INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D24/95

Penalty tax – failure to inform Commissioner of chargeability to tax – quantum of penalty – section 82A of Inland Revenue Ordinance.

Panel: Maxine Kwok Li Yuen Kwan (chairman), Calvin Fung Chor Hang and Edwin Wong.

Date of hearing: 2 May 1995.
Date of decision: 29 May 1995.

The taxpayer was a company which was carrying on business in Hong Kong and marking profit but failed to inform the Commissioner of Inland Revenue until some years later. The Commissioner imposed penalty tax assessments which ranged from a minimum of 14% to a maximum of 25%.

Held:

The penalty tax assessments were not excessive.

Appeal dismissed

Cases referred to:

D33/89, IRBRD, vol 4, 359
D5/92, IRBRD, vol 7, 84
D11/93, IRBRD, vol 8, 143

Ngai See Wah for the Commissioner of Inland Revenue.
Connie Lai Sung King of Messrs S H Yeung & Co for the taxpayer.

Decision:

This is an appeal by a taxpayer against additional tax assessments raised upon the Taxpayer under section 82A of the Inland Revenue Ordinance (the IRO) for the years of assessment 1989/90 to 1992/93 in respect of the failure by the Taxpayer to notify the Commissioner of Inland Revenue of the Taxpayer's chargeability to tax as required by section 51(2) of the IRO. The facts are as follows:

1. The Taxpayer was incorporated in Hong Kong in April 1989.

2. On 13 February 1990, a provisional profits tax return for the year of assessment 1989/90 was issued to the Taxpayer under section 51(1) of the IRO. It was completed and returned to the Inland Revenue Department on 2 March 1990. The Taxpayer declared in the return that the date of commencement of business was on 2 February 1990 and that there was no business turnover or receipts for the first six months from the date of commencement.

3. On 1 August 1990, the Revenue issued a letter to the Taxpayer. The relevant content of the letter is extracted as follows:

> 'I shall not call upon your corporation to submit annual returns of profits tax until it commences/recommences to carry on a trade of business in Hong Kong or earn income subject to Hong Kong profits tax.
>
> If your company commences/recommences to carry on a trade or business in Hong Kong or earn income that is chargeable to Hong Kong profits tax you must inform the Commissioner of Inland Revenue. Failure to do this is an offence for which the company can be fined.
>
> Please note that this letter does not authorize you to ignore any return form which may be issued to you under section 51(1) of the IRO from time to time. Thus, if you receive a return form in connection therewith, you must comply with its requirement, failing which legal action may be taken against your corporation.'
>
> During the course of agreeing the statement of facts for this appeal, the Taxpayer had in its letter of 20 April 1995 stated that so far it did not receive the letter of 1 August 1990 mentioned above.

4. On 23 April 1994, the Taxpayer's representative, S H Yeung & Company, certified public accountant wrote a letter to the Revenue requesting for profits tax returns for the years of assessment 1989/90 to 1992/93 for the Taxpayer's completion.

5. On 9 May 1994, the profits tax returns for the years of assessment 1989/90 to 1992/93 were issued to the Taxpayer under section 51(1) of the IRO. They were completed and returned to the Revenue on 12 May 1994. The returned profits for the years of assessment 1989/90 to 1992/93 were $102,276, $1,144,521, $2,023,110 and$3,331,056 respectively.

6. On 29 June 1994, notices of assessment for the years of assessment 1989/90 to 1992/93 were issued to the Taxpayer with assessable profits of $102,276, $1,144,521, $2,031,733 and $3,339,679 respectively. No objection has been lodged by the Taxpayer.

7. On 30 August 1994, the Commissioner gave notice to the Taxpayer in terms of section 82A(4) of the IRO that he proposed to assess the Taxpayer to additional tax in respect of the Taxpayer's failure to comply with the requirement under

section 51(2) of the IRO to notify him in writing that it is chargeable to tax for the years of assessment 1989/90 to 1992/93 not later than four months after the end of the basis period for those years of assessment and that the Taxpayer had the right to submit written representations to him with regard to the proposed assessment of additional tax not later than 30 September 1994.

8. On 27 September 1994, the department received a written representation from the Taxpayer.

9. On 27 October 1994, the Commissioner, after having considered and taken into account the representations, issued notices of assessment and demand for additional tax for the years of assessment 1989/90 to 1992/93 (the assessments) in the sum of $4,000, $47,000, $72,000 and $82,000 respectively.

10. On 21 November 1994, the representative for the Taxpayer gave a notice of appeal to the Clerk to the Board of Review against the assessments.

11. By letters dated 20 and 22 April 1995 addressed to the Revenue, the Taxpayer agreed to the above facts, but requested that the following allegation be included as facts:

> 'that the accountant of the company has tried her effort to obtain tax returns for the years of assessment 1989/90 to 1992/93 from information counter of the Revenue. But the staff of the Revenue replied that no tax returns can be issued from the counter and advised the accountant of the company that she should wait until tax returns generated from computers of Revenue.'

12. By memo dated 6 April 1995 addressed to the Clerk to the Board of Review, the Commissioner stated that the Revenue was unable to agree to include the Taxpayer's allegation in paragraph 11 above as facts.

At the hearing of the appeal, Miss A, accountant in the firm of the representative for the Taxpayer, appeared on behalf of the Taxpayer. Mr B, a director of the Taxpayer, was also present, but did not give evidence. Miss A submitted that the Taxpayer had reasonable excuse of failure to comply with section 51(2) of the IRO, and should not be liable to additional tax; and that even if the Taxpayer was liable to additional tax, the amount of tax was excessive having regard to the circumstances. She elaborated on the following grounds of appeal which were stated in the Taxpayer's notice of appeal of 21 November 1994:

(1) The Taxpayer alleged that it had no intention to conceal profits deliberately, because:

   (a) It did notify the Revenue that the date of first sales was 2 February 1990 in the provisional profits tax return for the year of assessment 1989/90.

(b) It alleged that initiative action was taken when its accountant tried to obtain the tax returns from the information counter of the Revenue several times.

(c) It appointed the representative for the Taxpayer to deal with its taxation affairs, especially to obtain outstanding tax returns for filing.

(2) The Taxpayer alleged that it had no intention to violate the regulations under the IRO, because:

(a) It had complied with all the instructions required by the Revenue (including payment of tax) except for non-compliance under section 51(2) of the IRO, which it considered to be a technical default rather than a serious default.

(b) It alleged that it had reasonable excuse for non-compliance, since it placed substantial reliance on the experience of its accountant, who in turn relied on the representation made by the staff at the information counter of the Revenue.

Miss A submitted that the Revenue should have issued a tax return instead of the letter dated 1 August 1990, because the Taxpayer had already declared in its 1989/90 provisional profits tax return that its first sale was on 2 February 1990; but that it stated its total business turnover for the first six month from commencement of business as 'Nil', and its estimated profit derived therefrom as 'Nil', because its accounting year end was end of December, so that the first set of accounts was closed on 31 December 1989, but the date of first sales was 2 February 1990.

Miss A gave further explanation on the Taxpayer's written grounds of appeal, made comments on the submission of the representative of the Commissioner, and answered questions posed by the Board.

The representative for the Commissioner Mr Ngai See-wah submitted that there was no reasonable excuse for failure to comply with the requirements of a notice given under section 51(2) of the IRO; that the Taxpayer was therefore liable to penalty under section 82A, that the additional tax was correctly imposed; and that the amount of additional tax having regard to the circumstances of the case was not excessive. Mr Ngai referred the Board to the relevant provisions of the IRO, and to the following Board of Review decisions where the Board confirmed penalty imposed for late filing of tax returns:

	Additional Tax Imposed
D33/89, IRBRD, vol 4, 359	37% of tax undercharged
D5/92, IRBRD, vol 7, 84	33% of tax undercharged
D11/93, IRBRD, vol 8, 143	20% of tax undercharged

Mr Ngai Submitted that in these cases, tax returns were issued, estimated notices of assessment and demands for tax were issued, and the returns were submitted to the Revenue a few months late; whereas the present case was far more serious in the degree of lateness, which was in terms of years and months. He noted the dates of the Taxpayer's auditor's reports as: 26 June 1992 for the years of assessment 1989/90 and 1990/91, and 2 December 1993 for the years of assessment 1991/92 and 1992/93. Mr Ngai then addressed the Taxpayer's point that the Taxpayer's accountant allegedly went to the information counter of the Revenue on the second floor several times and was allegedly misinformed each time. Mr Ngai submitted that the Revenue's central enquiry counter was on the first floor and not the second floor, that the normal procedure for staff handling request for tax return would be to give the enquirer a duplicate tax return only if the original one which has been issued was lost, but if the enquirer's company was liable to tax and no tax return has been sent the staff would ask the enquirer to write to the Revenue instead. Mr Ngai tabled at the hearing 33 newspaper advertisements made by the Revenue between 1 July 1991 to 31 March 1995 which reminded businessmen of their obligation to inform the Revenue of tax chargeability and to file tax returns, and indicated that notification of tax chargeability must be made in writing. As to the effect of the Taxpayer's lateness in informing the Revenue of chargeability to tax, Mr Ngai submitted that the Taxpayer should have paid provisional tax for the succeeding year in addition to payment of tax for that year of assessment; in which case the total tax payable for the Taxpayer for the years of assessment 1989/90 to 1992/93 should have been $1,709,841 (being final tax and provisional tax for succeeding years of assessment 1989/90 to 1992/93) payable by April 1994 instead of the much smaller sum of $1,125,398 actually paid by the Taxpayer (that is, addition of $16,875, $188,845, $335,235, and $584,443, being the amounts of tax payable for assessable profits for the years of assessment 1989/90 to 1992/93) payable by 15 August 1994 as was the actual case. Mr Ngai submitted that this was unfair to other taxpayers who discharged their obligations to inform the Revenue of chargeability within the time limit of 4 months after the end of the basis period for that year of assessment and to pay tax on time.

Having heard the parties and having considered all the facts and submissions, the Board finds that the Taxpayer has not discharged the onus under section 68(4) to prove on the balance of probabilities that the assessment to additional tax levied on the Taxpayer under section 82A for the years of assessment 1989/90 to 1992/93 is excessive or incorrect.

We find that the Taxpayer did not inform the Commissioner in writing that it was so chargeable not later than 4 months after the end of the basis period for the years of assessment 1989/90 to 1992/93 under section 51(2) of the IRO, and that notifying the date of first sales as 2 February 1990 in the 1989/90 provisional profits tax return does not discharge the Taxpayer of its obligation under section 51(2), especially since it also made 'Nil' declarations in the same tax return in both the item for stating total business turnover for the first 6 months from the date of commencement and also the item for stating estimated profit derived therefrom, thus not providing any basis to the Revenue for assessment of chargeability for tax. Assuming that the Taxpayer's accountant did try to obtain tax returns from the Revenue's information counter several times, which we do not accept as truth in view of lack of detailed evidence to substantiate such claim, this cannot be treated as being equivalent to informing the Commissioner in writing of its chargeability to tax. Therefore we find that the Taxpayer failed to comply with section 51(2) of the IRO.

In respect of the seriousness of the offence, we do not agree with the Taxpayer's submission in its notice of appeal dated 21 November 1994 that its failure to comply with section 51(2) of the IRO was a technical default and not a serious default such as having an intention to make incorrect return or intention to understate profits, etc. The Commissioner's representative has stated that the additional tax under section 82A was imposed not because the Taxpayer had intention to conceal profits deliberately. Although the Taxpayer made its first sale in February 1990, it waited until April 1994 before writing to the Revenue to request for profits tax returns for completion. We find that the Taxpayer's failure to comply with section 51(2) of the IRO to be a serious matter since a lapse of 4 years during which period profits were made and tax was not paid cannot be treated as a mere technical default.

We also find that the Taxpayer failed to show that it had reasonable excuse in failing to comply with section 51(2). The Taxpayer submitted that it had placed substantial reliance on the experience of its accountant who had been working in a local certified public accountants firm and was a friend of the Taxpayer's director. However, the obligation is placed on the Taxpayer to comply with the IRO, and it is no excuse to shift the blame on its accountant. It was the duty of the Taxpayer to employ staff with adequate knowledge in handling tax affairs or engage a tax representative to do so properly. The Taxpayer then submitted that the Revenue should have known that the Taxpayer had already commenced business in February 1990 and should have issued a tax return instead of the letter of 1 August 1990 (paragraph 3 above). We do not find this to be a reasonable excuse because of the Taxpayer's nil return submitted to the Revenue, the Revenue's assessor is entitled not to issue a tax return to the Taxpayer under section 51(1), but the obligation is placed on to report its chargeability to profits tax under section 51(2). Finally, the Taxpayer submitted that its accountant relied on the representations made by the staff at the information counter of the Revenue on several occasions, that it should wait for the tax returns to be issued from the computer. As stated above, we do not find this allegation to be a fact, and even assuming that this were possible for argument's sake, this does not constitute a reasonable excuse, especially since the Taxpayer would still have passed the 4 months' deadline imposed by section 51(2), because the Taxpayer alleged in its notice of appeal of 21 November 1994 that its accountant went to the Revenue's information counter after the completion of the audited accounts for the years of assessment 1989/90 and 1990/91. As can be seen from the submission by the Commissioner's representative, the Taxpayer's auditor's reports for the years of assessment 1989/90 and 1990/91 were both dated 26 June 1992, whereas the dead-lines for informing the Commissioner in writing of chargeability of tax should be 31 July 1990 and 31 July 1991 respectively. And if the Taxpayer's accountant had done the same for the years of assessments 1991/92 and 1992/93, its auditor's reports for those 2 years were both dated 2 December 1993, whereas the dead-lines should be 31 July 1992 and 31 July 1993 respectively. Therefore we find that the Taxpayer is liable to additional tax under section 82A for the years of assessment 1989/90 to 1992/93.

The Commissioner imposed additional tax in the amount of $4,000 for the year of assessment 1989/90, $47,000 for the year of assessment 1990/91, $72,000 for the year of assessment 1991/92, $82,000 for the year of assessment 1992/93 which came to 24%, 25%, 21%, 14% respectively of the amount of tax undercharged. In a case of this nature, giving full consideration to all the fact and submissions made, we find that the amount of additional tax for the years of assessment 1989/90 to 1992/93 levied against the Taxpayer

under section 82A of the IRO to be well within the normal range of percentages and not excessive having regard to the circumstances. According we order that the appeal be dismissed.