terms as the Board may determine, an appellant may not at the hearing of his appeal rely on any grounds of appeal other than the grounds contained in his statement of grounds of appeal given in accordance with subsection (1). (Replaced 35 of 1965 s. 32)'

156. Section 67 provides that:

'(1) Where notice of appeal is given to the Board under section 66, the appellant or the Commissioner may give notice in writing in accordance with this section that he desires the appeal to be transferred to the Court of First Instance:

Provided that if both the appellant and the Commissioner give such notice, the notice given by the Commissioner shall have no effect and shall be deemed not to have been given.

(2) A notice under subsection (1) shall, if given by the appellant, be given to the Commissioner, or, if given by the Commissioner, be given to the appellant within-

(a) 21 days after the date on which the notice of appeal is received by the clerk to the Board; or

(b) such further time as the Board may in any particular case permit upon application in writing by the appellant or the Commissioner,

and the person giving such notice shall at the same time send a copy thereof to the Board. (Amended 63 of 1997 s. 5)

(3) If the person to whom notice is given under subsection (1) consents thereto, he shall, within-

(a) 21 days after the date on which the notice is given; or

(b) such further time as the Board may in any particular case permit upon application in writing by the person,

notify his consent in writing to the Board and serve a copy of such notification on the person giving the notice, and on receipt of such notification by the Board the clerk to the Board shall transmit the notice of appeal to the Court of First Instance together with the documents delivered to the Board under this section and section 66(1) in connection with the appeal. (Amended L.N. 262 of 1985; 63 of 1997 s. 5)

(4) An appeal in respect of which notice of appeal is transmitted to the Court of First Instance under subsection (3) shall be heard and determined by the Court of First Instance as in all respects an appeal to the Court of

First Instance against the determination to which the notice of appeal relates.

(5) The following provisions shall apply in relation to the hearing of an appeal under this section-

(a) the Court of First Instance shall give 14 clear days' notice to the appellant and the Commissioner of the date fixed for the hearing of the appeal, and may adjourn the hearing to any other date as the Court of First Instance may deem fit;

(b) the Commissioner shall be entitled to appear and be heard at the hearing of the appeal;

(c) save with the leave of the Court of First Instance and on such terms as to costs or otherwise as the Court of First Instance may order, the appellant shall not at the hearing of the appeal rely on any grounds of appeal other than the grounds contained in his statement of grounds of appeal given with the notice of appeal under section 66(1);

(d) the onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant;

(e) the Court of First Instance may summon any person appearing to the Court of First Instance to be able to give evidence respecting the appeal to attend at the hearing of the appeal and may examine any such person as a witness on oath or otherwise.

(6) An appeal in respect of which notice of appeal is transmitted to the Court of First Instance under subsection (3) shall not be withdrawn without the leave of the Court of First Instance and except on such terms as to costs or otherwise as the Court of First Instance may order.

(7) In determining an appeal under this section, the Court of First Instance may-

(a) confirm, reduce, increase or annul the assessment determined by the Commissioner;

(b) make any assessment which the Commissioner was empowered to make at the time he determined the assessment, or direct the

Commissioner to make such an assessment, in which case an assessment shall be made by the Commissioner so as to conform to that direction;

(c) make such order as to costs as the Court of First Instance may deem fit.

(Added 12 of 1979 s. 3. Amended 25 of 1998 s. 2)'

157. Sections 68(3) – (9) provide that:

'(3) The assessor who made the assessment appealed against or some other person authorized by the Commissioner shall attend such meeting of the Board in support of the assessment.

(4) The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant. (Replaced 35 of 1965 s. 34)

(5) All appeals shall be heard in camera, but any appeal may be reported in such publications as may be approved by the Secretary for Justice in such a manner that the identity of the appellant is not disclosed. (Replaced 2 of 1971 s. 43. Amended L.N. 362 of 1997)

(6) The Board shall have power to summon to attend at the hearing any person whom it may consider able to give evidence respecting the appeal and may examine him as a witness either on oath or otherwise. Any person so attending may be allowed by the Board any reasonable expenses necessarily incurred by him in so attending.

(7) At the hearing of the appeal the Board may, subject to the provisions of section 66(3), admit or reject any evidence adduced, whether oral or documentary, and the provisions of the Evidence Ordinance (Cap 8), relating to the admissibility of evidence shall not apply.

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

(b) Where a case is so remitted by the Board, the Commissioner shall revise the assessment as the opinion of the Board may require and in accordance with such directions (if any) as the Board, at the request at any time of the Commissioner, may give concerning the

revision required in order to give effect to such opinion. (Replaced 35 of 1965 s. 34)

(9) Where under subsection (8), the Board does not reduce or annul such assessment, the Board may order the appellant to pay as costs of the Board a sum not exceeding the amount specified in Part I of Schedule 5, which shall be added to the tax charged and recovered therewith. (Amended 11 of 1985 s. 5; 56 of 1993 s. 27; 12 of 2004 s. 14)'

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

159. Section 69(1) provides that:

'The decision of the Board shall be final:

Provided that either the appellant or the Commissioner may make an application requiring the Board to state a case on a question of law for the opinion of the Court of First Instance. Such application shall not be entertained unless it is made in writing and delivered to the clerk to the Board, together with a fee of the amount specified in Part II of Schedule 5, within 1 month of the date of the Board's decision. If the decision of the Board shall be notified to the Commissioner or to the appellant in writing, the date of the decision, for the purposes of determining the period within which either of such persons may require a case to be stated, shall be the date of the communication by which the decision is notified to him.'

160. In respect of a salaries or profits tax assessment which a taxpayer has not validly objected to under section 64, section 70, so far as relevant, provides as follows:

'Where no valid objection ... has been lodged within the time limited by this Part against an assessment as regards the amount of the assessable income [for salaries tax] or profits [for profits tax] ... assessed thereby, ... the assessment as made ... shall be final and conclusive for all purposes of this Ordinance as regards the amount of such assessable income or profits ... (Amended 49 of 1956 s. 51; 35 of 1965 s. 35; 40 of 1972 s. 9; 7 of 1979 s. 4; 12 of 2004 s. 16)

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. (Amended 35 of 1965 s. 35)'

161. In respect of a salaries or profits tax assessment which a taxpayer has objected to and the Commissioner has determined the objection but the taxpayer has not appealed to the Board, section 70, so far as relevant, provides as follows:

> *'Where ... the amount of such assessable income or profits ... has been determined on objection ... the assessment as ... determined on objection ... shall be final and conclusive for all purposes of this Ordinance as regards the amount of such assessable income or profits ... (Amended 49 of 1956 s. 51; 35 of 1965 s. 35; 40 of 1972 s. 9; 7 of 1979 s. 4; 12 of 2004 s. 16) 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. (Amended 35 of 1965 s. 35)'*

162. In respect of a salaries or profits tax assessment which a taxpayer has objected to, the Commissioner has determined the objection, the taxpayer has appealed to the Board and the Board has decided the appeal but the taxpayer has not appealed to the Court of First Instance, section 70[6], so far as relevant, provides as follows:

> *'Where ... the amount of the assessable income or profits ... has been determined on ... appeal, the assessment as ... determined on ... appeal ... shall be final and conclusive for all purposes of this Ordinance as regards the amount of such assessable income or profits ... (Amended 49 of 1956 s. 51; 35 of 1965 s. 35; 40 of 1972 s. 9; 7 of 1979 s. 4; 12 of 2004 s. 16)*
>
> *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. (Amended 35 of 1965 s. 35)'*

163. Section 80(2) provides that:

> *'(2) 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 a partnership;*
>
> *(b) makes an incorrect statement in connection with a claim for any deduction or allowance under this Ordinance;*

[6] See also section 69 on the finality of the Board' s decision.

(c) gives any incorrect information in relation to any matter or thing affecting his own liability to tax or the liability of any other person or of a partnership;

(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 be guilty of an offence: Penalty a fine at level 3[7] *and a further fine of treble the amount of tax which 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 which 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. (Replaced 43 of 1975 s. 6. Amended L.N. 411 of 1984; 43 of 1989 s. 27; L.N. 338 of 1995)'*

164. Section 82(1) provides that:

'(1) Any person who wilfully with intent to evade or to assist any other person to evade tax-

(a) omits from a return made under this Ordinance any sum which should be included; or (Amended 30 of 1950 Schedule)

(b) makes any false statement or entry in any return made under this Ordinance; or

(c) makes any false statement in connection with a claim for any deduction or allowance under this Ordinance; or

(d) signs any statement or return furnished under this Ordinance without reasonable grounds for believing the same to be true; or

(e) gives any false answer whether verbally or in writing to any question or request for information asked or made in accordance with the provisions of this Ordinance; or

[7] $10,000 under section 113B and Schedule 8 of Criminal Procedure Ordinance, Chapter 221.

(f) prepares or maintains or authorizes the preparation or maintenance of any false books of account or other records or falsifies or authorizes the falsification of any books of account or records; or

(g) makes use of any fraud, art, or contrivance, whatsoever or authorizes the use of any such fraud, art, or contrivance,

shall be guilty of an offence: Penalty on summary conviction a fine at level 3 and a further fine of treble the amount of tax which has been undercharged in consequence of the offence or which would have been undercharged if the offence has not been detected, and to imprisonment for 6 months, and on indictment a fine at level 5[8] *and a further fine of treble the amount of tax so undercharged or which would have been so undercharged and to imprisonment for 3 years. (Amended 49 of 1956 s. 63; 40 of 1972 s. 12; L.N. 411 of 1984; 50 of 1991 s. 4; L.N. 338 of 1995)'*

165. Section 82A(1) provides that:

'(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 a partnership; 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 to tax or the liability of any other person or of a partnership; 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-

[8] $50,000 under section 113B and Schedule 8 of Criminal Procedure Ordinance, Chapter 221.

(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. (Amended 43 of 1975 s. 8; 43 of 1989 s. 28)

(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) An assessment of additional tax may be made only by the Commissioner personally or a deputy commissioner personally. (Amended 48 of 1995 s. 12)

(4) Before making an assessment of additional tax the Commissioner or a deputy commissioner, as the case may be, shall- (Amended 48 of 1995 s. 12)

(a) cause notice to be given to the person he proposes so to assess which shall-

(i) inform such person of the alleged incorrect return, incorrect statement or incorrect information or alleged failure to comply with the requirements of the notice given to him under section 51(1) or (2A) or the alleged failure to comply with section 51(2) in respect of which the Commissioner or a deputy commissioner intends to assess additional tax under subsection (1); (Replaced 43 of 1975 s. 8. Amended 43 of 1989 s. 28; 48 of 1995 s. 12)

(ii) include a statement that such person has the right to submit written representations to him with regard to the proposed assessment on him of additional tax;

(iii) specify the date, which shall not be earlier than 21 days from the date of service of the notice, by which representations

which such person may wish to make under subparagraph (ii) must be received;

(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.

(4A) Notwithstanding subsection (4), if the Commissioner or a deputy commissioner is of the opinion that the person he proposes to assess to additional tax under subsection (1) is about to leave Hong Kong, he need not serve a notice under subsection (4)(a), but may assess that person to additional tax under subsection (1). (Added 43 of 1975 s. 8. Amended 7 of 1986 s. 12; 48 of 1995 s. 12)

(5) Notice of intention to assess additional tax and notice of an assessment to additional tax shall be given in the same manner as is provided in section 58(2) in respect of a notice of assessment under section 62.

(6) Where a person who is liable to be assessed to additional tax has died, an assessment to additional tax may be made on his executor, and the additional tax shall be recovered as a debt due from and payable out of the deceased person's estate.

(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). (Added 26 of 1969 s. 38)'

166. Section 82B provides that:

'(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 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). (Replaced 12 of 2004 s. 18)

(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). This subsection shall apply to an appeal relating to any assessment in respect of which notice of assessment is given on or after the commencement[9] of the Inland Revenue (Amendment) Ordinance 2004 (12 of 2004). (Added 12 of 2004 s. 18)

(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. (Added 26 of 1969 s. 38)'

CFA judgment in Koon Wing Yee case

167. Koon Wing Yee v Insider Dealing Tribunal [2008] 3 HKLRD 372 raised important and interesting questions concerning an inquiry by the Insider Dealing Tribunal[10] ('the Tribunal')

[9] 25 June 2004.

[10] Not the Market Misconduct Tribunal which Mr Mok repeatedly referred to in paragraphs 2 and 8 of the appellant's second written submission. In contrast with the Insider Dealing Tribunal, the Market Misconduct Tribunal has no power to impose a fine. This was influenced by legal advice received by the Government to the effect that the existence of such a power might lead to a breach of the BOR, see paragraph 48 of Koon Wing Yee.

conducted under the Securities (Insider Dealing) Ordinance, Chapter 395 ('SIDO') which has now been repealed and replaced by the Securities and Futures Ordinance, Chapter 571 ('SFO'). The principal questions were whether articles 10 and 11 of the BOR applied to the proceedings and, if so, whether the use by the Tribunal of incriminating answers compulsorily given to incriminating questions and the standard of proof applied by the Tribunal complied with these provisions.

168. The Court of Final Appeal held that:

(a) The decisions of the European Court of Human Rights ('the Strasbourg Court') on provisions of the Convention [and applied by English Courts in the interpretation and application of the Human Rights Act 1998 (UK)] which are in the same, or substantially the same terms, as the relevant provisions of the BOR, though not binding on the courts of Hong Kong, are of high persuasive authority and have been so regarded by the Court of Final Appeal, see paragraphs 26 & 27 of the judgment.

(b) The insider dealing proceedings involved the determination of a criminal charge by reason of the power to impose a penalty[11] under section 23(1)(c) of SIDO, see paragraph 66 of the judgment.

(c) As then advised, their lordships would not regard the argument that legislation, which provides for a dual regime of civil and criminal sanctions to deal with insider dealing, may infringe the BOR as soundly based, see paragraph 67 of the judgment.

(d) Section 6(1) of the BORO should be construed, in accordance with its terms, as conferring a power which will enable the courts to resolve the tension which exists between the legislative will and the protection given by the BOR by striking down only that part of the statute that causes the violation or breach, even if it does not itself infringe the BOR, when to do so best gives effect to the legislative intention, see paragraph 113 of the judgment.

(e) It is appropriate and just to hold that the power under section 23(1)(c) to impose a penalty is invalid on the ground that it has resulted in violations of articles 10 and 11 of the BOR, see paragraph 120 of the judgment.

Criminal charge

[11] An amount not exceeding three times the amount of any profit gained or loss avoided by any person as a result of the insider dealing.

169. In the respondent's written skeleton argument dated 22 May 2008, the respondent conceded, correctly in our view, that:

(a) applying the principles stated by the Court of Final Appeal in Koon Wing Yee, the central question was whether, in substance, proceedings under section 82A involve the imposition of a substantial penalty, see paragraphs 49 – 51 of the judgment;

(b) the imposition of a tax surcharge as a penalty on those who fail to make proper returns has been recognised by the Strasbourg Court as involving a criminal charge, see Janosevic at paragraph 65 – 71 and the judgment of the English Court of Appeal in Han which was cited with approval at paragraphs 31-32, 35 and 62 of the judgment;

(c) proceedings under section 82A do involve a criminal charge; and

(d) the respondent needs to justify the imposition by section 68(4) of the Ordinance of a reverse persuasive[12] burden which interferes with the presumption of innocence under Article 11(1) by placing on the taxpayer the persuasive burden of proving a central fact.

170. The penalty under section 82A is the same as the penalty under section 23(1)(c) of SIDO. Applying Koon Wing Yee, proceedings under section 82A do involve a criminal charge.

171. It must, however, be emphasised that the fact that additional tax proceedings involve a 'criminal charge' for human rights purposes does not necessarily mean that all the consequences of a criminal trial apply in relation to the substance of the matter, see Han at paragraphs 84, 88:

> *'It by no means follows from a conclusion that article 6 applies that civil penalty proceedings are, for other domestic purposes, to be regarded as criminal and, therefore, subject to those provision of the Police and Criminal Evidence Act 1984 ('PACE') and/or the Codes produced thereunder, which relate to the investigation of crime and the conduct of criminal proceedings as defined by English law. Any argument as to whether and how far PACE and the Codes apply is one which will have to be separately considered if and when it is advanced. In this context, however, the specific provisions of section 60(4) of VATA are plainly of considerable importance. I would merely add my view that, if matters are made clear to the taxpayer on the lines indicated in paragraph 77 above at the time when the nature and effect of the inducement procedure are also made clear to him (whether by VAT Notice 730 or otherwise), it is difficult to see that there would be any breach of article 6. It also seems to me that, even*

[12] The case of the respondent is that section 68(4) imposes a persuasive, and not evidential, burden.

> *if PACE were applicable, it is most unlikely that a court or tribunal would rule inadmissible under section 76 or section 78 any statements made or documents produced as a result, at any rate in the absence of exceptional circumstances. On the other hand, it follows from this decision that a person made subject to a civil penalty under section 60(1) will be entitled to the minimum rights specifically provided for in article 6(3)', per Potter LJ at paragraph 84.*
>
> *'The classification of a case as criminal for the purposes of article 6(3) of the Convention on Human Rights, using the tests established by the Strasbourg jurisprudence, is a classification for the purposes of the Convention only. It entitles the defendant to the safeguards provided expressly or by implication by that article. It does not make the case criminal for all domestic purposes. In particular, it does not, necessarily, engage protections such as those provided by the Police and Criminal Evidence Act 1984. The submissions before us did not address this point, or, indeed, the subject of burden of proof (although I note that no objection was even raised to a civil burden in Georgiou's case). As Mr Oliver and Potter LJ have both observed, the precise implications under the Convention of classification of any case as criminal for the purposes of the Convention will have to be worked out on a case-by-case basis' per Mance LJ at paragraph 88.*

Application of section 68(4) to section 82B appeals

172. Mr Mok contended that section 68(4) does not apply to additional tax appeals because of the words 'so far as they are applicable' in section 82B(3) but did not respond to the Chairman's question on the criteria for application.

173. We have no hesitation in rejecting his contention.

174. We do so for a number of reasons. The first is that we accept Mr Pannick's submission that the search is for any legitimate reason not to apply, rather than for any legitimate reason to apply. By way of example, there is a legitimate reason not to apply that part of section 68(3) which provides for representation of the respondent by the assessor who made the assessment appealed against. The reason for not applying is that additional tax assessments can only be made by the Commissioner or her deputy, but not by any assessor. In contrast, there is no reason, and Mr Mok has not put forward any, not to apply section 68(4).

175. Secondly, Mr Mok's contention is unconvincing in the absence of any criteria for application, if the search is for reason to apply.

176. Thirdly, sub-section (3) must be construed in the context of the Ordinance as a whole. It follows sub-section (2) which provides in effect that it shall be open to the taxpayer to argue on

appeal that the penalty assessment is incorrect because he is not liable and that the penalty assessment is excessive because it exceeds the statutory maximum or is excessive having regard to the circumstances. There is every reason to incorporate by reference section 68(4) on burden of proof on these issues, i.e. the issues of the incorrectness and excessiveness of the assessment appealed against.

177. The Revenue knows of no exception to the consistent approach by the Board in placing the burden of proof in additional tax appeals on the taxpayer. We know of no exception either. The following are examples of such approach.

(a) In the first of the appellant's written submissions, the appellant alleged in paragraph 26 that D17/72, an incorrect reference for the appeal in BR17/72 IRBRD 97, 'was actually abandoned by the taxpayer before the Board's ruling was given'. This is incorrect. The Board [Chan Ying-hung, Benjamin T M Liu, K H A Gordon & G H P Pritchard] gave its ruling in the following terms before leading counsel for the taxpayer opened his case (see page 99):

'We do not think it can be disputed that the nature of these proceedings is an appeal against an assessment - albeit a very special kind of assessment.

In our opinion the answer to the question raised before us is to be found in section 82B. There the legislature describes an appeal such as the present one as an appeal against an assessment. It goes on to incorporate by reference the provisions of section 68(4) of the Ordinance that the onus of proof that an assessment appealed against is excessive or incorrect shall be on the appellant. We do not think that the presence of the words "without reasonable excuse" in section 82A have the effect of throwing the onus upon the Revenue.

It is to be observed that section 82A gives the Revenue two mutually exclusive remedies. They can either launch a criminal prosecution or levy an additional tax by an assessment made by the Commissioner personally.

We are not concerned here with a prosecution. However, when the alternative course is adopted as is in this case, our view is that, for the removal of doubt, the legislature has extended the provisions of section 68(4) to an assessment of additional tax.

We rule that the onus of proof that the assessment made by the Commissioner is wrong lies on the appellant and he should begin.'

The taxpayer intended to adduce evidence to show that the original assessments which gave rise to the assessments for additional tax were excessive having regard to all the circumstances. The Commissioner objected immediately and submitted that by virtue of section 70 the assessable profits had been conclusively determined and that no evidence should be allowed which sought to prove that such profits were excessive or that the appellant's original returns were correct. The Board ruled in favour of the Commissioner for the following reasons (at page 100):

> *'In our view, the appellant's original tax returns must be taken to be incorrect. This is a finding implicit from the decision of the former Board and from the nature of the successive proceedings which we have described above. Any evidence or argument seeking to prove or establish the contrary must, of necessity, involve the proposition that the assessable profits determined and confirmed as aforesaid were wrong. That would be violating the provisions of section 70 if they apply to these proceedings, and we hold that they do.*
>
> *As to the words "so far as they are applicable" in section 82B(3), we can see nothing in the Ordinance or in the circumstances of this case which make it inappropriate for us to apply the provisions of section 70. It follows that in our opinion the assessments above referred to are final and conclusive for all purposes including any purpose under section 82A and section 82B.'*

(b) In D57/06, (2006) IRBRD, vol 21, 1061, the Board [Kenneth Kwok Hing Wai SC, Ip Tak Keung and Horace Wong Yuk Lun SC] held at paragraph 10 that:

> *'Section 68(4) of IRO provides that the "onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant". Section 82B(3) further provides that the provisions in, inter alia, section 68 "shall have effect with respect to appeals against additional tax as if such appeals were against assessments to tax other than additional tax". Accordingly, section 68(4) applies to the present appeal and the burden is upon the Appellant to prove that the Assessment is excessive or incorrect.'*

Persuasive burden

178. Mr Mok submitted that section 68(4) imposed an evidential burden because of the involvement of a criminal charge and the need to be BOR compliant. Mr Pannick submitted that section 68(4) imposed a persuasive burden.

179. The difference between the two burdens was explained by Sir Anthony Mason NPJ in HKSAR v Lam Kwong Wai (2006) 9 HKCFAR 574 at paragraphs 25 – 27:

'25. A reverse onus, which places an onus on the defendant to prove all or any of the elements of the offence, appears to be inconsistent with the presumption of innocence because it allows the defendant to be convicted on failing to discharge the reverse onus, even though the prosecution fails to prove all the elements of the offence beyond reasonable doubt. In the cases on reverse onus, a distinction has been drawn between the "legal" or "persuasive" burden of proof and what has been called the "evidential" burden. The distinction is important because an evidential burden (which is not, strictly speaking, a burden of proof) is generally regarded as consistent with the presumption of innocence (Tse Mui Chun v HKSAR (2003) 6 HKCFAR 601 at pp.618J-619D, per Bokhary PJ and Lord Scott of Foscote NPJ; R v Lambert [2002] 2 AC 545 at p.563G, per Lord Slynn of Hadley; p.572D per Lord Steyn and p.589B, per Lord Hope of Craighead; but cf Downey v The Queen (1992) 90 DLR (4th) 449). It will be necessary to return to this proposition later, as it is the subject of a submission by Mr Gerard McCoy SC for the appellant.

26. An evidential burden, unlike a persuasive burden, does not expose the defendant to the risk of conviction because he fails to prove some matter on which he bears an evidential onus. An evidential burden:

... requires only that the accused must adduce sufficient evidence to raise an issue before it has to be determined as one of the facts in the case. The prosecution does not need to lead any evidence about it, so the accused needs to do this if he wishes to put the point in issue. But if it is put in issue, the burden of proof remains with the prosecution. The accused need only raise a reasonable doubt about his guilt.

(R v DPP, ex p Kebilene & Others [2000] 2 AC 326 at pp.378H-379A, per Lord Hope of Craighead). See also R v Lambert [2002] 2 AC 545 at p.588H, where his Lordship said:

What the accused must do is put evidence before the court which, if believed, could be taken by a reasonable jury to support his defence.

27. A persuasive burden, on the other hand, requires a defendant to prove, on a balance of probabilities, an ultimate fact which is necessary to the determination of his guilt or innocence. The burden relates to an essential element of the offence. It reverses the burden of proof by transferring it from the prosecution to the defendant (R v DPP, ex p Kebilene & Others [2000] 2 AC 326 at p.378H, per Lord Hope of

> *Craighead). It may be either mandatory or discretionary in its operation. With a mandatory persuasive burden, it is possible for a conviction to be returned, even where the tribunal of fact entertains a doubt as to the defendant's guilt (Emmerson and Ashworth, Human Rights and Criminal Justice (2001) para.9-03).'*

180. Sir Anthony Mason NPJ went on to state at paragraph 29 the broad questions to be addressed:

> *'Our first task is to ascertain the meaning of s.20 according to accepted common law principles of interpretation as supplemented by any relevant statutory provisions. Our second task is to consider whether that interpretation derogates from the presumption of innocence and the right to a fair trial as protected by the Basic Law and the BOR. If that question is answered 'Yes', we have to consider whether the derogation can be justified and, if not, whether it could result in contravention of the Basic Law or the BOR and consequential invalidity. If invalidity could result, then it will be necessary to decide whether the validity of the section or part of it can be saved by the application of any rule of construction, severance of the offending part, reading down, reading in or any other remedial technique available to the Court. Consideration of this question will require examination of the powers of the courts as established by the Basic Law.'*

181. The BORO is a local statute. We do not understand Sir Anthony Mason's reference to 'any relevant statutory provisions' as including the provisions of the BORO. By way of example, the first task of interpretation of the impugned provisions was performed by the Court of Final Appeal[13] in HKSAR v Ng Po On FACC 6/2007 without reference to the BORO:

> *'48. Where a person prosecuted under section 14 seeks to contend that he has a reasonable excuse for failing to comply with the notice served on him, the combined effect of section 14(4) and section 24 ... is to impose on him the persuasive burden of establishing the existence of such reasonable excuse on the balance of probabilities. The wording of section 24 – "the burden of proving a defence of ... reasonable excuse shall lie upon the accused" – leaves no room for doubt that a persuasive burden is expressly imposed.'*

182. If, having performed the first two tasks referred to by Sir Anthony Mason NPJ, one concludes that the presumption of innocence is not engaged, that is an end to the discussion. But if it is engaged, the third task is to consider whether its abrogation is justified, it being recognized that the individual's right to the presumption is not absolute, per Ribeiro PJ in Ng Po On at paragraph

[13] Which also comprised Sir Anthony Mason NPJ

42. If the reverse onus provision fails the rationality or proportionality test so that it contravenes Article 87(2) of the Basic Law and Article 11(1) of the BOR, the court proceeds to its fourth task, which is to decide whether validity of the provision or part of it can be saved by the application of any remedial technique available to the Court.[14]

183. If the first task of interpretation is to be carried out in a way as submitted by Mr Mok so as to be BOR compliant, there is no need to perform the other tasks. Mr Mok's approach confuses the first task of interpretation with the second task of considering whether *that* interpretation derogates from the presumption of innocence and the right to a fair trial as protected by the Basic Law and the BOR. It also confuses the first task with the last task of considering the remedies. His approach skips the third task of considering whether abrogation is justified and would lead to a wrong conclusion in cases where abrogation is justified. His approach is plainly wrong.

184. In Ng Po On, the Court of Final Appeal adopted the correct approach and concluded at paragraph 78 that:

> *'(i) Section 24, read together with section 14(4), places a persuasive burden on the defence; (ii) this is inconsistent with the presumption of innocence protected by Article 87(2) of the Basic Law and Article 11(1) of the Bill of Rights; and (iii) the two sections, read in conjunction, do place a persuasive burden on the prosecution and an evidential burden on the defence after a remedial interpretation has been applied, giving them such effect.'*

185. In Ng Po On at paragraph 48[15], Ribeiro PJ held that the wording 'the burden of proving a defence of ... reasonable excuse shall lie upon the accused' – leaves no room for doubt that a persuasive burden is expressly imposed. Absence of 'reasonable excuse' is an element of the penalty tax. Section 68(4), read together with section 82B(3), places the burden on the taxpayer of proving that the penalty tax assessment is incorrect (which includes the element of 'reasonable excuse'). This leaves no room for doubt that a persuasive burden is expressly imposed.

186. If section 67 applies to additional tax appeals, the burden under section 67(5)(d) is a persuasive burden.

187. So far as we know, the Courts and the Board have interpreted the burden under section 68(4) as a burden on the taxpayer throughout.

188. In Mok Tsze Fung v Commissioner of Inland Revenue [1962] HKLR 258 at page 281, Mills Owens J said that:

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[14] Lam Kwong Wai paragraph 29.
[15] See paragraph 181 above.

> *'It was for the appellant to adduce evidence before the Board of Review in order to discharge the onus resting upon him, and on his failure to do so the Board was entitled, indeed bound, to reject his appeal (vide Pyrah v Amis).'*

189. In Commissioner of Inland Revenue v The Board of Review, ex parte Herald International Ltd [1964] HKLR 224, Blair Kerr J said that:

> *'According to section 68(3) the assessor attends the hearing before the Board "in support of the assessment", but the onus of proving that "the assessment as determined by the Commissioner .... is excessive" is placed fairly and squarely on the appellant by section 68(4).' (at page 229)*
>
> *'The question for the Board of Review is not whether the Commissioner erred in some way, but whether the assessment is excessive. As Mr. Sneath so aptly put it:*
>
> > *"The question is: ' Did the Commissioner get the correct answer' ; not ' did the Commissioner get the correct answer by the wrong method' . "*
>
> *And the onus of proving that the assessment is excessive lies on the taxpayer-appellant.' (at page 237)*

190. In All Best Wishes Limited v Commissioner of Inland Revenue (1992) 3 HKTC 750 at page 772, Mortimer J (as he then was) said that:

> *'It must be remembered that the burden of disturbing the assessment, rests upon the taxpayer.'*

191. The Commissioner does not have the burden of proving that a case had been made out for invoking the anti-avoidance provisions, section 61 or section 61A. The burden of proving that the assessment appealed against is excessive or incorrect shall be on the taxpayer: section 68(4) and the burden rests with the taxpayer, to prove that the Commissioner was wrong, see Cheung Wah Keung v Commissioner of Inland Revenue [2002] 1 HKLRD 172 at paragraph 29, Deputy Judge Poon, as he then was, held that:

> *'The last question of law stated[16] relates to the burden of proof. Mr Burkett relied on the Singaporean case of CEC v Comptroller of Income Tax (Singapore) (1950-1985) MSTC 551. There, the Taxpayer had made out a prima facie case showing, among other things, that everything was above board and genuine. In such circumstances, the court said that the onus of*

[16] 'Did the Board err in law in failing to impose on the Commissioner the burden of proving that a case had been made out for invoking s.61 and s.61A?', see paragraph 15(e) of DJ Poon' s judgment.

> *proving a sham was on the CEC v Comptroller of Income Tax (Singapore). However, at p.555 of the judgment, the court made it abundantly clear that the burden of proof throughout, until the end ofCEC v Comptroller of Income Tax (Singapore) rested on the taxpayer, to show that the tax is excessive. I do not find this case of particular assistance to the Taxpayer. The burden of proving that the additional salary assessments were excessive or incorrect, shall be on the Taxpayer: s.68(4). The burden rests with the Taxpayer, to prove that the Commissioner was wrong. Accordingly, I would also answer the last question with a "no".'*

The passage above taken from the Hong Kong Law Report and Digest does not read well. The following version is taken from the word document of the judgment as posted by the Judiciary on its Legal Reference System:

> *'The last question of law stated relates to the burden of proof. Mr Burkett relied on the Singaporean case of CEC v Comptroller of Income Tax (Singapore) (1950-1985) MSTC 551. There the Taxpayer had made out a prima facie case showing among other things that everything was above board and genuine. In such circumstances, the court said that the onus of proving a sham was on the Comptroller. However, at 555 of the judgment, the court made it abundantly clear that the burden of proof throughout until the end of the Comptroller's case rested on the taxpayer to show that the tax is excessive. I do not find this case of particular assistance to the Taxpayer. The burden of proving that the additional salary assessments were excessive or incorrect shall be on the Taxpayer: section 68(4). The burden rests with the Taxpayer to prove that the Commissioner was wrong. Accordingly, I would also answer the last question with a "no".'*

192. On appeal, Cheung Wah Keung v Commissioner of Inland Revenue [2002] 3 HKRLD 773, CA, Woo JA said the following of section 68(4):

> *'43. Nothing that Mr Thomson has shown to us persuades us that the determination or the Board' s decision was wrong. Mr Cooney points out that the method by which an assessment was made by the Revenue is quite irrelevant at the stage of proceedings before the Board, and that the crux is whether the assessment is correct. He refers us to CIR v Board of Review, ex p Herald International Ltd [1964] HKLR 224 as to how the Board should deal with an appeal against an assessment. Blair-Kerr J in the Full Court said at p.237:*

> *The question for the Board of Review is not whether the Commissioner erred in some way, but whether the assessment is excessive. As Mr Sneath so aptly put it:*
>
> > *The question is: "Did the Commissioner 'get the correct answer'; not 'did the Commissioner get the correct answer by the wrong method.'"*
>
> *And the onus of proving that the assessment is excessive lies on the taxpayer-appellant.'*

'52 *Secondly, s.68(4) of the Ordinance makes it crystal clear that "the onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant." Judicial utterances to the same effect can also be found in CIR v Board of Review, ex p Herald International Ltd [1964] HKLR 224 referred to in para.42 above and CEC v Comptroller of Income Tax (Singapore) (1950-1985) MJTC 551.'*

Derogation from the presumption of innocence

193. Sections 82B(3) and 68(4) read together impose on the taxpayer a reverse persuasive burden and derogate from the presumption of innocence under Article 87 of the Basic Law and Article 11(1) of BOR, given constitutional effect by Article 39 of the Basic Law.

Justification of the encroachment

194. The presumption is not absolute and derogation may be justified. The approach, as summarised by Ribeiro PJ in Ng Po On, is as follows:

'28 *Returning to the persuasive burden, it is established that the constitutional protection accorded to the presumption of innocence is not absolute and that derogation from it may be justified if such derogation has a rational connection with the pursuit of a legitimate aim and if it is no more than necessary for the achievement of that aim.*[17] *Where the legislature has chosen to impose a reverse onus on the defendant, the Court gives weight to that legislative decision, taking into account the nature of the problem addressed in the statute and in particular, whether it involves adoption of a policy which the legislature is better placed than the Court to assess, as discussed in Lam Kwong*

[17] Lam Kwong Wai at paragraph 21.

Wai.[18] *The Court must of course ultimately exercise its constitutional responsibility by determining the issue, after giving appropriate respect to the legislative judgment.'*

'43. In accordance with the principles laid down by this Court in Leung Kwok Hung v HKSAR,[19] *the dual test for justifying an encroachment on the presumption of innocence was stated in Lam Kwong Wai in the following terms:*

"(1) is the derogation rationally connected with the pursuit of a legitimate societal aim (the rationality test); and

(2) are the means employed, the imposition of the reverse persuasive onus, no more than is necessary to achieve that legitimate aim (the proportionality test)?"[20]

44. The burden is on the state to justify the derogation for reasons which must be compelling,[21] *although, as previously noted ... the Court will carry out its constitutional responsibilities with appropriate respect for the legislature's decision under challenge. As Lord Bingham of Cornhill noted in Sheldrake v DPP:*

"The justifiability of any infringement of the presumption of innocence cannot be resolved by any rule of thumb, but on examination of all the facts and circumstances of the particular provision as applied in the particular case."[22]*'*

The rationality test

195. The long title of the Ordinance is to 'impose a tax on property, earnings and profits'. The aim is to punish and deter failure to submit timely and correct tax returns and information to the Revenue. Having regard to Articles 64, 73, 106, 107 and 108 of the Basic Law, the legitimacy and importance of that societal objective is obvious. Imposing an administrative penalty with a reverse onus on appeal is a rational means of enforcing compliance with the duties to submit timely and correct tax returns and information to the Revenue.

The proportionality test

[18] Lam Kwong Wai at paragraph 45.
[19] (2005) 8 HKCFAR 229 at 253-254.
[20] Lam Kwong Wai at paragraph 17.
[21] Lam Kwong Wai at paragraph 44.
[22] [2005] 1 AC 264 at 297, paragraph 21.

196. The question here, as summarised by Ribeiro PJ at paragraphs 43 & 44 in Ng Po On is 'are the means employed, the imposition of the reverse persuasive onus, no more than is necessary to achieve that legitimate aim (the proportionality test)?' The burden is on the state to justify the derogation for reasons which must be compelling, although, as previously noted, the Court will carry out its constitutional responsibilities with appropriate respect for the legislature's decision under challenge.

197. In Janosevic, the Strasbourg Court held that:

> *'102 In assessing whether, in the present case, this principle of proportionality was observed, the Court acknowledges that the applicant was faced with a presumption that was difficult to rebut. However, he was not left without any means of defence. It is clear that, in challenging the Tax Authority's decisions on taxes and tax surcharges, the applicant has maintained that he submitted correct information in his tax returns and that the Authority's tax assessments were erroneous as they were based on inaccurate information gathered during the tax audit. In so doing, the applicant has relied in his defence in so far as the surcharges are concerned on Ch.5, s.11 of the Taxation Act (and similar provisions in other relevant laws), according to which a successful objection to the taxes themselves will automatically result in a corresponding reduction in the surcharges. However, it was open to the applicant to put forward grounds for a reduction or remission of the surcharges and to adduce supporting evidence. Thus, he could have claimed, as an alternative line of defence, that, even if he was found to have furnished incorrect information to the Tax Authority, it was excusable in the circumstances or that, in any event, the imposition of surcharges would be manifestly unreasonable. However, apart from his contention that the surcharges should be remitted due to the length of the proceedings, the applicant has not made any such claim and the Country Administrative Court—which was obliged to examine on its own motion whether there were grounds for remission—concluded, in its judgments of December 7, 2001, that no legal basis for remitting the tax surcharges had been found.*
>
> *103 The Court also has regard to the financial interests of the State in tax matters, taxes being the State's main source of income. A system of taxation principally based on information supplied by the taxpayer would not function properly without some form of sanction against the provision of incorrect or incomplete information, and the large number of tax returns that are processed annually coupled with the interest in ensuring a foreseeable and uniform application of such sanctions*

undoubtedly require that they be imposed according to standardised rules.

104 In view of what has been stated above, in particular the fact that the relevant rules on tax surcharges provide certain means of defence based on subjective elements and that an efficient system of taxation is important to the State's financial interests, the Court considers that the presumptions applied in Swedish law with regard to surcharges are confined within reasonable limits. Nevertheless, as the Supreme Administrative Court stated in a judgment delivered on December 15, 2000 ... this conclusion in general "requires that the courts…make a nuanced and not too restrictive assessment in each individual case as to whether there are grounds for setting aside or remitting the tax surcharge". As has been mentioned above, however, except for the reference to the length of the proceedings, the applicant did not rely on the grounds for remission in the relevant tax assessment proceedings.'

198. There the Strasbourg Court was faced with the question of proportionality of 'a presumption that was difficult to rebut' in respect of a tax surcharge. The relevant considerations succinctly articulated in these paragraphs apply with equal, if not greater force in Hong Kong.

199. In Strasbourg jurisprudence, tax matters still form part of the hard core of public authority prerogatives, with the public nature of the relationship between the taxpayer and the tax authority remaining predominant. In Ferrazzini v Italy [2001] STC 1314 at paragraph 29, the Strasbourg Court said:

'In the tax field, developments which might have occurred in democratic societies do not, however, affect the fundamental nature of the obligation on individuals or companies to pay tax. In comparison with the position when the convention was adopted, those developments have not entailed a further intervention by the state into the "civil" sphere of the individual's life. The court considers that tax matters still form part of the hard core of public authority prerogatives, with the public nature of the relationship between the taxpayer and the tax authority remaining predominant. Bearing in mind that the convention and its protocols must be interpreted as a whole, the court also observes that art 1 of Protocol 1, which concerns the protection of property, reserves the right of states to enact such laws as they deem necessary for the purpose of securing the payment of taxes (see, mutatis mutandis, Gasus Dosier-und Fordertechnik GmbH v Netherlands (1995) 20 EHRR 403 at 434, para 60). Although the court does not attach decisive importance to that factor, it does take it into account. It considers that tax disputes fall outside the scope

of civil rights and obligations, despite the pecuniary effects which they necessarily produce for the taxpayer.'

200. The BOR does not apply to the determination of civil rights and obligations. However, by virtue of Articles 64 and 73 of the Basic Law, approval of taxation and public expenditure are matters within the prerogative of the Legislative Council. By Article 108 of the Basic Law, the enactment of laws concerning types of taxes, tax rates, tax reductions, allowances and exemptions, and other matters of taxation are matters for the Legislative Council. The legislature has chosen to impose a reverse onus on the taxpayer and weight must be given to that legislative decision, taking into account the nature of the problem addressed in the statute and in particular, whether it involves adoption of a policy which the legislature is better placed than the Court to assess, as discussed in Lam Kwong Wai.

201. The Hong Kong Special Administrative Region ('HKSAR') enjoys financial autonomy under Article 106 but is constrained by Articles 107 and 108 to:

(a) take the low tax policy previously pursued in Hong Kong as reference in enacting laws on its own on matters of taxation;

(b) keep expenditure within the limits of revenue in drawing up its budget;

(c) strive to achieve a fiscal balance;

(d) avoid deficits; and

(e) keep the budget commensurate with the growth rate of its gross domestic product.

202. To put the low tax policy in perspective:

(a) the standard rate[23] ranges from a minimum of 10% for the years of assessment 1947/48 – 1949/50 to a maximum of 17% for the years of assessment 1984/85 – 1986/87; and

(b) the corporate profits tax rate[24] ranges from a minimum of 16% for the years of assessment 1998/99 – 2002/03 to a maximum of 17.5% for the years of assessment 1992/93 to 1993/94 and 2003/04 – 2006/07.

203. Direct taxation on earnings and profits brought in 40% - 55% of government's general revenue. As stated by the Financial Secretary in his speech on 18 June 1977, our fiscal

[23] See Schedule 1 to the Ordinance.
[24] See section 90 and Schedule 8 to the Ordinance.

system is also narrowly based. Introducing new taxes, whether direct or indirect, is easier said than done. In enacting new type of taxes under Article 108, HKSAR must still take the low tax policy previously pursued in Hong Kong as reference. When times are bad, it is unpopular to try to bring in new taxes. When times are good, some will argue that there is no need to do so.

204. While the tax rate is low and the fiscal system narrowly based, the demands on general revenue are ever increasing.

205. Omission or understatement of receipts in tax returns, if accepted by the Revenue causes loss in revenue. Failure to notify chargebility, if undetected by the Revenue, causes loss in revenue. Delay in submitting returns may delay the timely collection of revenue.

206. With a total of 2.98 million to 3.63 million assessments being made by the Revenue each year, a high degree of compliance by the taxpayers in submitting timely and correct tax returns and information to the Revenue is crucial for the effective operation of HKSAR's tax system.

207. The revelations by the Financial Secretary on 2 April 1975 showed that non-compliance was somewhat frightening. If the Board's experience is anything to go by, there is still a lot more to be done to improve compliance.

208. Defaults, if not deterred and punished, put our fiscal system at risk. It is also unfair to the honest taxpayers.

209. With limited income and ever increasing demands on expenditure, there is a limit to which the Revenue and the Department of Justice could and should deploy resources to check the accuracy of returns, conduct field audits and prosecute suspected offenders. These may be time and cost intensive. Even in cases where the Revenue has decided to conduct an investigation into a taxpayer's tax affairs, the Revenue may not know where to look. Once having been caught out, the taxpayer often sits back and leaves it to the Revenue to find out and build up its case. This is a laborious, painstaking and costly task. As we shall see, despite the reverse burden the appellant's attitude is one of 'catch us if you can'[25].

210. Some form of sanction against the provision of incorrect or incomplete information is necessary. A 100% sanction proved to be unsatisfactory and the legislature increased it to 300%.

211. There is no contention that the burden of proving that the penalty tax assessment is incorrect is difficult to rebut. Even if it is, the relevant rules of penalty tax provide certain means of defence based on subjective elements (for example, under the element of 'reasonable excuse') and it is open to the taxpayer to put forward grounds for a reduction under the excessiveness element. An efficient system of taxation is important, if not crucial, to HKSAR's financial interests. We

[25] See paragraph 336(h) below.

consider that the presumption under sections 68(4) and 82B(3) is confined within reasonable limits. The appellant's right to be presumed innocent has not been violated in the present case.

212. As the third task is decided against the appellant, there is no need to proceed to the last task.

Section 70

213. The appellant argued that the respondent is not entitled to rely on section 70.

214. Our only concern is whether section 70 applies to an appeal against a penalty tax assessment. Whether section 70 applies to prosecution under section 80(2) does not arise on the facts of this case. There is nothing inherently wrong with having dual regime of civil and criminal sanctions to deal with incorrect or incomplete tax reporting, see paragraph 168(c) above.

215. The combined effect of sections 68(4) and 82B(3) is to impose on the taxpayer the burden of proving that the penalty tax assessment is incorrect. Neither section deals in terms with the correctness of the underlying profits (or salaries or property) tax assessment.

216. Section 70 is the provision dealing with the correctness and quantum of the underlying profits (or salaries or property) tax assessment.

217. In an appeal against a penalty tax assessment, the question of the burden of proof on the correctness or quantum of the underlying profits (or salaries or property) tax assessment is academic if that assessment has become final and conclusive under section 70. So far as we know, the practice of the Commissioner is to commence penalty tax proceedings only after the underlying profits (or salaries or property) tax assessment has become final and conclusive under section 70.

218. It is in any event academic on the facts of this case because of the appellant's agreement on the amount of profits understated and tax undercharged, see paragraph 129 above.

219. Section 70 binds the taxpayer. Subject to the proviso, it also binds the Revenue.

220. Section 70 is governed by Article 108 of the Basic Law on the legislature's enactment of laws 'concerning types of taxes, tax rates, tax reductions, allowances and exemptions, and other matters of taxation'. The necessity and rationality of enacting a provision governing the finality of a profits, salaries or property tax assessment is obvious - so that the HKSAR may budget and use its financial revenues without fear that profits (or salaries or property) tax assessments may be re-opened years down the line. We do not think the right of the HKSAR to tax and to provide finality on a tax assessment has to strike a fair balance between proportionality between the means employed and the aims pursued, see Weson Investment Ltd v Commissioner of Inland Revenue [2007] 2 HKLRD 568:

> *'**Even if it were right** to construe the power to tax given under art.108 as being subject to an overriding requirement of proportionality stemming from art.105, and I do not for one moment consider that is correct, the question of proportionality has to be considered in the context of the case as well as the provisions of the Ordinance. In the context of this case, the fact is that the plaintiff was given an opportunity to purchase a TRC which would have entitled it to interest. Hence the argument that the Commissioner is entitled to interest on unpaid tax whereas the individual is not entitled to interest on tax subsequently refunded falls away. The fact that the amount of interest may be different is of no relevance. The sums involved are on the one hand the payment of a form of penalty and on the other putative interest',* per Rogers VP at paragraph 26, emphasis added.
>
> *'Mr Mok submitted that BL 105 and 108 should be read in the same way. In other words, the court must strike a fair balance, so that there must be a reasonable relationship of proportionality between the means employed and the aims pursued. He submitted that if one were to apply the proportionality test, s.79(1) whether read alone or considered together with s.71, failed the test. I do not believe it is right to read BL 105 and 108, as if the right of the HKSARG to tax has to strike such a fair balance. Rather, I am of the view that unless the taxation scheme cannot be regarded as genuine, but was in fact a disguised expropriation of property, BL 105 has no application. And the court has no power to interfere. Mr Mok accepted that, on his submission, even if the Ordinance had provided for the payment of interest, that would not be a sufficient compliance with BL 105, unless the interest so provided corresponded to "the real value of the property concerned at the time". I do not believe BL 105 could have such wide ranging effect',* per Tang VP at paragraph 85.

221. Further, if justification on the grounds of rationality and proportionality is required, then for reasons given above, including the reasons above on section 68(4), we consider that they are justified.

222. Further still, our view on the question whether a taxpayer has a right to re-open is in line with Hong Kong and English authorities.

223. We are bound by authority to hold that section 70 applies to an appeal against a penalty tax assessment. D5/07, (2007-08) IRBRD, vol 22, 245 was an appeal against penalty tax assessments. The Board [Kenneth Kwok Hing Wai SC, Malcolm Merry and Kenny Suen Wai Cheung] held that unappealed original salaries tax assessments were final and conclusive for all purposes of the Ordinance as regards the amounts of such assessable income by virtue of section 70 (see paragraphs 8 and 44 of that decision) and the amounts of the assessable income assessed

by the additional salaries tax assessments, as determined on objection, in respect of which there was no valid appeal were final and conclusive for all purposes of the Ordinance as regards the amounts of such assessable income by virtue of section 70 (see paragraphs 15, 17, 18 and 45 of that decision). The taxpayer appealed by way of case stated and the questions were 'whether having regard to all the facts as found by the Board and on the true construction of the Ordinance, the Board erred in law in [so] holding'? By a judgment handed down on 13 June 2008, Burrell J answered the questions in the negative, see Chu Ru Ying v Commissioner of Inland Revenue, HCIA 7/2007.

224. In Khan v Customs and Excise Commissioners [2006] STC 1167, the English Court of Appeal rejected at paragraph 74 the suggestion that human rights conferred on the taxpayer during the tax penalty phase a right to re-open findings made in relation to the earlier stage of the assessment, when no appeal had been brought against the assessment:

> *'This view is reinforced by a number of considerations: (i) it is the appellant who knows, or ought to know, the true facts; (ii) s 60(7) makes express provision placing the burden on Customs in relation to specified matters. This suggests that the draftsman saw it as an exception to the ordinary rule, and seems inconsistent with an implied burden on Customs in respect of other matters; (iii) the distinction is also readily defensible as a matter of principle. Mr Young relied on "the presumption of innocence" under art 6 of the Convention, but he was unable to refer us to any directly relevant authority. The presumption clearly justifies placing the burden of proof on Customs in respect of tax evasion and dishonesty; but once that burden has been satisfied, a different approach may properly be applied (compare R v Benjafield [2002] UKHL 2, R v Rezvi [2002] UKHL 1 (on appeal from R v Benjafield, R v Leal, R v Rezvi, R v Milford) [2003] 1 AC 1099, [2002] 1 All ER 815, in relation to confiscation orders in criminal proceedings); (iv) in relation to the calculation of tax due the subject-matter of the assessment and penalty appeals is identical. This link is given specific recognition by s 76(5) (allowing combination in one assessment). It would be surprising if the Act required different rules to be applied in each case; (v) s 73(9) provides that the assessed amount, subject to any appeal, is "deemed to be an amount of VAT due ...". In a case where either there was no appeal against the assessment, or the penalty proceedings followed the conclusion of any such appeal, this provision would appear to preclude any attempt to reopen the assessment for the purpose of assessing the penalty. The subsection does not apply directly where, as here, the penalty appeal is combined with an appeal against the assessment, and the assessment has not therefore become final, but it indicates another link between the two procedures. (I do not see the provision as necessarily confined to enforcement, as Mr Young argues. Nor in the present context do I need to spend time on his argument that this interpretation could cause unfairness in proceedings against*

a third party under s 61, although I note that under that provision there appears to be a general power to mitigate the penalty.); (vi) to reverse the burden of proof would make the penalty regime unworkable in many cases. In a case such as the present, a "best of judgment" assessment is needed precisely because the potential taxpayer has failed to keep proper records, so that positive proof in the sense required in the ordinary civil courts is not possible. The assessment may be no more than an exercise in informed guesswork. Indeed to put the burden on Customs would tend to favour those who have kept no records at all, as against those who have kept records, which are merely inadequate, but may be enough to give rise to an inference on the balance of probabilities.'

225. For reasons given above, the question whether section 70 applies is academic. If it is not, section 70 applies and it is not open to the appellant to re-open the issues.

Public hearing

226. Mr Mok made passing references to the hearings by the Board in camera under section 68(5) of the Ordinance.

227. This point can be disposed of quickly by adopting Mr Pannick's submission which we accept.

228. The appellant has at no time requested a public hearing and has waived any right to a public hearing, see Hakansson v Sweden (1990) 13 EHRR 1 at paragraphs 64 – 68:

'64. The Göta Court of Appeal was the first and only tribunal to deal with all aspects of the applicants' complaint against the compulsory auction in 1985. The applicants were accordingly entitled to a public hearing before that court, as none of the exceptions laid down in the second sentence of Article 6(1) applied.

65. The Government submitted that the requirements of Article 6(1) on the point at issue had been satisfied, in particular as the applicants had not requested any public hearing, thereby waiving any right thereto.

66. The public character of court hearings constitutes a fundamental principle enshrined in paragraph (1) of Article 6. Admittedly neither the letter nor the spirit of this provision prevents a person from waiving of his own free will, either expressly or tacitly, the entitlement to have his case heard in public. However, a waiver must be made in an unequivocal manner and must not run counter to any important public interest.

> *67. No express waiver was made in the present case. The question is whether there was a tacit one. While in some earlier cases dealt with by the Court the confidentiality of the proceedings at issue stemmed from legislation or practice, in the present case the Swedish law expressly provided for the possibility of holding public hearings: the Code of Judicial Procedure gave the Göta Court of Appeal power to hold public hearings "where [this was] necessary for the purposes of the investigation."*
>
> *Since the applicants' appeal mainly challenged the lawfulness of the 1985 auction and since in Sweden such proceedings usually take place without a public hearing, the applicants could have been expected to ask for such a hearing if they had found it important that one be held. However, they did not do so. They must thereby be considered to have unequivocally waived their right to public hearing before the Göta Court of Appeal. Their misgivings as to their treatment before that court only seem to have emerged in the course of the proceedings before the Convention organs; in their application to the Supreme Court for leave to appeal, no complaint was raised in this respect. Furthermore, it does not appear that the litigation involved any questions of public interest which could have made a public hearing necessary.*
>
> *68. There has accordingly been no violation of the public-hearing requirement in Article 6(1).'*

Had the appellant ever requested one, applying Koon Wing Yee at paragraph 113, the appropriate and just remedy would, at most, be a finding that the appellant should have been entitled to a public hearing had it requested one.

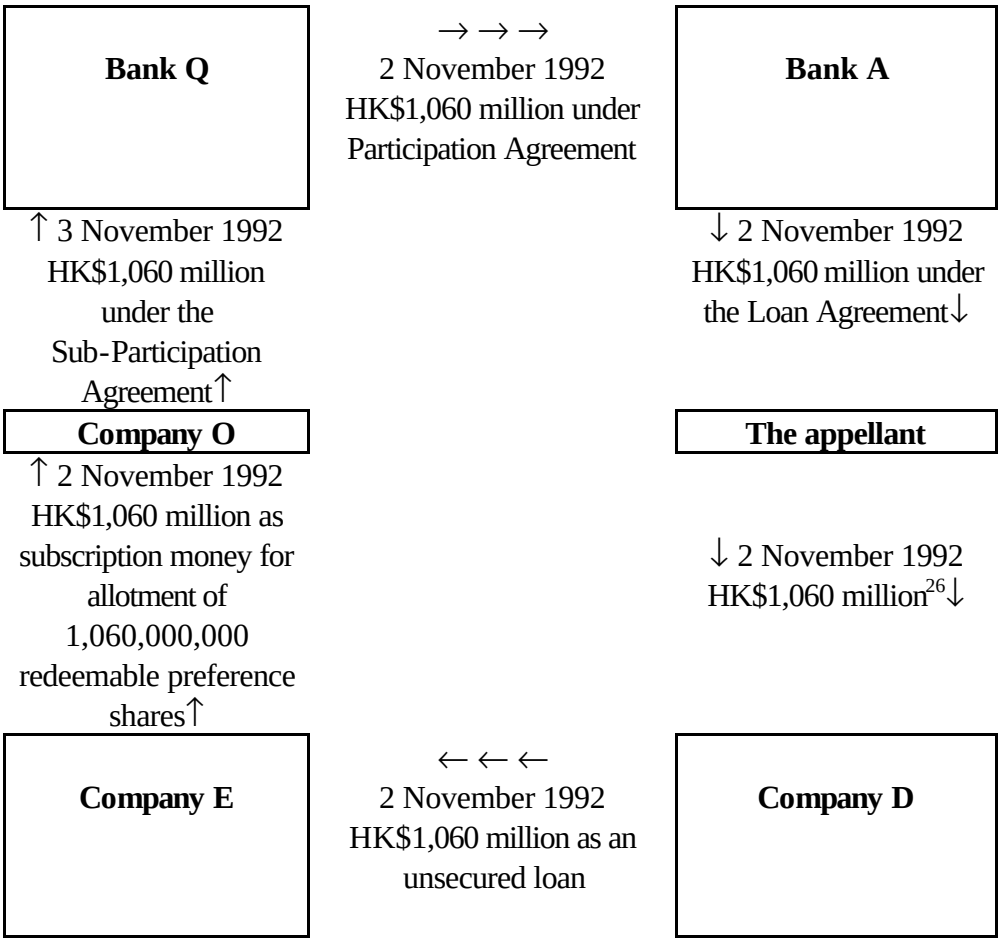
Conclusion

229. For reasons given above, Koon Wing Yee does not assist the appellant in this appeal.

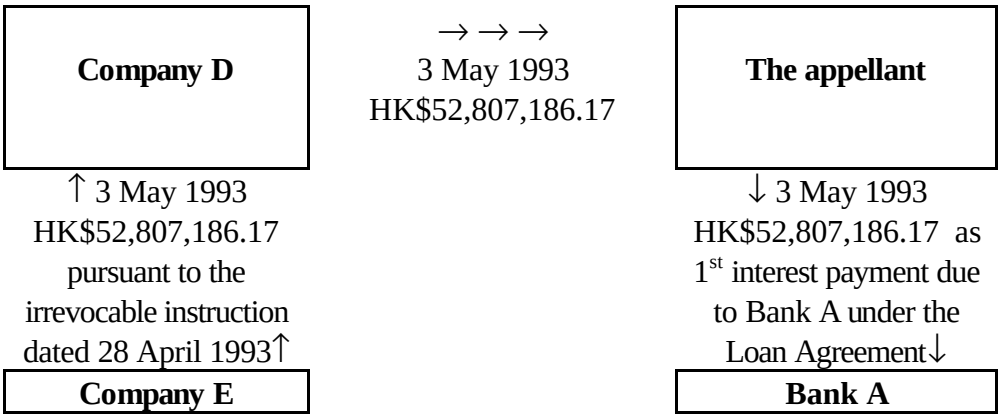
BOARD' S DECISION ON ORIGINAL GROUNDS OF APPEAL

Movement of funds

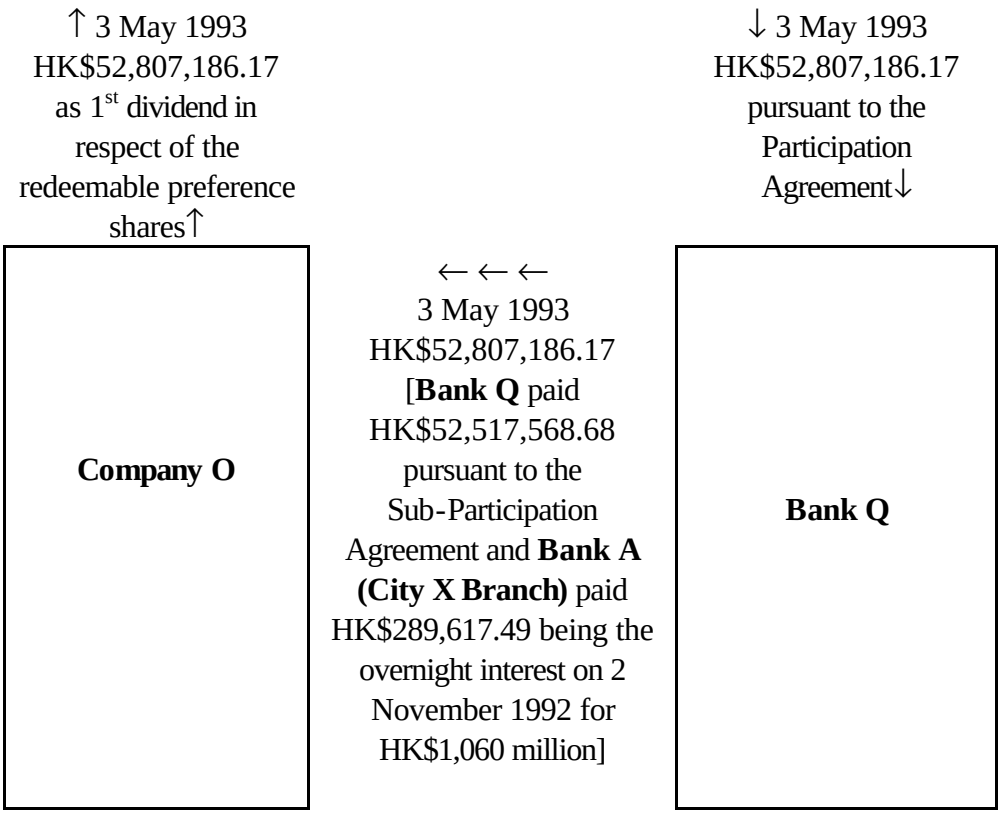
230. The following diagram illustrates the movement of funds referred to in paragraphs 44 – 49 above on the appellant' s drawdown of the HK$1,060 million loan by Bank A:



231. The following diagram illustrates the movement of funds on payment of interest by the appellant to Bank A referred to in paragraphs 50 – 52 above:



[26] The appellant borrowed $1,060 million from Company D on 21 September 1992 for acquisition of the Property.



Points which are *decided by the Decision*

232. The figures determined by the Board by the Decision are final for those years of assessment. In the course of ascertaining those figures, it was necessary for the Board to, and the Board did, decide and find, among others, the following (the paragraph numbers in the following sub-paragraphs are the paragraph numbers in the Decision):

1. On 19 November 1991, Accounting Firm AA introduced to Mr H a written 'tax planning memorandum' which eventually was acted on in November 1992 [paragraph 40 (1)].

2. The lending by Bank A can never be described as a true arm' s length advance of funds. In short, there was never any real exposure to Bank A and that they were participating in a circle of fund flow and in the end of the day, Bank A only obtained management fees [paragraph 40 (12)].

3. The tax scheme was put up for the appellant by Mr H (as director of the appellant) and Mr I [paragraph 42].

4. There was never any true lending or loan arrangements between Bank A and the appellant. There was a circle of fund flow on 2 and 3 November 1992 [paragraph 43].

5. As a consequence of delaying the payment of HK$1,060 million by Company O to Bank Q under the Sub-Participation Agreement by 1 day was that in the books of Bank Q, there was an outstanding loan of a very substantial amount (HK$1,060 million) overnight. In order to ensure that Bank Q would not be subject to any commercial risk of default, it was arranged that Company O, when it received the fund of HK$1,060 million, which originated from Bank Q and had passed through the accounts of Bank A, the appellant, Company D and Company E, on 2 November 1992, would place the funds on deposit with the City X branch of Bank A for one night, and the deposit would be uplifted on 3 November 1992 and transferred back to Company O's Bank Q account and then paid to Bank Q under the Sub-Participation Agreement. That circular movement of funds took place on 2 and 3 November 1992 [paragraph 44].

6. There was no evidence adduced to illustrate or support the appellant's submission that the main commercial purpose was to achieve a group reorganisation and to segregate property holding activity from the other business operations. The Board rejected such a contention [paragraph 45].

7. The loan was constructed to be repaid soonest upon issuance. The appellant could not be said to be indebted and Bank A could not be said to be beneficially entitled to the proceeds of the loan. That was the commercial reality of the loan transaction [paragraph 60].

8. There was never any loan between the appellant and Bank A in commercial reality. The accounting and book entries were structured in such a way that at least on the face of the records, Bank A was fully repaid by Bank Q even before it paid anything out to the appellant [paragraph 61].

9. The money borrowed by the appellant from Bank A and the interest paid by the appellant to Bank A under the loan agreement was not for the purpose of producing any profits. It was paid for exactly the opposite purpose, namely to reduce the profits of the appellant. The interest and related expenses paid or incurred by the appellant pursuant to the Loan Agreement cannot be deducted as outgoings or expenses for the purpose of ascertaining the appellant's chargeable profits [paragraph 62].

10. Each repayment of interest by the appellant was effectively secured by an instrument or undertaking (in the form of a payment instruction) executed or given in advance by Company E (an associate of the appellant) to Bank Q to pay the deposit (derived from dividends received from Company O) in its bank account to Company D/ Company B. Any sums payable by way of interest on such deposit by Company E with Bank Q (an offshore bank) would not be chargeable to tax under the Ordinance. Condition (d) in section 16(2) cannot be satisfied and the interest paid by the appellant to Bank A under the Loan Agreement is not deductible for the purpose of ascertaining the appellant's chargeable profit [paragraphs 65 and 66].

11. The 'transaction' for the purpose of section 61A of the Ordinance, can be considered in its widest form, i.e. the whole financing scheme including the temporary loan that originated from [Company D] to the appellant followed by the financial proposal as described in the Accounting Firm AA/Bank A documents involving the Loan Agreement, the Participation Agreement, the Sub-Participation Agreement, the issue of redeemable preference shares by Company O and the circular movement of funds on the drawdown date and on the subsequent interest dividend payment dates [paragraph 68].

12. The appellant in fact did enter into the financing scheme for the sole or dominant purpose of avoiding its liability to pay profits tax on the rental income or reducing the amount of tax payable on such rental income [paragraph 70].

13. The 'sole or dominant purpose' of the transaction was to obtain a 'tax benefit' for the appellant [paragraph 81].

14. The Commissioner was fully justified under section 61A in disallowing deduction of the interest and related bank charges and legal fees from the rental income [paragraph 83].

15. The transaction has no commercial reality and was indeed 'artificial' and the Commissioner was entitled under section 61 to disregard the Loan Agreement and any interest and related bank charges and legal fees 'paid' by the appellant to Bank A pursuant to that agreement and assess the appellant's liability to pay profits tax accordingly [paragraph 86].

INCORRECT RETURN – FIRST GROUND OF APPEAL

233. Mr Sieker told us that that he was bound by the Board's findings of fact in the Decision and that they were 'obliged by the virtue of the board decision and [their] review of the case law to accept that an incorrect return was made'.

234. However, he went on to argue that:

(a) page 1 of the profits tax return informed the taxpayer that he/she was required to prepare the return by virtue of section 51(1);

(b) in accordance with section 51(1), a taxpayer was 'required to file the return in accordance with the provision of Part IV of the IRO';

(c) section 16 falls under Part IV while sections 61 and 61A fell under Part X; and

(d) it was commonly believed that an assessment raised under sections 61 and/or 61A of the IRO could not in itself justify the conclusion that the taxpayer had made an incorrect return.

235. With respect, his contention is clearly unarguable and we reject it. We do so for a number of reasons.

236. The first reason is that the contention does not even get off the ground because, by the Decision, the Board decided against the appellant on the section 16 point (see paragraph 232(10) above). Section 16 was and is in Part IV. The Decision is final and conclusive under section 69.

237. The second reason is that whether a return is incorrect is a question of fact, not a question of belief or opinion. Common belief, even if established, is irrelevant.

238. We turn now to the third reason and consider what a taxpayer was and is required by section 51(1) to do.

239. What the 1993 version of section 51(1) required the appellant to do was to furnish the returns specified by the Board of Inland Revenue for profits tax. The specified forms required the appellant to state 'The Assessable Profits'.

240. The appellant reported the following assessable profits or adjusted loss in its tax returns (see paragraph 71 above):

Year of assessment	Assessable profits/(adjusted loss)
	$
1994/95	544,263
1995/96	(18,067,502)
1996/97	(17,908,782)
1997/98	(25,562,646)
1998/99	(52,683,453)

1999/2000	(68,483,142)
2000/01	(67,992,935)

241. By the Decision, the Board upheld the Commissioner's determination (see paragraphs 77 and 80 above):

Year of assessment	Assessable profits	Tax payable
	$	$
1994/95	106,683,672	17,602,805
1995/96	88,032,498	14,525,362
1996/97	88,191,218	14,551,550
1997/98	86,889,467	12,903,085
1998/99	85,310,519	13,649,683
1999/2000	69,475,699	11,116,111
2000/01	72,064,262	11,530,281
Total	596,647,335	95,878,877

242. As the appeal by way of case stated has been abandoned, the Decision has become final by virtue of section 69(1).

243. The assessments as determined on appeal are final and conclusive for all purposes of the Ordinance as regards the amount of such assessable profits by virtue of section 70.

244. Further and in any event, it is an agreed fact that (see paragraph 81 above):

'The amount of profits understated and tax undercharged are tabulated as follows:

Year of assessment	Total assessable profits	Assessable profits already reported	Profits understated	Percentage of profits understated to total assessable profits
	$	$	$	
1994/95	106,683,672	544,263	106,139,409	99%
1995/96	88,032,498	Nil	88,032,498	100%
1996/97	88,191,218	Nil	88,191,218	100%
1997/98	86,889,467	Nil	86,889,467	100%
1998/99	85,310,519	Nil	85,310,519	100%
1999/2000	69,475,699	Nil	69,475,699	100%
2000/01	72,064,262	Nil	72,064,262	100%
Total	596,647,335	544,263	596,103,072	

Year of	Total tax payable	Tax already	Tax	Percentage of tax undercharged to total

assessment		charged	undercharged	tax payable
	$	$	$	
1994/95	17,602,805	Nil	17,602,805	100%
1995/96	14,525,362	Nil	14,525,362	100%
1996/97	14,551,550	Nil	14,551,550	100%
1997/98	12,903,085	Nil	12,903,085	100%
1998/99	13,649,683	Nil	13,649,683	100%
1999/2000	11,116,111	Nil	11,116,111	100%
2000/01	11,530,281	Nil	11,530,281	100%
Total	95,878,877	Nil	95,878,877'	

245. For the reasons given above, including in particular the appellant's agreement of the fact stated in paragraph 81 above, the appellant had clearly not reported the correct amounts of assessable profits.

246. The returns filed by the appellant were incorrect.

247. The fourth reason why the argument is untenable is that section 51(1) did not and does not provide that for the filing of a profits tax return by a taxpayer 'in accordance with the provision of Part IV'.

248. The phrase 'in accordance with' did not and does not appear in 1993 version or the current version of section 51(1). What section 51(1) required and requires a taxpayer to do was and is to furnish a return as specified by the Board of Inland Revenue. The reference to Part IV etc. related and relates to the three taxes[27], not the return. Property tax was and is under Part II and liability for provisional property tax under Part XC. Salaries tax was and is under Part III and liability for provisional salaries tax under Part XA. Profits tax was and is under Part IV and liability for provisional profits tax under Part XB.

249. Our rejection of the contention is in line with authorities.

250. Newton v Commissioner of Taxation [1958] AC 450 was an appeal to the Privy Council from Australia. Section 260 of the Commonwealth of Australia Income Tax and Social Services Contribution Assessment Act, 1936-1951 provided that:

> *'Every contract, agreement, or arrangement ... entered into, orally or in writing, ... shall so far as it has or purports to have the purpose or effect of ... (c) ... avoiding any ... liability imposed on any person by this Act ... be absolutely void as against the commissioner ...'*

[27] Property tax, salary tax and profits tax.

251. The arrangement in that case was held to be caught by the section and the commissioner imposed a £600,000 penalty under section 226(2) of the Act. The advice of the Privy Council was delivered by Lord Denning who rejected the argument that there was no omission of income[28]:

> *'The commissioner assessed the shareholders in the tax due on the moneys received by them – and in addition included a sum as a penalty under section 226 (2) of the Act. This penalty amounts to over £600,000. Sir Garfield sought to say that section 226 (2) did not apply because the taxpayer could not properly be said to have 'omitted' the income from his return – seeing that it was not income when he received it or when he made his return – but only has become so ex post facto when the commissioner decided to treat it so. Their Lordships were not disposed to allow Sir Garfield to raise this point as it had not been raised before and does not appear in the case of the appellants – but in any case they think it is a bad point. In the events that have happened, the money has been determined to be assessable income. As such it ought to have been included – and was not. The taxpayer is therefore liable to the penalty.'*

Newton was decided and reported before section 61A was enacted in 1986. The 'common belief' which Mr Sieker relied on is at odds with Newton.

252. In D40/88, IRBRD, vol 3, 377, revised additional or revised original profits tax assessments were issued on 5 November 1986 based on the second revised assets betterment statement agreed by the taxpayer, Mr A. On appeal against additional tax assessments, solicitor for Mr A contended that the taxpayer's business could not have produced the profits that were agreed to in the revised assets betterment statement. The Board [Denis Chang QC, Chan Pang Fee and Duncan A Graham] ruled at pages 383 – 384 that the contention was not open to the taxpayer:

> *'Under section 70 of the Ordinance, the relevant assessments made on 5 November 1986 became final and conclusive "for all purposes of this Ordinance as regards the amount of such assessable income or profits or net assessable value."*
>
> *In our view, "all purposes of the Ordinance" includes determining the issue as to whether the relevant returns were or were not "incorrect" within the meaning of section 82A thereof.*
>
> *The consequence is that the assessable profits for the relevant periods are conclusively deemed to be the amounts assessed. The relevant returns made by Mr A and Mrs A are therefore for present purposes conclusively presumed to be*

[28] At p. 469.

> *incorrect in that the amounts of assessable profits returned were far below the amounts thus assessed. That is, the assessable profits had been understated. There is no basis in the light of the agreed statement of facts for any suggestion that, if the assessable profits were incorrectly returned, it was not because of any omission or understatement of anything in respect of which the Taxpayer was required by the Ordinance to make a return.*
>
> *By reason of the statutory provisions and in the light of the matters stated in the agreed statement of facts, we ruled that the Taxpayers could not contend that the amount of assessable profits had not been understated or that the same had been correctly returned.'*

253. The first ground of appeal fails.

REASONABLE EXCUSE – SECOND GROUND OF APPEAL

254. The appellant contended that it had reasonable excuse for omitting or understating its income.

'Reasonable person' approach vs 'reasonable excuse' approach

255. Mr Sieker cited the following passage from D13/85, IRBRD, vol 2, 173 at page 176 [William Turbull, E J V Hutt and Lee Wing Kit] and argued that in ascertaining what is a 'reasonable excuse', one looks to see what a reasonable person would do in all of the circumstances:

> *'The question which we now have to decide is whether or not the Taxpayer had a reasonable excuse for the second mistake which he made and which is the subject matter of this appeal. As we have stated we consider that the correct test to be applied in ascertaining "reasonable excuse" is what one would expect a reasonable person to do in all of the circumstances. A reasonable person is not a perfect person, but an average person using the reasonable skill and care in handling his taxation affairs which one would expect to see from such an average person. To paraphrase English legal expressions, the word "reasonable" introduces the concept of the standard of care in handling his tax affairs which one would expect from the average man on a Hongkong tram or the M.T.R. or who takes his family out on a Sunday for lunch or to the Ocean Park.'*

This approach was adopted in some Board decisions but queried in others.

256. With respect, such approach is wrong.

257. 'Reasonable man' was used in the tort of negligence as the standard of care. We quote from the following passage in Charlesworth & Percy on Negligence, 11th Edition, paragraph 6-02.

> '**The reasonable man as the standard of care.** The ordinary standard of care adopted is referred to as "reasonable care", namely the standard of care of a reasonable man. In Alderson B.'s classic statement[29],
>
> > "Negligence is the omission to do something which a reasonable man, guided upon those considerations which ordinarily regulate the conduct of human affairs, would do: or do something which a prudent and reasonable man would not do." '

258. The learned editors go on to state in paragraph 6-06 that to say that the standard of care is that of a reasonable man can be to beg the question in that a tribunal of fact can only be directed to apply the standard of reasonable care if it is explained what amount of care the law regards as reasonable under the circumstances of the case being tried.

259. A search of the Department of Justice's Bilingual Laws Information System in mid-June 2008 found:

(a) the phrase 'reasonable excuse' in 979 statutory provisions in Hong Kong;

(b) the phrase 'reasonable man' in 2; and

(c) the phrase 'reasonable person' in 11.

260. If the legislature had intended to use the 'reasonable person' as the test for liability to additional tax, the legislature could easily have so enacted.

261. But the legislature did not do so.

262. What was enacted is that a person 'who without reasonable excuse' makes an incorrect return etc. shall be liable to be assessed to additional tax.

263. The correct approach is not to decide what a reasonable person would do or would omit to do. This is to confuse what was used as the standard of care in the tort of negligence with the *excuse* for non-compliance.

---

[29] Blyth v Birmingham Waterworks (1856) 11 Ex 781 at 784.

264. Reasonable excuse does not come in unless there is understatement or omission of income or profits etc. The wording in section 82A is 'any [taxpayer] who without reasonable excuse'. Instead of considering the excuse of the taxpayer on the *actual* facts of the case, the 'reasonable person' approach looks at what one may or may not expect from the *hypothetical* 'reasonable person'.

265. The significance of this is that, on the one hand, it excludes relevant actual personal attributes (which are not true in respect of the hypothetical 'reasonable person') of the taxpayer from consideration.

266. On the other hand, it includes irrelevant (which are not true on the facts of the case) matters.

267. By way of example, we do not think it is probable that 'the average man on a Hongkong tram or the MTR or who takes his family out on a Sunday for lunch or to the Ocean Park' would enter, or would have the resources and sophistication to enter, into a tax avoidance scheme such as the one in this case. If the 'reasonable person' approach were the correct approach, this is not what one would expect of the 'reasonable person' and the appellant must fail on the second ground of appeal.

268. As section 68(4) puts the burden of proving that the additional tax assessment is incorrect on the taxpayer:

(a) the taxpayer must identify and prove an excuse; and

(b) the Board must be satisfied that that excuse is reasonable.

'Excuses' put forward by the appellant

269. Whether or not the appellant had any excuse is a question of fact for the Board, not for the appellant, Accounting Firm AA, or any witness, factual or expert.

270. Whether or not any proven excuse is reasonable is a question for the Board, not for the appellant, Accounting Firm AA, or any witness, factual or expert.

271. The practice of accountants and the principles on which accountants acted and act in practice is a matter for recourse to evidence by accountants. Whether or not that practice was and is reasonable is a matter for the Board[30].

272. The appellant contended that on the 1986 version of section 16(2)(d):

[30] Cf. CIR v Secan Limited & another (2000) 3 HKCFAR 411 pages 418-419.

(a) 'the filing position adopted by [the appellant] was reasonable in light of the law and practice in relation to the IRO at that time'; and

(b) 'it was reasonable for [the appellant] to rely on [Accounting Firm AA]' s advice when preparing the Returns during the years in dispute'.

273. Both components or aspects of the reasonableness put forward by the appellant are premised on the following facts:

(a) advices given by Accounting Firm AA; and

(b) the appellant' s reliance on Accounting Firm AA' s advice.

274. We pressed Mr Sieker to:

(a) identify Accounting Firm AA' s advice and evidence on it; and

(b) identify evidence on reliance.

275. Mr Sieker took us through some documents but was unable to identify any evidence on the appellant' s reliance. He argued that it was an irresistible inference that the appellant relied on Accounting Firm AA' s advice.

Accounting Firm AA's 'advices'

276. In paragraph 4.2 of its Tax Planning Memorandum sent under cover of its letter dated 28 November 1991, Accounting Firm AA warned Mr H of the risk involved in these terms:

> '... It must be accepted as inevitable, however, that there exists a risk of having to defend the schemes against the anti-avoidance provisions. Nevertheless it could argue that the arrangement is a part the group re-organisation of [Group AU] with commercial substance (e.g. decentralisation – for easy/better management and control and other commercial reasons, property holding activities be segregated from the [merchandise] distribution/dealing business and other trading/retail activities).'

Accounting Firm AA estimated the front end costs and other legal and professional fees/charges were $3 million to $4 million.

277. By a note dated 12 December 1991 made by Ms AG of Accounting Firm AA of a luncheon meeting with Mr H, Ms AG noted that:

> '3. ... He was also amused that [Company C] previously sought our advice on every single matter (which should have been dealt with internally) and hence our fees were very high.
>
> 4. A Group Financial Controller had been appointed, who was an Ex. [Accounting Firm AK] ([Mr H] worked for [Accounting Firm AK] for eight years).
>
> ...
>
> 6. ... He said that based on his experience the local tax practice of [Accounting Firm AK] was weak whilst international tax planning was satisfactory; [Accounting Firm AK] offered quick local tax advice. (Note: He has previously expressed concern over the tax services provided by [Accounting Firm AA] [City AI, Country AJ] to [Company C] [(Country AJ)]).'

278. By fax dated 14 April 1992[31], Accounting Firm AA wrote to Legal Firm AL and copied to Mr I and 2 others in these terms:

> 'As discussed between yourself and [Ms AG] of our office, the loan participation agreement between [Bank A] Hong Kong branch and [Bank A] [City X] branch would require consideration and attention to documentation because of the fact that the Hong Kong branch and the [City X] branch of [Bank A] are the same legal entity. It is considered that the arrangement in respect of the loan sub-participation from [Bank A] to SPC through another [Bank A] branch/separate entity instead of direct participation from [Bank A] to SPC, would mainly give certain cosmetic effects to, and would not, in law, improve the tax effectiveness of the sub-participation financing arrangement. However, as you will appreciate, in order to maintain the cosmetic effect of the arrangement and to avoid uncertainties involved in the participation agreement between the Hong Kong and [City X] branches of [Bank A], it may be advisable if [Bank A] would participate the loans to another separate entity, e.g. a subsidiary or an associate of [Bank A], which would then enter into a sub-participation agreement with SPC.'

279. By letter dated 16 April 1992, Mr AB advised Mr I that from a taxation standpoint, the use of an offshore subsidiary as opposed to an offshore branch of Bank A was 'purely cosmetic':

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[31] Mr AB said the copy fax which he was looking at was not signed and he questioned whether this document had been sent. Under cross-examination in the afternoon of 25 January 2007, he was referred to a letter dated 16 April 1992 signed by himself referring to a 'recommendation made in our letter dated 14 April 1992' and he accepted that the fax dated 14 April 1992 had been faxed.

> 'I have spoken at length with [Mr AM] of [Legal Firm AL] concerning the recommendation made in our letter dated 14th April 1992. In that letter it is stated that preference is given to using an offshore subsidiary rather than the [City X] branch of [Bank A] as the intermediary vehicle between [Bank A] Hong Kong branch and the SPC.
>
> The use of an offshore branch is in accordance with our earlier discussions and recommendations hence [Bank A] are concerned that we should look to amend the structure at this late stage.
>
> From a taxation standpoint I do not believe that the use of an offshore subsidiary as opposed to an offshore branch would add a great deal to the structure. The reasons for this is that the structure is ultimately reliant on the fact that the funds are borrowed from a bank and the loan is not secured or guaranteed in any way by a deposit place by an associated company with a financial institution. Hence the advantage of using a subsidiary is purely cosmetic in that it is unusual to arrange for a subparticipation between two branches. However as the loan is ultimately sub-participated to a [Bank A] subsidiary, the SPC, the end result has been effectively achieved.
>
> Summarising the position I would prefer to see an offshore subsidiary used as opposed to an offshore branch of [Bank A] but I am of the opinion that the current structure does not weaken the basis on which the Group will seek to claim a tax deduction for interest paid on the loans from [Bank A].'

280. The undated note made by Ms AG of Accounting Firm AA of a meeting on 12 May 1992 with Mr I, Ms AN, Mr AM, Mr AO, Mr AB and herself at the office of Legal Firm AL referred to Mr AM's suggestion to seek counsel's opinion on stamp duty relief and continued as follows:

> '4. [Mr AB] said that he could understand the risk involved in this issue which would be similar to S61A anti-avoidance risk in all kinds of tax schemes. [Mr AB] furthered that, however he was not aware of any practical problem in similar arrangement previously.
>
> 5. It was agreed that [Mr I] would discuss with [Mr H] on the risk involved in the stamp duty exemption and suggested that [Mr H] would discuss with [Mr AM] directly, if considered appropriate.
>
> 6. After the meeting [Mr I] agreed that the Council (*sic*) opinion might also be inconclusive and would not help them to resolve the uncertainties. He requested us to send him a letter stating that the risk involved was a technical risk and we had not encountered any practical problems before. We would

> also include our suggested alternative. [Mr I] would after receiving our letter discuss with [Mr H] accordingly.'

281. By letter dated 13 May 1992, Mr AB advised Mr I of an alternative arrangement by which the property sale be financed by an inter-company loan shortly after which a financing arrangement be effected:

> 'If this option was adopted it could technically raise a profits tax issue in that it would be necessary to consider if it could be maintained that the loan had not been incurred to earn profits chargeable to tax but merely to refinance intra-group loans.
>
> I have reviewed various Hong Kong, Australian and U.K. Case law but I have been unable to find any persuasive authority on this issue. However, the U.K. case of Lawson (HMIT) v Brooks does provide an element of comfort. The case concerned an appeal from a decision of the general commissioners, who had concluded that relief was available in respect of interest on loans which replaced various overdrafts incurred for the improvement of land. However the High Court overturned this decision as the replacement loan was effected by book entries, i.e. nothing was paid. Notwithstanding the decision of the High Court, one might infer that the decision would have been different if the overdrafts had been physically repaid from the proceeds of a new loan.
>
> Reference might also be made to the U.K. case of Scorer v Olin Energy System Ltd, particularly at page 58 TC 606:
>
> > "Whether interest was paid for the purposes of a trade must depend on whether the loan, on which the interest was paid, was itself incurred for the purpose of the trade. It does not necessarily follow that the purpose of the loan can be ascertained by looking at the immediate use to which the borrower applies the money. The question is one of fact to be decided on the evidence available in each case."
>
> If one followed these lines of argument it would be possible to conclude that the loan had been taken out for business purposes and, in so far as the interest on the initial loan was accepted as a revenue expense, the interest on the replacement loan should be ascribed the same character. I would further add that we have many examples in the office of interest payable on refinancing loans and I cannot recall a single situation which has been challenged by the IRD on the basis that the replacement loan was not incurred for earning profits chargeable to tax.'

282. The undated note made by Ms AG of Accounting Firm AA of a meeting on 3 June 1992 with Mr I, Ms AN, Mr AP and Ms AQ, both of Legal Firm AR, Mr AO of Legal Firm AL

and herself at Company C's office referred to the potential stamp duty issue and the decision to split the transaction into two sections, i.e. to sell and assign first and to arrange for the banks loans to repay inter-company accounts 2 – 3 weeks later and continued as follows:

> '2. The potential risk associated with the deductibility of interest expenses was discussed. [Mr AP] said that this alternative might expose [Company C] to a higher risk that interest costs incurred by the borrowers would be disallowed. [Mr I] replied that they would rely on [Accounting Firm AA] who were happy with this arrangement.
>
> [Ms AG] reiterated our comments as contained in our letter to [Mr I] in this connection that although in practice we had not come across any interest disallowance on borrowings to repay inter-company loan arising from a property acquisition; however in other jurisdictions, e.g. UK there were court cases which were determined to the disadvantage of the taxpayer.'

283. By a note dated 26 June 1992 of a meeting between Bank A and Company C, Mr AS noted that he was told by Mr I who had been advised by Accounting Firm AA that the Revenue had recently disallowed an internal refinancing scheme identical to the one which [Bank A] was then involved for Company C. The file note stated as follows:

> 'I had a meeting with [Mr I] from [Company C] this afternoon (26 June 1992). He had just been advised by [Accounting Firm AA] that the IRD had, within the past few days, disallowed an internal refinancing scheme identical to the one in which we are currently involved for [Company C].
>
> Apparently, the completion of internal funding arrangements all in one day (which from our point of view will involve a number of book entries here and in NAB), is too transparent for the Revenue. …
>
> You will recall that this arrangement has been structured to reduce the aggregate Hong Kong Profits Tax burden of the [Group AU]. The structure involves us in granting two 5-year loans totalling HKD1,410m, enabling [the appellant] and [Company AV] to acquire two Service Centres from the parent. The loans will be sub-participated to an offshore SPC owned by the Bank, whilst the loan proceeds will flow through the [Group AU] and be used to purchase Redeemable Preference Shares in SPC, thereby funding the SPC's loan sub-participation. Interest on the loans will flow through as dividends on the Redeemable Preference Shares. Our fees for this transaction are a pro-rata upfront Arrangement Fee totalling HKD4.23m (30bp), and an annual HKD100,000 management fee.

> [Accounting Firm AA]' s initial response to the IRD stance on this structure is to suggest that if the sub-participation of the loan is delayed by one day, then that will be enough to legitimise the deal. We had originally obtained approval on the basis that our only risk was a management risk relating to the passing of entries in the books of HKH and corresponding entries over the HKD account of NAB with HKH.
>
> [Accounting Firm AA] are now suggesting that NAB' s sub-participation to the SPC should be delayed; this will give rise to an overnight loan in NAB' s books (which will require credit approval), although there will also be a deposit for an equal amount with them in the name of the SPC. [Mr I] asked if we would have any problems with this proposed change and what the pricing implications of this "back-to-back" arrangement would be. I think we can probably absorb a lending margin of say 50bp for one day (HKD19,300) in the Arrangement Fee.'

284. By letter dated 30 June 1992, Accounting Firm AA advised Mr I to delay the sub-participation by one day:

> 'As discussed with you, the funds flow movement is an essential factor which requires particular attention in order to ensure the tax effectiveness of the financing arrangement. For the purposes of claiming deductions in respect of the interest costs and other related expenses incurred, it is important that the conditions specified in section 16 Inland Revenue Ordinance are satisfied. Accordingly [Company AV] and [the appellant] need to be able to demonstrate that such expenses are incurred on borrowings advanced to them by [Bank A], and not on funds provided by [Company E], an associated corporation. We stress that there exists a high risk that the interest expense deductions would be denied if the financing transaction was effected only by accounting entries recorded in the books of [Company AV], [the appellant] and [Company E], i.e. with no funds movements, or in the absence of evidence proving that loans were advanced to [Company AV] and [the appellant] by [Bank A].
>
> Because any inappropriate movement of funds would be detrimental to the whole financing arrangement we suggest that the following sequence is adopted and supported by evidence (e.g. bank advice):
>
> FUND FLOWS MOVEMENTS
>
> | | FROM | TO | PURPOSES |
> |---|---|---|---|
> | Day 1 | | | |
> | i) | Bank Q (City X) | Bank A | Loan participation |

ii)	Bank A	the appellant and Company AV	Provision of bank loans
iii)	the appellant and Company AV	Company C	Repayment of interest-bearing loan
iv)	Company C	Group AU	Repayment of inter-company current account
v)	Group AU	Company E	Provision of interest-free inter-company loan
vi)	Company E	SPC	Subscription of non-voting redeemable preference shares.
vii)	SPC	Bank A or Bank Q (City X)	Deposit placement
<u>Day 2</u>			
i)	Bank A or Bank Q (City X)	SPC	Deposit uplift
ii)	SPC	Bank Q (City X)	Loan sub-participation'

285. By an undated note which should be made on about 29 July 1992, [Ms AG] made a note of her review of the draft minutes on the proposed disposal of property by Company C to the appellant and commented in respect of the minutes of Company E that:

> 'It may be considered appropriate to approve the option agreement in a separate minutes (to avoid the explicit link of the option agreement with the transaction (although this is the fact).'

The revised draft minutes received by Accounting Firm AA on 29 July 1992 had not incorporated her comments and she discussed the matter with 'Mr I' who would follow up with Ms AN.

The draft resolution included the following:

> 'that an option agreement is intended to be executed between the [Company E] and [Bank A] under which the [Company E] shall grant to [Bank A] an option to require the [Company E] to purchase and [Bank A] shall grant to the [Company E] an option to require [Bank A] to sell the Option Shares.'

286. By letter dated 7 September 1992, Accounting Firm AA informed Mr I that it had reviewed the final draft of the documents and in paragraph 5 repeated its warning of the risk involved:

> 'ANTI-AVOIDANCE LEGISLATION
>
> (a) The enclosed draft documents have been considered in conjunction with the specific provisions in the Inland Revenue Ordinance (' IRO') which limit interest deductibility, for Profits Tax purposes. The draft documents have been prepared to ensure better arguments in favour of obtaining the required tax relief. However, it must be recognised that, to a certain extent, the financing arrangement adopted depends on the interpretation of those provisions and in such circumstances, it must be accepted that the IRD may adopt a different interpretation.
>
> (b) As you appreciate, any tax planning arrangement may be subject to the scrutiny of and attack by the IRD under the general anti-avoidance provisions contained in Section 61A of the IRO, under which any arrangement may be set aside if its sole and dominant motive is the avoidance of taxation.
>
> However, it is not anticipated that the general anti-avoidance provisions would be applied where a scheme is supported by a genuine commercial motive, even though tax planning is a major feature in the way in which the re-organisation is carried out. Accordingly, there always exists the risk of having to contend that the commercial motive is the dominant factor for entering into the arrangement thereby negating the contention that the anti-avoidance provisions apply. In this context it could be argued that the entire arrangement forms a part of Group AU reorganisation, following the acquisition Group AU by Company B. The reorganisation has commercial substance of decentralisation of the property investment business of Company C for better/efficient management, further development of the core business of Company C etc.'

Board' s decision on second ground of appeal

287. Dr AC told us that he had no actual knowledge of what the appellant in fact believed at the material time when the tax returns were filed and that he did not know for a fact what the appellant' s intentions were in entering into the tax scheme.

288. Mr AB told us that he was not actually in a position to tell us all the detail of advice that would have been given to the client about the tax scheme.

289. On the facts of this case, Accounting Firm AA's advices were non-committal and some what wishy-washy:

(a) In Accounting Firm AA's letter dated 28 November 1991, having warned that there existed a risk of having to defend against the anti-avoidance provisions; Accounting Firm AA put forward some arguments but expressed no opinion on the prospects of success of the arguments.

(b) At the meeting on 12 May 1992, Mr AB said the risk would be similar to, that is to say, no greater and no less than, S61A anti-avoidance risk in all kinds of tax schemes. He went on to say that he was not aware of any practical problem in similar arrangement previously.

(c) In his letter dated 13 May 1992, Mr AB raised the issue of deductibility; stated that there was no 'persuasive' authority; cited a case which had been 'overturned' on appeal and argued that one *might* infer that the decision would have been different if the overdrafts had been physically repaid from the proceeds of a new loan.

(d) At the meeting on 3 June 1992, having said in one breath that they had not come across any interest disallowance on borrowings to repay inter-company loan arising from a property acquisition, Ms AG went on to say in the next breath that in other jurisdictions, e.g. UK, there were court cases which were determined to the disadvantage of the taxpayer.

(e) By 26 June 1992, Mr I had just been advised by Accounting Firm AA that the Revenue had recently disallowed an internal refinancing scheme which was identical to the one which Bank A and Company C was involved in, Accounting Firm AA claimed that delaying the sub-participation by one day would make a material difference but did not explain why.

(f) By letter dated 30 June 1992 to Mr I, Accounting Firm AA stressed that there exists a 'high' risk that the interest expense deductions would be denied if the financing transaction was effected only by accounting entries with no funds movements; stated that any inappropriate movement of funds would be 'detrimental to the whole financing arrangement'; and suggested delaying the sub-participation by one day, without expressing any view on the effectiveness of the deferment. This is a case where the funds remained throughout under the control of the Bank A group and a circular flow of funds did not cease to be circular merely by extending the time it took by one day.

(g) By letter dated 7 September 1992, Accounting Firm AA sent the final draft of the documents; warned in no uncertain terms of the risk involved; put forward some arguments; but did not say a word about the prospects of success of such arguments.

290. In his evidence in chief, Mr AB dealt with the warning in the 9 September 1992 letter thus:

'A. ... Our belief was that the taxpayer was entitled to deduction under section 16(2). However, we felt that it is always our responsibility to alert a taxpayer to the existence of section 61A. In fact, even though we believed it wasn't applicable, it was up to the assistant commissioner to take his view as to what he felt was or was not appropriate.

Q. So would this be a risk that you would identify in any tax planning arrangement?

A. Yes. It was a policy of, certainly of [Accounting Firm AA] at that time, that if we were advising on any structure which had a tax impact we would always qualify any opinion we gave as to the application of section 61A because at that time there was insufficient evidence or precedents to give us any specific guidance as to how the revenue would apply it.'

In re-examination, Mr AB said it was not for Accounting Firm AA to judge whether sections 61 or 61A applied:

'Q. Did you think that section 61 or 61A applied?

A. We felt that it wasn't for us to judge. There was insufficient court material, cases, from which to determine how it was to be applied in Hong Kong by the commissioner at that time. I don't think we or any other person really knew then where 61 or 61A was to be applied and where it was not, whether it was affected by having specific anti-avoidance legislation or whether it was not. We believed Ramsay didn't apply at that time, for certain, which made the application of 61A even more difficult to interpret.'

291. Given the sophistication of the client, the extensive documentation, the fact that advices were given some 14 years ago and the fact that this was just one of his many cases, we look to the documentation for the contents of advices given. The beliefs or views of Mr AB or Accounting Firm AA are irrelevant if they were not communicated to the appellant. There is no evidence of any oral communication to the appellant of any beliefs or views which departed from or

modified the advices contained in or evidenced by letters, faxes, attendance notes or other documents.

292. It is clear from the documents referred to above and from the evidence in chief and in re-examination of Mr AB that Accounting Firm AA refrained from expressing any view on the applicability of section 61A. Advices on such footing are non-committal and somewhat wishy-washy. To advise that the Revenue might take a different view and that the Revenue might seek to invoke the anti-avoidance provisions without advising on whether the Revenue's view was the correct view is pretty useless advice.

293. Whether the appellant did in fact rely on the advices of Accounting Firm AA is a matter peculiarly within the knowledge of the appellant. The appellant's group financial controller had been with [Accounting Firm AK] for 8 years. There is no evidence, oral or documentary, such as internal documents, on reliance.

294. Absent any factual basis for the second ground of appeal, it must fail.

295. Even if, contrary to our decision, the appellant did rely on Accounting Firm AA's advices, we do not think it was reasonable for the appellant to do so. In other words, we do not think the excuse of reliance on Accounting Firm AA's advices was a reasonable excuse:

(a) The appellant had been warned about local and overseas cases which went against taxpayers. The appellant chose to ignore those warnings. It did so at its own peril.

(b) The appellant also chose to ignore the advice given by Legal Firm AR at the meeting on 3 June 1992 that the decision to split the transaction into two sections, i.e. to sell and assign first and to arrange for the banks loans to repay inter-company accounts 2 – 3 weeks later might expose Company C to a higher risk that interest costs incurred by the borrowers would be disallowed.

(c) Mr Sieker placed heavy reliance on what he described as the 'uncertainty and evolving nature of section 61A'. Those were reasons for caution, not reasons for turning a blind eye to the uncertainty; ignoring the warnings, and choosing to implement the tax scheme, as the Board so found as a fact in the Decision, for the sole or dominant purpose of avoiding its liability to pay profits tax on the rental income or reducing the amount of tax payable on such rental income.

296. The least which the appellant should have done was to seek an advance ruling under Departmental Interpretation & Practice Notes, No. 15, issued on 1 May 1986, paragraphs 30 and 31 of which provided that:

*'**The ruling itself***

30. Rulings will be issued in letter form personally signed by the Commissioner or Deputy Commissioner. The Department does, however, reserve the right not to issue a ruling in any particular case, for example, where the information provided is considered to be insufficient. In such cases, the taxpayer will be advised of the reason why a ruling will not be issued. So far as the issue of rulings is concerned the Department will adopt a case by case approach. A ruling given in one case should not be regarded as binding the Department to a similar ruling in a subsequent case. In this regard, it should be apparent that rulings under Sections 61A and 61B will invariably turn on their own facts.

31. As a matter of law, rulings cannot be made binding on the Department. At the same time, taxpayers may assume that provided that there are no deviations between the information supplied when the ruling was given and the eventual facts, the Department will act in accordance with the ruling. Of course, it is expected any changes to the basis fact situation which take place after a favourable ruling has been given will be notified to the Department.'

297. If the Revenue should change its mind after issuing a favourable ruling to the taxpayer, the taxpayer might have some factual basis for a reasonable excuse. This was not what happened in this case. The appellant did not seek any advance ruling.

298. Seeking an advance ruling is premised upon full and frank disclosure to the Revenue. What Accounting Firm AA and Bank A did was to make the tax scheme more complex and more difficult for the Revenue to know about and to unravel the scheme.

(a) A more 'sophisticated' sub-participation scheme involving redeemable preference shares was adopted in place of Bank A's 'simple' sub-participation schemes.

(b) Bank Q was interposed between Company O and Bank A.

(c) The funds were channelled through an overseas entity, 'otherwise the circulation of funds may be too transparent'.

(d) Ms AG' s mindset and approach was to avoid the factually correct 'explicit' link to the option agreement. On the face of the tax scheme, Company O was a Bank Q or Bank A group company. However, when one looked at the option agreement (see paragraph 41 above), it became clear that Company E had full

control of Company O and that Company E had a call option and Bank Q had a put option.

299. We agree with the submission of Ms Li that acting on advices on the tax scheme which depended on concealment, or not giving the Revenue full and frank disclosure, for its success does not constitute a reasonable excuse.

300. We have already ruled that reasonableness is a matter for the Board, not for any witness. In any event, the evidence of Dr AC does not assist the appellant because of what he said at the end of his re-examination:

> 'Q. Ms Li also asked you how you would advise a taxpayer if the taxpayer was entering into a transaction for the sole or dominant purpose of tax avoidance, and you said you would only advise not to disclose if there was not a strong chance of section 61A being invoked. Did you think, during the years in question, that there was a strong chance of section 61 or 61A being invoked for transactions of the type entered into with relation to [the appellant]?
>
> A. I think there are several questions there. Section 61 and 61A, I would have had totally different views on. Section 61 at the time was believed to be rather impotent and I think that was the reason for 61A being introduced; it was a much stronger tool for the revenue to use against whatever transaction that they thought it had to be used against. The issue is not likelihood or possibility. The question I believe I was asked is if I knew the commissioner would invoke 61A what would my reaction be? If I knew for certain that section 61A would be invoked, then I would have a totally different approach towards a transaction of this nature. The type of loan sub-participation arrangement that [the appellant] entered into, it was questionable, debatable, arguable, and if I had to put a percentage on it, it was probably no more than 50/50. At the time [the appellant] did this transaction it really wasn't clear in what circumstances the revenue or assistant commissioner would invoke the anti-avoidance powers that were embraced in section 61A.
>
> Q. And that would be true even if you operated under the assumption that the transaction was solely tax motivated or principally tax motivated?
>
> A. Indeed, indeed.'

301. Ground 2 fails.

WHETHER EXCESSIVE HAVING REGARD TO THE CIRCUMSTANCES – THIRD GROUND OF APPEAL

Penalty for unsuccessful tax avoidance

302. In D115/01, IRBRD, vol 16, 893 at paragraph 14, the Board [Patrick Fung Pak Tung SC, Michael Robert Daniel Bunting and Susan Beatrice Johnson] stressed the importance of true and complete reporting by taxpayers:

> *'The notes accompanying a tax return make it quite clear that the duty is on a taxpayer to complete a true and correct tax return. As is stated in the Guidelines, the effective operation of Hong Kong's simple tax system requires a high degree of compliance by taxpayers. If every taxpayer is careless or reckless in making tax returns, the task of the already over-burdened IRD will become impossible to perform. This is unfair to the community at large. A taxpayer therefore cannot be heard to complain if a penalty is imposed against him or her according to the statutory provisions.'*

303. Tax avoidance is not unlawful. Tax avoidance schemes may succeed or fail. If they succeed, tax has been lawfully avoided. If they fail, whether because they are caught by the anti-avoidance provisions or otherwise, in the absence of any reasonable excuse, the question of penalty falls to be considered.

304. Tax avoidance scheme cases are not cases of carelessness or recklessness. Taxpayers enter into tax avoidance schemes as a matter of choice. They do so knowingly and deliberately.

305. They submit returns which appear on their face to be regular and there may be nothing to alert the Revenue to the need to look further.

306. If the Revenue does not begin investigation within 6 years after the expiration of a year of assessment, in the absence of fraud or wilful evasion, the Revenue is out of time and cannot assess under section 60. Revenue is permanently lost in these cases.

307. In most cases, there will be actual loss of revenue. The taxpayers will have had the use of the amounts which should have been paid as tax and there is a corresponding loss in revenue during which the taxpayers have had the use of the tax avoided.

308. If the Revenue does begin investigation within 6 years, it may face delaying tactics and un-cooperativeness, if not obstruction.

309. Tax avoidance schemes are usually complex, if not highly complex. It is in the interests of scheme vendors and those who charge fees for devising and advising on schemes to increase the scheme's complexity so as to make it difficult to detect and crack.

310. It will take the assessors, the Assistant Commissioners, and the Commissioner or her deputies a lot of resources and expertise to piece the schemes together, unravel and to crack them.

311. If the matter goes on appeal, the Revenue will have to undertake the task of assisting the Board/Court to understand, unravel and crack the tax avoidance schemes.

312. As stated earlier, if the tax avoidance schemes work, taxpayers benefit to the extent of the tax avoided.

313. If the tax avoidance schemes fail, there is no reason why taxpayers should not pay a price. They must be punished and other taxpayers must be deterred from incorrect reporting without reasonable excuse.

314. Section 82A provides for the maximum amount by reference to *'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'*.

315. For incorrect return cases, the maximum amount varies, depending on the size of the tax *'which 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'*.

316. This is precisely the reason why there are numerous Board decisions making it clear that the correct approach in additional tax cases is to look at the additional tax as a percentage of the amount of tax involved.

317. Where the amounts of tax involved are high, the maximum amount of additional tax will correspondingly be high in dollars. Taxpayers who chose to play with high stakes must be prepared to pay a penalty in terms of a percentage of the stack which they chose to play with.

Whether excessive having regard to the circumstances in this case

318. The appellant was a sophisticated taxpayer, with experienced professional accountants in senior management and is part of a large listed group.

319. The appellant entered into the tax scheme for the sole or dominant purpose of tax avoidance.

320. It entered into the tax scheme as a matter of choice, doing so knowingly and deliberately, despite the warnings and qualifications by Legal Firm AR and Accounting Firm AA.

321. Mr Sieker submitted that the fact that the appellant had no intention to evade tax was a mitigating factor. As the Board has said time and again, see e.g.:

(a) D62/96, IRBRD, vol 11, 633, at paragraph 23 [Robert Wei Wen Nam QC, John Peter Victor Challen and Benjamin Kwok Chi Bun]; and

(b) D59/05, (2005-06) IRBRD, vol 20, 821 at paragraph 32 [Kenneth Kwok Hing Wai SC, David Ho Chi Shing and David Wu Chung Shing];

while an intention to evade tax is undoubtedly an aggravating factor, lack of intention to evade tax is not a mitigating factor for the simple reason that no taxpayer should have the intention to evade tax. The appellant chose to enter into the tax scheme.

322. Payment of tax is not a mitigating factor. It is the duty of every taxpayer to pay the correct amount of tax. If the taxpayer does not pay tax, on time or at all, the taxpayer will be subject to enforcement action, see, e.g.:

(a) D3/02, IRBRD, vol 17, 396, at paragraph 12 (Kenneth Kwok Hing Wai SC, Winnie Lun Pong Hing and Daniel Wan Yim Keung); and

(b) D59/05, (2005-06) IRBRD, vol 20, 821 at paragraph 31 (Kenneth Kwok Hing Wai SC, David Ho Chi Shing and David Wu Chung Shing).

Mr Sieker relied on the purchase of tax reserve certificates. The Commissioner had already taken this into account in computing interest or commercial restitution by treating tax as paid on the actual due dates, see paragraph 331 below.

323. The tax scheme was a complex one because the appellant made it so, see paragraph 298 above.

324. It was not easy to piece the tax scheme together, see paragraph 336 below.

325. The hearing of the previous appeal to the Board took 8 days. The respondent had instructed 2 leading and 1 junior counsel to conduct the appeal and had incurred substantial legal costs. We agree with the submission of Mr Sieker that the appellant's previous appeal to the Board cannot be held against the appellant. On the other hand, there can be no discount for a 'guilty' plea.

326. We should add that we have not held the current appeal against the Assessments against the appellant. The current appeal against the Assessments is not a factor in our assessment on excessiveness in this case.

327. By extending the repayment date by 5 years in November 1997, the appellant deliberately continued its omission or understatement for 5 more years.

328. By increasing the interest rate to 13% in November 1997, the appellant deliberately increased the amounts of omission or understatement.

329. In the event, the omission or understatement went on for at least 7 years.

330. The appellant's returns omitted or understated its assessable profits by 99.91%. In dollars, it omitted or understated its assessable profits by $596,103,072, a phenomenal amount. The amount of tax undercharged, or would have been so undercharged if its return had been accepted as correct, was $95,878,877, or 100% of the correct amount of tax of $95,878,877. Had the understatements in this case not been detected, honest taxpayers would have to come up with an extra $95 million. The appellant chose to play with high stakes and the time has come for the appellant to pay a correspondingly high penalty.

331. There is actual loss in revenue in this case:

Year of assessment	Tax undercharged ($)	Normal due date	Actual due date	No of complete months
1994/95	17,602,805	January 1996	11 May 2001	64
1995/96	14,525,362	January 1997	24 April 2002	63
1996/97	14,551,550	January 1998	30 August 2002	55
1997/98	12,903,085	January 1999	30 August 2002	43
1998/99	13,649,683	January 2000	30 August 2002	31
1999/2000	11,116,111	January 2001	30 August 2002	19
2000/01	11,530,281	January 2002	30 August 2002	7

332. On average, the prime rate of Bank A from January 1996 to 30 August 2002 was more than 7% per annum.

333. Section 49(1)(b) of the High Court Ordinance, Chapter 4, and section 50(1)(b) of the District Court Ordinance, Chapter 336, provide that judgment debts carry simple interest at such rate as may be ordered by the judge, in the absence of which, at such rate as may be determined from time to time by the Chief Justice by order. The Chief Justice has ordered the rate of interest on judgment debts as follows:

% per annum	Effective date	% per annum	Effective date

10.000	1-5-1990	10.860	1-11-1990
13.110	1-2-1991	12.940	1-3-1991
12.500	1-4-1991	12.660	1-7-1991
13.500	1-8-1991	12.500	1-9-1991
12.250	1-11-1991	12.000	1-12-1991
11.280	1-1-1992	11.500	1-4-1992
11.270	1-7-1992	9.690	1-10-1992
9.500	1-1-1993	9.730	1-7-1994
10.300	1-10-1994	10.720	1-1-1995
11.630	1-4-1995	12.000	1-7-1995
11.750	1-4-1996	11.500	1-7-1996
11.680	1-7-1997	12.060	1-1-1998
12.900	1-4-1998	13.080	1-7-1998
13.000	1-10-1998	12.860	1-1-1999
11.940	1-4-1999	11.540	1-7-1999
11.260	1-10-1999	11.260	1-12-1999
11.500	1-1-2000	11.540	1-4-2000
11.980	1-7-2000	12.500	1-10-2000
12.500	1-1-2001	12.080	1-4-2001
10.860	1-7-2001	9.820	1-10-2001
8.720	1-1-2002	8.140	1-4-2002
8.125	1-7-2002	8.125	1-10-2002
8.093	1-1-2003	8.000	1-4-2003
8.000	1-7-2003	8.000	1-10-2003
8.000	1-1-2004	8.000	1-4-2004
8.000	1-7-2004	8.000	1-10-2004
8.069	1-1-2005	8.000	1-4-2005
8.245	1-7-2005	9.234	1-10-2005
10.088	1-1-2006	10.711	1-4-2006
10.921	1-7-2006	11.000	1-10-2006
10.934	1-1-2007	10.750	1-4-2007
10.750	1-7-2007	10.750	1-10-2007
10.420	1-1-2008	9.398	1-4-2008

334. The Commissioner started with a penalty loading of 35%, then added interest at 7% per annum compounded monthly, but capped it at 60%. Having regard to the commercial and judgment interest rates referred to in paragraphs 332 and 333 above, 7% is a modest rate. Capping it at 60% resulted in a discount of the total penalty by $8,632,294.

Percentage of penalty

Year of assessment	Tax undercharged	Penalty loading	Commercial restitution	Total penalty	Penalty imposed	imposed to tax undercharged
	$	$	$	$	$	
1994/95	17,602,805	6,160,981	7,938,689	14,099,670	10,560,000	60%
1995/96	14,525,362	5,083,876	6,428,634	11,512,510	8,720,000	60%
1996/97	14,551,550	5,093,042	5,485,788	10,578,830	8,730,000	60%
1997/98	12,903,085	4,516,079	3,666,540	8,182,619	7,740,000	60%
1998/99	13,649,683	4,777,389	2,697,040	7,474,429	7,470,000	55%
1999/2000	11,116,111	3,890,638	1,298,917	5,189,555	5,190,000	47%
2000/01	11,530,281	4,035,598	479,083	4,514,681	4,510,000	39%
Total	95,878,877	33,557,603	27,994,691	61,552,294	52,920,000	55%

335. The tax scheme was entered into in October and November 1992. The Assistant Commissioner issued the first of the assessments referred to in paragraph 75 above, i.e. the one for 1994/95, on 30 March 2001. By that time, more than 6 years have elapsed after the expiration of the 1992/93 and 1993/94 years of assessment. The Revenue suffered permanent loss of revenue because it was out of time and could not assess under section 60 in respect of the 1992/93 and 1993/94 years of assessment. Mr Sieker objected to any reliance on the amounts of tax lost for these 2 years of assessment. We upheld his objection on the ground that it was raised too late in the day. We have thus not heard the parties on this aspect. If we had not upheld the objection, we would have to be persuaded why such permanent loss is not a material circumstance for consideration on the question of excessiveness. As Madam Justice Yuen said *obiter* in Chan Min Ching v CIR [1999] 2 HKLRD 586 at page 589, the reference to 'having regard to the circumstances' gives a wide discretion to the Board.

336. The Commissioner treated this as a case of 'disclosure with full information promptly on challenge'. With respect, the Commissioner erred in favour of the appellant. There is some co-operation, but not full and prompt co-operation. There was some obstruction:

(a) Accounting Firm AA and Bank A sought to make it more difficult for the Revenue to know about and to unravel the tax scheme, see paragraph 298 above.

(b) By letter dated 26 January 2000, the assessor wrote under section 51(4)(a) to the Account Services Department – Official Enquiries Section of Bank A to require production of documents in respect of the Loan. Interestingly, Bank A asserted by letter dated 1 February 2000 that the appellant did "not appear to have maintained any Loans Account with us". The assessor wrote again by letter dated 11 February 2000 to the Corporate Banking – International Division of Bank A and Bank A replied by letter dated 9 March 2000 enclosing some documents. By the time of the reply, the time limit for assessing under section 60 in respect of the 1993/94 year of assessment was about to expire.

(c) By letter dated 15 February 2001, the assessor informed the appellant that the Revenue was conducting an audit on its tax return for 1997/98 and would like to discuss its financial affairs.

(d) By letter dated 25 June 2002, the assessor wrote to Company B to make enquiries including 'whether sums payable as preference share dividend by [Company O] were used to settle the interest payments of [the appellant], directly or indirectly through intermediaries'. By letter dated 15 October 2002, Accounting Firm AA replied on behalf of Company B asserting that there 'was no correlation of fund flows in respect of the receipt of preference share dividend income by Company E from Company O and the payment of interest expenses by [the appellant] to Bank A.' Accounting Firm AA's assertion on behalf of Company B was false, see paragraphs 51 and 231 above.

(e) The appellant has at no time volunteered to tell the Revenue about the whole scheme. It responded to enquiries.

(f) By letter dated 28 September 2004, the assessor wrote under section 51(4)(a) to Accounting Firm AA asking for information and documents in connection with the Loan. By letter dated 26 October 2004, Accounting Firm AA asserted that it would be more appropriate for the assessor to address the requests to Bank A and claimed that 'the engagement partner has already retired from the firm'. By letter dated 29 October 2004, the assessor pointed out that Ms AG was still with Accounting Firm AA and persisted in the requests under section 51(4)(a). By letter dated 9 November 2004, Accounting Firm AA replied enclosing some copy documents.

(g) Bank A and Accounting Firm AA produced relevant documents in late 2004 pursuant to section 51(4)(a).

(h) We agree with Ms Li that the appellant's attitude was one of 'catch us if you can'.

337. Mr Sieker told us that this is a test case and that 'dozens and dozens of other taxpayers (perhaps hundreds) entered into similar transactions'. Prevalence of a breach of statutory reporting duty calls for a deterrent penalty. Taxpayers in failed tax avoidance schemes should not have unrealistic hope for sympathy.

338. Mr Sieker has said everything which could be said on behalf of the appellant. We have carefully considered his submission. In our decision, the Assessments are not excessive in the circumstances.

Board's power to increase additional tax assessments

339. On the contrary, we think that the Commissioner erred in being too lenient with the appellant. 35% is too modest a penalty for this case and, in general, for scheme cases. Taxpayers who played with high stakes should be prepared to lose high stakes. Further, there is no reason why the penalty should be capped at 60%.

340. The Board's power under section 68(8)(a) includes the power to increase the assessment appealed against.

341. In D41/89, IRBRD, vol 4, 472, the Board [H F G Hobson, Graeme Large and Norman Leung Nai Pang] increased the penalty assessment from 65% to 100%.

342. In D53/92, IRBRD, vol 7, 446, the Board [William Turnbull, Eugene Ho and Jao Yu Chung] increased the penalty assessments from $104,000 to $348,950, i.e. 200% of the tax involved.

343. In D37/94, IRBRD, vol 9, 254, the Board [William Turnbull, Gillian M G Stirling and Yu Yui Chiu] considered that the Commissioner was unduly lenient with penalty assessments of 108% and 104% and would have increased them had the Commissioner asked for an increase.

344. In D65/00, IRBRD, vol 15, 610, the Board [Kenneth Kwok Hing Wai SC, Berry Hsu Fong Chung and Vincent Mak Yee Chuen] increased the penalty assessment from 75% to 100%.

345. We have considered the question of whether we should increase the Assessments. As this is the first case of its kind to be argued before the Board, we have decided not to do so in this case, but to send a clear message to taxpayers. We wish to impress upon taxpayers, scheme vendors, devisers and advisers that taxpayers in subsequent cases should not expect exceptional leniency, even if they have, as the appellant did, the benefit of representation by an able advocate like Mr Sieker.

CONCLUSION

346. The appeal fails and must be dismissed.

DISPOSITION

347. We dismiss the appeal and confirm the Assessments.