

## INLAND REVENUE BOARD OF REVIEW DECISIONS

### Case No. D25/97

**Penalty tax** – delay in filing profits tax returns – whether penalty tax assessments excessive.

Panel: Robert Wei Wen Nam SC (chairman), Arthur Chan Ka Pui and Peter R Griffiths.

Date of hearing: 21 February 1997.

Date of decision: 28 May 1997.

For the years of assessment 1992/93, 1993/94 and 1994/95, the taxpayer company was late in filing its profits tax returns by 20 months and 24 days, 14 months and 5 days and 3 months and 3 days respectively and was assessed to additional (penalty) tax in the respective sums of \$40,000, \$50,000 and \$30,000, representing 17.40%, 16.12% and 15.37% of tax which would have been undercharged if each of the returns in question had been accepted as correct. There was no appeal against the 1992/93 assessment, and this is an appeal against the 1993/94 and 1994/95 assessments. The taxpayer's case is that the delay in the submission of returns was due to shortage of accounting staff, which was in turn caused by a variety of reasons, such as high staff turnover rates, frequent resignations of accounting staff, difficulties in recruitment, substantial increase in business turnover and heavy workload, removal to an enlarged plant, directors too busy tackling other problems and travelling, accounts being left to skeleton subordinate accounting staff and the implementation of a computerized accounting system which increased workload.

Held:

The explanation for the delay were all factual allegations which have not been proved, and, even assuming that they were all true, they did not amount to reasonable excuses. As for quantum, it is a fact that all three returns were submitted in 1995 within a period of seven months. Each of the two later ones was an improvement in terms of length of delay. In the case of the 1994/95 return, the assessment should strike a balance between showing recognition of the improvement and reminding the taxpayer that a delay of three months and three days is still a substantial non-compliance with the obligations under section 51(1) of the Inland Revenue Ordinance. A sum of \$19,500, representing 10% of the tax which would have been undercharged, would be an appropriate measure. As for the delay in the filing of the 1993/94 return, it was well over a year even though it was an improvement upon the 1992/93 return. The \$50,000 assessment is 16.12% of the tax undercharged, which is about the middle of the normal range of 10% to 20%. It is not excessive and should not be distributed.

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### Appeal dismissed.

Cases referred to:

D61/90, IRBRD, vol 5, 449  
D2/92, IRBRD, vol 7, 58  
D33/89, IRBRD, vol 4, 361  
D11/93, IRBRD, vol 8, 146  
D42/93, IRBRD, vol 8, 321  
D2/90, IRBRD, vol 5, 81

G S Chadha for the Commissioner of Inland Revenue.

Tai Sheung Yan of Messrs Billy Ho and Company for the taxpayer.

### Decision:

### Nature of appeal

1. This is an appeal against the additional tax assessments raised under section 82A of the Inland Revenue Ordinance (the IRO) on a limited company (the Taxpayer) for the years of assessment 1993/94 and 1994/95 for failure to comply with the requirements of a notice given to it under section 51(1) of the IRO, that is, for failure to file profits tax returns for those two years within specified periods of time.

### Facts

2. Particulars of delay in the filing of returns for the years of assessment 1992/93, 1993/94 and 1994/95 are as follows:

Year of assessment	Extended due date	Date filed	Period of delay	Tax under-charged \$	Additional tax \$	Percentage of additional tax on tax undercharged
1992/93	31-7-93	24-4-95	20 months & 24 days	229,755	40,000	17.40%
1993/94	30-7-94	5-10-95	14 months & 5 days	310,039	50,000	16.12%

Percentage of

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<b>Year of assessment</b>	<b>Extended due date</b>	<b>Date filed</b>	<b>Period of delay</b>	<b>Tax under-charged \$</b>	<b>Additional tax \$</b>	<b>additional tax on tax undercharged</b>
1994/95	31-7-95	3-11-95	3 months & 3 days	195,172	30,000	15.37%

3. The Taxpayer was incorporated in Hong Kong on 13 March 1984 and has carried on business as advertising agent, books and periodicals distributors and consultant to newspapers and publications.

4. The Taxpayer closes its accounts annually on 31 December in each year.

5. On 22 November 1995, the Commissioner of Inland Revenue (the CIR) assessed the Taxpayer to additional tax in the sum of \$40,000 for the year of assessment 1992/93. No appeal was made by the Taxpayer to the assessment.

6. On 22 March 1996, the CIR assessed the Taxpayer to additional tax in the sums of \$50,000 and \$30,000 for the years of assessment 1993/94 and 1994/95 respectively. On 22 April 1996, the Taxpayer gave notice of appeal to the Board of Review against the assessments.

### **Grounds of appeal**

7. The Taxpayer's grounds of appeal may be summarised as follows.

7.1 The Taxpayer found it extremely difficult to recruit suitable accounting staff. Besides there were high staff turnover rates and frequent resignations of accounting staff, resulting in disruption in office routine and bottlenecks in accounting records and administration.

7.2 The Taxpayer underwent relocation and reassignment of responsibilities. This accounts for the substantial increase in turnover and heavier workload for the inadequate accounting staff.

7.3 In order to cope with business expansion the Taxpayer removed to an enlarged plant shortly after the year ended 31 December 1994. Renovation and planning took up a substantial part of human resources facilities. Difficulties in hiring staff of all grades forced the directors to operate with a skeleton management and office team. The directors had to concentrate on tackling procurement and distribution problems.

7.4 The directors travelled heavily both locally and outside Hong Kong to canvas clients and reinforce networks. They could not spend more time on handling accounting matters and such duties were left to the skeleton subordinate accounting staff.

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7.5 The installation of a computer and implementation of a computerised accounting system demanded extra manpower. This imposed extra workload resulting in delay in accounts preparation and submission of tax returns for the years in question.

7.6 As a result of the above circumstances, the profits tax returns for the years of assessment 1992/93, 1993/94 and 1994/95 were all submitted late. The 1993/94 and 1994/95 returns are in a much better position than the 1992/93 return. The Taxpayer tried its best to submit the 1994/95 return in time, so it is in the best position. The late submission of all the three returns should be considered the same incident because they are the result of the same unforeseen and uncontrollable circumstances and the returns were all submitted in 1995 within seven months. Since the late submission of the 1992/93 return has already been penalised heavily at a loading of over 17%, the Taxpayer should not be penalised again for the late submission of the 1993/94 and 1994/95 returns. The Taxpayer did not appeal against the assessment for the year of assessment 1992/93 because it was thought that the Commissioner had singled out the 1992/93 return for penalty in order to teach the Taxpayer a lesson and that as the penalty loading of 17% was heavy enough, the other two returns would not be considered again for penalty.

7.7 The Taxpayer did not have the least intention to avoid or delay payment of tax.

7.8 In line with the loading for the year of assessment 1992/93, the Taxpayer should at most be penalised as follows:

Year of Assessment	Penalty Loading	Penalty
1993/94	$17.4\% \times 13/20 = 11.31\%$	\$35,000
1994/95	$17.4\% \times 2/20 = 1.74\%$	\$3,000

### Hearing and parties

8. At the hearing of this appeal, the Taxpayer was represented by Mr Tai, audit manager of Messrs Billy Ho and Company, certified public accountants, while the Commissioner was represented by Mr Chadha, senior assessor. No witness was called.

9. Mr Chadha's written submission referred to the Taxpayer's record in regard to the submission of returns for the years of assessment 1988/89 to 1991/92. Mr Tai pointed out that there was no delay in relation to the years of assessment 1989/90 and 1990/91. As for the years of assessment 1988/89 and 1991/92, he submitted that previous non-compliance should be dealt with in the relevant years of assessment and should not be left pending as a potential aggravating factor for subsequent non-compliance. Mr Chadha explained that the four years' record was only intended as part of the historical background, and that he was not relying on that record to justify the additional tax assessments under appeal. Consequently, we have not taken into account the four years' record in considering the merits of this appeal.

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### Findings and reasons

10. The Taxpayer's case is that the delay in the submission of returns was due to shortage of accounting staff, which in turn was caused by a variety of reasons, such as high staff turnover rates, frequent resignations of accounting staff, difficulties in recruitment, substantial increase in business turnover and heavier workload, removal to an enlarged plant, directors too busy tackling other problems and travelling, accounts being left to skeleton subordinate accounting staff and the implementation of a computerised accounting system which increased workload (see paragraphs 7.1 to 7.5 above).

11. We agree with Mr Chadha when he pointed out that the explanations for the delay were all factual allegations which have not been proved and that, even assuming that they were all true, they did not amount to reasonable excuses. He cited the following cases:

11.1 D61/90, IRBRD, vol 5, 449

*'The excuse that accounting staff were difficult to obtain in 1989 has been put to the Board on many occasions. The Board has consistently stated that it is the duty of a taxpayer to ensure that its accounting records are maintained up-to-date and that the returns required to be made by taxpayers under the Ordinance are made within the time limits specified in the Ordinance. Difficulties in recruiting staff do not excuse taxpayers from fulfilling their statutory obligations.'*

11.2 D2/92, IRBRD, vol 7, 58

*'It is well known that problems can arise when accounts are changed from a manual system to a computer system.'*

11.3 D33/89, IRBRD, vol 4, 361

*'It is the duty of all taxpayers who carry on business in Hong Kong to so regulate their affairs that they are able to comply with their obligations under the Ordinance.'*

11.4 D11/93, IRBRD, vol 8, 146

*'Those who decide that their obligations under the Inland Revenue Ordinance are of a low priority must recognise that the consequence of their action or inaction may lead to very substantial financial penalties being imposed upon them or their company.'*

12. As to quantum, we accept Mr Chadha's submission that absence of an intention to evade or delay payment of tax is not a mitigating factor because no taxpayer should have such intention. We also agree with him when he stated that the normal range of penalties in cases such as the two under appeal would be between 10% and 20% of the tax involved (see

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D42/93, IRBRD, vol 8, 321 and D2/90, IRBRD, vol 5, 81). We cannot accept Mr Tai's contention that all the three returns are the result of the same unforeseen and uncontrollable circumstances (see paragraph 7.6 above) because the circumstances have not been proved. However, it is a fact that all three returns were submitted in 1995 within a period of seven months. Each of the two later ones was an improvement in terms of length of delay (see paragraph 2 above). In the case of the 1994/95 return, the assessment should in our view strike a balance between showing recognition of the improvement and reminding the Taxpayer that a delay of three months and three days is still a substantial non-compliance with the obligations under section 51(1) of the IRO. We think that a sum of \$19,500, representing 10% of the tax which would have been undercharged, would be an appropriate measure. As for the delay in the filing of the 1993/94 return, it was well over a year even though it was an improvement upon the 1992/93 record. The \$50,000 assessment is 16.12% of the tax undercharged, which is about the middle of the normal range of 10% to 20%. In our view, it is not excessive and should not be distributed.

13. It follows that the assessment for the year of assessment 1994/95 should be reduced to \$19,500 and so we direct. Subject to that, this appeal is dismissed and the assessment for the year of assessment 1993/94 is hereby confirmed.