

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D36/00

Penalty tax – incorrect returns – basis of assessment.

Panel: Ronny Wong Fook Hum SC (chairman), Cheung Wai Hing and David Lam Tai Wai.

Date of hearing: 5 June 2000.

Date of decision: 12 July 2000.

In about July 1994, the Revenue investigated into the tax affairs of the taxpayer. Finally a proposal for settlement was confirmed. By notice dated 15 July 1999, the Commissioner of Inland Revenue imposed additional tax on the basis of 150% of the amount of the tax undercharged against the taxpayer.

Held:

It is well established that ignorance, illiteracy and inability to comprehend one's obligations do not constitute a reasonable excuse for failing to comply with one's obligations under the Inland Revenue Ordinance ('IRO'). Nor is it a reasonable excuse to assert that compliance with the obligations was delegated to one's subordinates. The Board found that the taxpayer has no reasonable excuse for his incorrect returns.

The Board did not find any error in principle for the Revenue to assess the additional tax on the basis of 150% of the amount of the tax undercharged.

Appeal dismissed.

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Tse Kin Chuen for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

Background

1. This is the Taxpayer's appeal against additional tax assessments imposed on him for the years of assessment 1987/88 to 1992/93.
2. The Taxpayer carried on a construction business in the name of Company A. Company A had a building office licence which gave Company A entitlement to bid for private but not for Government building contracts. In relation to Government building contracts, Company A acted as sub-contractors of the registered main contractors.
3. In about July 1994, the Revenue commenced investigation into the tax affairs of the Taxpayer. During an interview held on 13 July 1994, the Taxpayer was shown the profits tax returns of Company A for the years of assessment 1988/99 to 1991/92. The Taxpayer indicated that he could not confirm the accuracy of those returns until after verification with his main contractors.
4. By letter dated 12 August 1994, the Revenue asked the Taxpayer to submit for its consideration particulars of his personal assets and information in relation to his businesses.
5. The Taxpayer was further interviewed on 17 March 1995 in the presence of his professional adviser. The Taxpayer was reminded that he failed to supply details of assets and liabilities and books of account of Company A and was urged to co-operate with the Revenue by submission of such information.
6. Company A ceased business in about June 1996.
7. By letter dated 15 August 1997, the Taxpayer's attention was drawn to the sum of \$1,647,000 which he received from Company B in the year of assessment 1987/88 and the sum of \$4,869,178 which he received from Company C in the year of assessment 1990/91. The Taxpayer was asked to explain why these two sums were omitted in his previous returns.
8. The Taxpayer attended a further meeting with officers of the Revenue on 26 March 1999. The Taxpayer confirmed a proposal for settlement as follows :

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Year of assessment	Assessable profits/(loss) \$	Reported profits/(loss) \$	Additional assessable profits \$
1987/88	1,636,565	(12,535)	1,649,100
1988/89	16,038	(154,148)	170,186
1989/90	1,434,147	129,560	1,304,587
1990/91	4,672,159	(444,105)	5,116,264
1991/92	356,131	356,131	0
1992/93	978,573	785,091	193,482

9. The Taxpayer was warned by officers of the Revenue ‘ that the proposal for settlement would be subject to senior officers’ approval and there would be penalty and the maximum amount would be 3 times the tax undercharged.’

10. The Taxpayer confirmed the notes of the 26 March 1999 interview on 10 May 1999.

11. By notices dated 15 July 1999, the Commissioner of Inland Revenue imposed the additional tax appealed against.

12. The relationship between the additional tax and the profits understated is as follows :

Year of assessment	Assessable profits/(loss) \$	Reported profits/(loss) \$	Additional assessable profits \$	Tax undercharged \$	Additional tax \$	Relationship between additional tax and tax undercharged
1987/88	1,636,565	(12,535)	1,649,100	270,033	405,000	150%
1988/89	16,038	(154,148)	170,186	2,485	3,000	121%
1989/90	1,434,147	129,560	1,304,587	215,122	322,000	150%
1990/91	4,672,159	(444,105)	5,116,264	700,823	1,051,000	150%
1991/92	356,131	356,131	0	53,419	80,000	150%
1992/93	978,573	785,091	193,482	45,906	69,000	150%
				1,287,788	1,930,000	

Hearing before us

13. The Taxpayer elected not to give sworn testimony but to give a statement before us. He told us that he started off in 1985 to 1989 with projects valued between two to three million dollars. Business prospered. By 1989 to 1990 he was handling projects of about twenty million dollars. He devoted his entire attention to his projects. He delegated to his accountant the task of maintaining his accounts. He has no idea how various entries were made. His business contracted after commencement of investigation by the Revenue. He decided to close down his business in

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1996. His mother is now 94 and his son is 4½. He and his wife each holds a job. Their financial commitments are heavy. He has to pay mortgage instalments in respect of his home. He had no intention to defraud the Revenue. The additional tax is a severe burden on his family.

14. The Revenue submitted that the additional tax imposed is reasonable in the circumstances bearing in mind the degree of co-operation on the part of the Taxpayer; the amount short reported each year; the reasons leading to such omission and time when the Taxpayer ought to have discharged his liability had there been no understatement of his earnings.

Our decision

15. It is well established that ignorance, illiteracy and inability to comprehend one's obligations do not constitute a reasonable excuse for failing to comply with one's obligations under the Inland Revenue Ordinance. Nor is it a reasonable excuse to assert that compliance with those obligations was delegated to one's subordinates. The Taxpayer has no reasonable excuse for his incorrect returns.

16. As far as the amount of additional tax is concerned, the starting point must be the settlement between the Taxpayer and the Revenue which he confirmed on 10 May 1999. The Taxpayer made no challenge before us of the substantial additional assessable profits of \$8,433,619. It took the Revenue five years in order to arrive at this position. The correspondence indicates that the Taxpayer was not active in his co-operation. In these circumstances, we do not detect any error in principle for the Revenue to conclude that additional tax should be assessed on the basis of 150% of the amount of tax undercharged, giving due allowance to the year of assessment 1988/89 bearing in mind that the tax undercharged that year was only \$2,485.

17. For these reasons, we dismiss the Taxpayer's appeal.