Case No. D26/99

Penalty Tax – taxpayer's return filed late – factors to be taken into account to assess propriety of additional tax being imposed – good track record of submitting returns on time – lack of candour on the part of the taxpayer – mitigating circumstances – sections 82A and 82B(2)(c) of the Inland Revenue Ordinance ('IRO').

Panel: Ronny Wong Fook Hum SC (chairman), Michael Seto Chak Wah and Ronald Tong Wui Tung.

Date of hearing: 24 April 1999.
Date of decision: 17 June 1999.

The taxpayer was incorporated in Hong Kong in 1974 as a travel agency business. It was required, on 1 April 1998, to submit its completed return for the year of assessment 1997/98 within one month. This was not done. On 11 June 1998, the Revenue assessed the taxpayer's profits to be $30,030,000. The return was eventually submitted on 19 July 1998, together with the audited accounts of the taxpayer for the year ended 30 June 1997 which were dated 25 August 1997.

The taxpayer was additionally assessed on 24 July 1998 in relation to actual profits earned. However, by notice dated 19 October 1998 the Commissioner informed the taxpayer of his intention to invoke section 82A of the IRO for the late filing of its return. After representations were made by the taxpayer, by notice dated 19 November 1998, the Commissioner imposed additional tax of $250,000 representing 4.69% of the tax which would have been undercharged if the taxpayer's failure to submit timely return had not been detected.

The taxpayer appealed. Before the Board, the financial controller of the taxpayer admitted that the return had been filed late because, inter alia, its computer system was being overhauled during the relevant period and was only completed in June/July 1998.

Held by the Board, after setting out the relevant principles:

(1) Although there were several mitigating circumstances on the part of the taxpayer which included a good past track record of submitting returns on time and that there was no actual loss of revenue, there were also several aggravating circumstances to record;

(2) It was clear that the audited accounts had been ready since 25 August 1997, therefore, the change of the computer system was not a hindrance to the submission of the return. The overhauling of the computer system had been used as a smokescreen by the taxpayer to conceal its failure to file its return on time;

(3) There was a lack of candour on the part of the taxpayer. Considerable weight would be attached to this important factor by the Board (D59/96, ibid., distinguished) to take into account.

(4) Although the penalty of $250,000 was excessive it would only be reduced to $150,000 in light of the above factors.

Appeal allowed in part.

Cases referred to:

D56/96, IRBRD, vol 12, 1
D59/96, IRBRD, vol 12, 8

Chan Chor Ming for the Commissioner of Inland Revenue.
Taxpayer represented by its financial controller.

Decision:

The background

1. The Taxpayer is a company incorporated in Hong Kong on 14 December 1973. Commencing from 1 April 1974, the Taxpayer carries on a travel agency business with its accounts made up to the 30th of June of each year.

2. On 1 April 1998, the Revenue sent to the Taxpayer a return for the year of assessment 1997/98. The Taxpayer was required to complete and submit the same within 1 month from the date of the Revenue's despatch. The Taxpayer failed to comply with this 1 month period.

3. By notice of assessment dated 11 June 1998, the Revenue (in the absence of the Taxpayer's return) assessed the Taxpayer's profit for year of assessment 1997/98 at $30,030,000 with tax payable thereon at $4,954,950.

4. The Taxpayer submitted its return for the year of assessment 1997/98 on 19 July 1998. The amount of assessable profits disclosed in this return was $32,267,244. Annexed

to the return was the audited accounts of the Taxpayer for the year ended 30 June 1997. The reports of the auditors and the directors forming parts of those accounts were both dated 25 August 1997.

5. By a notice of additional assessment dated 24 July 1998, the Taxpayer was additionally assessed on $2,237,244 being the difference between the actual profit returned ($32,267,244) and the estimated profits ($30,000,000).

6. By notice dated 19 October 1998, the Commissioner informed the Taxpayer of his intention to invoke section 82A of the Inland Revenue Ordinance (the IRO).

7. By letter dated 24 October 1998, the Taxpayer made the following representations:

(a) 'During the period of filing the 1997/98 return, our company was in changeover of the computer system, we faced the shortage of manpower and large volume of work-load. We are sorry about the late filing of the return, please accept our apology.'

(b) 'We have a good records in previous years.'

8. After considering these representations, the Commissioner by notice dated 19 November 1998 imposed additional tax in the sum of $250,000. This amounts to 4.69% of $5,324,095 which is the amount of tax which would have been undercharged if the Taxpayer's failure to submit timely return had not been detected.

9. The Taxpayer appeals against the additional tax so imposed.

The hearing

10. The financial controller of the Taxpayer, gave evidence before us.

(a) She admitted that the Taxpayer was late in relation to its return for the year of assessment 1996/97. She explained that the return for that year was submitted within time but the Taxpayer failed to annex to that return its audited account. The omission was rectified immediately after the Taxpayer's attention was drawn to it.

(b) The Taxpayer commenced planning for its computer change in February 1998. Whilst the change did not affect the Taxpayer's data integrity, the conversion was not finalised until June/July 1998.

(c) She herself was not in Hong Kong 19 June 1998 and 25 August 1998. She therefore could not pay immediate personal attention to this matter.

Our decision

11. Our attention has been drawn to various decisions of this Board. The Taxpayer laid particular emphasis on D56/96, IRBRD, vol 12, 1 and D59/96, IRBRD, vol 12, 8. The following principles can be distilled form those cases:

(a) In deciding the question under section 82B(2)(c) of the IRO whether the amount of additional tax is excessive having regard to the circumstances, the Board must have regard to the actual as opposed to the hypothetical circumstances.

(b) The purpose of enforcing the submission of returns on time is a means to enforce payment of the correct amount of tax on time, not an end in itself.

(c) Section 82A is not and must not be used as a means to generate revenue. Nor should it be used or abused to oppress, harass or bully taxpayers or their tax representatives.

(d) A clear record is a mitigating factor of some importance.

(e) The fact that there is no actual loss of revenue is also a mitigating factor.

(f) The 'punishment' must fit the 'crime'.

12. The delay in this case was 2 months and 9 days.

13. There are the following mitigating circumstances:

(a) The Taxpayer commenced business in January 1974. Apart from the year 1996/97 where there was a delay of 19 days, it has a good track record.

(b) There is no actual loss of revenue. The estimated and additional assessments were paid on due dates.

(c) The Taxpayer did not object to the estimated assessment or the additional assessment. The Revenue has not been burdened by any unwarranted objection.

14. There are the following aggravating circumstances:

(a) The delay in 1996/97 was 19 days. This was followed by the current delay of 2 months and 9 days.

(b) The audited accounts were ready as long ago as 25 August 1997. The change of the company's computer was not a hindrance in the submission of its return.

(c) The computer change was a smokescreen put forward by the Taxpayer to conceal its failure to afford timely submission of return its proper priority.

(d) The financial controller grudgingly conceded that part of the delay was attributable to her personal convenience.

15. We attach considerable weight to the lack of candour on the part of the Taxpayer. This is an important factor which distinguishes the present case from D59/96.

16. In all the circumstances, we are of the view that the penalty of $250,000 is excessive. We allow the appeal but would only reduce the assessment to $150,000.