INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D25/03

Penalty tax – sections 51(2), 68(4) and 82A(1) of the Inland Revenue Ordinance ('IRO') – burden on taxpayer to make a return within the statutory period – whether mere oversight or carelessness can constitute 'reasonable excuse' from complying with section 51(2) of the IRO – whether or not the penalty is modest in view of the excessive delay and the amount involved.

Panel: Ronny Tong Ka Wah SC (chairman), Frederick Kan Ka Chong and Vincent Mak Yee Chuen.

Date of hearing: 24 April 2003.
Date of decision: 28 May 2003.

The taxpayer is a limited company. The taxpayer incurred a tax loss for the year of assessment 1997/98 because of a provision of bad debt. On 22 January 1999, the Revenue warned the taxpayer by letter that under section 51(2) of the IRO, if the taxpayer commences or recommences to earn chargeable profits, then the taxpayer must inform the Commissioner within four months after the end of the accounting period. The audited accounts of the taxpayer showed profits in the financial years of 1999 and 2000.

By a letter dated 10 September 2001, some 13 months after the expiration of the four-month period after the end of the accounting year, the taxpayer notified the Revenue in writing and requested a profits tax return. The Commissioner assessed the taxpayer additional tax of $60,000 representing a 9.48% of tax undercharged under section 82A of the IRO.

Held:

1. The burden is on the taxpayer to make a return within the statutory period. The effective operation of Hong Kong's simple tax system demands a high degree of compliance by taxpayers. In this respect, mere oversight or carelessness cannot in any view constitute 'reasonable excuse'. Nor will mere suspicion of the existence of bad debts without sufficient evidence suffice. Such conduct is not conductive to the efficient operation of Hong Kong's tax system nor is it fair to the community at large. It follows that in order to be excused, the taxpayer must show a reasonable explanation supported by credible evidence. The Board found that the taxpayer was not reasonably excused from complying with section 51(2) of the IRO.

2. The Board rejected the allegation of the taxpayer that a further letter was handed to the enquiry counter of the Revenue in September 2001 asking for a profits tax return. The Board rejected this allegation because the letter sent in September 2001 was hardly relevant and by then there had already been a very substantial delay.

3. The penalty is indeed modest in view of the excessive delay and the amount involved. There are no mitigating factors and the penalty can hardly be said to be excessive.

Appeal dismissed.

Lee Kong Chun for the Commissioner of Inland Revenue.
Ma Kam Choi of Messrs K C Ma & Co, Certified Public Accountants, for the taxpayer.

Decision:

Background facts

1. The Taxpayer is a limited company trading in polychemical and resin. It incurred a tax loss for the year of assessment 1997/98. The main reason for the loss was a provision for bad debts of $3,374,806.

2. On 22 January 1999, the Inland Revenue Department ('the Revenue') sent a letter to the Taxpayer excusing the latter from submitting annual profits tax returns. The letter, however, also carried a warning, in line with the requirement of section 51(2) of the IRO in these terms:

> 'If your company commences or recommences to earn chargeable profits, that is, current year profits without regard to any losses brought forward, then your company must inform the Commissioner of Inland Revenue in writing within 4 months after the end of the accounting period. Failure to do so is an offence which may render your company liable to be fined.'

3. The audited accounts of the Taxpayer for the year ending 31 March 2000 ('the Accounts') showed a turnover of $176,193,604 from $93,186,567 in 1999 and a profit of $4,952,478 from $500,492 in the previous year. Taxation was projected at $632,730. The Accounts were approved and signed by the directors of the Taxpayer on 5 October 2000.

4. By a letter dated 10 September 2001, some 13 months after the expiration of the four-month period after the end of the accounting year, the Taxpayer by its tax representatives

(' the Firm') notified the Revenue in writing that there were assessable profits for the year of assessment 1999/2000 and requested a profits tax return.

5. On 6 December 2002, the Commissioner of Inland Revenue (' the Commissioner') assessed the Taxpayer additional tax of $60,000, representing a 9.48% of tax undercharged under section 82A of the IRO. From this assessment, the Taxpayer appealed.

Grounds of appeal

6. The Taxpayer by its officials did not attend the hearing of the appeal. Nor did it call any witnesses. Instead, the appeal was conducted by a Mr Ma of the Firm without giving evidence.

7. Mr Ma raised two points in pursuance of the appeal:

(a) there was no breach of section 51(2) of the IRO;

(b) the amount of additional tax was excessive and unreasonable.

8. In his argument on the first point, he initially alleged that there were justifiable grounds for the Taxpayer not to notify the Commissioner within the four-month time limit laid down in section 51(2) (' the First Allegation'). Later on, when pressed with that allegation, he alleged that in fact the Commissioner was notified within time and certainly earlier than the letter of 10 September 2001 (' the Second Allegation').

The First Allegation

9. We can dispose of the First Allegation fairly quickly. It was alleged that there were substantial bad debts in both the financial years of 1999 and 2000. By that, we suppose Mr Ma was alleging that in fact there were no taxable profits.

10. We have difficulty in understanding this allegation. The Accounts did not show any provision for bad debts nor the amount thereof. Mr Ma himself admitted that he was not instructed there were definitely bad debts nor was he instructed the amount of the alleged bad debts. No evidence in support of the allegation of the existence of bad debts was produced.

11. Furthermore, no objection was raised on the profits tax assessed by the Revenue based on the figures submitted by the Taxpayer.

The law

12. The material part of section 82A(1) of the IRO reads:

> *'(1) Any person who without reasonable excuse –*
>
> *...*
>
> *(e) fails to comply with section 51(2),*
>
> *shall ... be liable to be assessed under this section to additional tax of an amount not exceeding treble the amount of tax which –*
>
> *(i) ...*
>
> *(ii) has been undercharged in consequence of the failure to comply with ... section 51(2), or which would have been undercharged if such failure had not been detected.'*

13. Plainly, the burden is on a taxpayer to make a return within the statutory period. The effective operation of Hong Kong's simple tax system demands a high degree of compliance by taxpayers. In this respect, mere oversight or carelessness cannot in any view constitute 'reasonable excuse'. Nor will mere suspicion of the existence of bad debts without sufficient evidence suffice. Such conduct is not conducive to the efficient operation of our tax system nor is it fair to the community at large. It follows that in order to be excused, the taxpayer must show a reasonable explanation supported by credible evidence.

14. It follows that we have no hesitation in rejecting this allegation and we find that the Taxpayer was not reasonably excused from complying with section 51(2) of the IRO.

The Second Allegation

15. Mr Ma then alleged that in fact there was no breach of section 51(2). He based his argument on a letter dated 26 October 2002 written to the Commissioner as part of the representation made in opposition to the assessment of additional tax.

16. In that letter, he alleged that the Firm had 'issued letter for (*sic*) asking for profits tax returns to [the Revenue's] enquiry counter during October 2000 and January 2001.'

17. It was further alleged in that letter that a further letter was sent in September 2001 asking for a profits tax return but received a reply that no return would be issued.

18. These are very strange allegations. The Revenue has no record of these letters and Mr Ma could produce none. In the letter of 10 September 2001, there was no mention of these previous letters. Nor was there a complaint that no return was issued.

19. When pressed, Mr Ma alleged that what happened was he sent a subordinate to the enquiry counter of the Revenue armed with a letter requesting the issuance of a tax return. It was not the practice of the Revenue to issue tax returns over the counter and the subordinate apparently left without leaving a copy of the letter he was armed with.

20. Mr Ma gave no further elaboration on the alleged letter sent in September 2001 nor the reply the Firm allegedly received. Neither letter was produced.

Application for adjournment

21. After much hesitation, Mr Ma applied for an adjournment generally to enable him to ' locate' his subordinate who he said left the employ of the Firm some time ago. Mr Ma' s request for an adjournment was not based on the ground that he wished to call this person to give evidence. He said ' something in writing' could be produced to show the subordinate did approach the enquiry counter of the Revenue as alleged.

22. The Revenue objected to the application on the ground that it would serve no useful purpose. It was submitted that since no return would normally be issued over the counter, the alleged evidence would be neither here nor there. The crucial fact here is whether a written notice as required under section 51(2) was given to the Commissioner at any time prior to the written notice which the Firm eventually did give on behalf of the Taxpayer on 10 September 2001.

23. We think there is much force in the Revenue' s argument. In any event, we doubt very much a document signed by the subordinate without him giving evidence on oath will clear our hesitation in accepting the version of facts presented by Mr Ma. The fact remains the Revenue was not notified in writing until 10 September 2001. If there was a previous notification, why was it not produced? The fact that the subordinate had left the employ of the Firm has no bearing on the existence of such a letter. Presumably, there would be at least a copy of such a letter, if it did exist, on file.

24. The fact that there might be another letter sent in September 2001 is hardly relevant. By then there had already been a very substantial delay.

25. For these reasons, we dismissed the application for adjournment.

26. In the absence of further evidence, we are not persuaded that the Taxpayer had properly or at all discharged its burden under section 68(4) of the IRO. We dismiss this part of the appeal.

Whether penalty excessive

27. Mr Ma produced no evidence challenging the amount of the additional tax. He can

hardly be blamed. The general tariff in these cases is well known. The amount of the penalty is indeed modest in view of the excessive delay and the amount involved.

28. There are no mitigating factors. In our view, the penalty can hardly be said to be excessive. We also affirm the Commissioner' s assessment in this respect.

29. The appeal is therefore dismissed.