

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D5/89

Penalty assessment – whether penalty excessive — s 82A of the Inland Revenue Ordinance.

Panel: William Turnbull (chairman), Gordon M Macwhinnie and Lincoln Yung Chu Kuen.

Date of hearing: 27 January 1989.

Date of decision: 11 April 1989.

The taxpayer carried on business as an unlicensed hawker. Over the course of 15 years, he did not notify the IRD of his liability to profits tax and did not submit any returns. He thought that, because his business was illegal and therefore not registered under the Business Registration Ordinance, he was not obliged to pay profits tax.

Upon discovering his existence, the IRD issued him with profits tax returns, but the taxpayer understated his taxable profits in those returns by an average of 44%. Finally, the taxpayer agreed to assessments based on an assets betterment statement.

The Commissioner assessed the taxpayer to penalties equal to an average of 43% of the maxima permitted. The taxpayer appealed.

Held:

The penalties were not excessive.

Appeal dismissed.

Raymond Ng for the Commissioner of Inland Revenue.

Taxpayer in person.

Decision:

This is an appeal by a Taxpayer against the quantum of certain additional tax assessments imposed on him by way of penalty under section 82A of the Inland Revenue Ordinance.

The facts are as follows:

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1. The Taxpayer was an unlicensed hawkker who carried on a cooked food stall business in partnership with his mother-in-law. The business commenced trading in 1970 and ceased in 1984.
2. The cooked food stall sold noodles, sandwiches and coffee and was not licensed by the Urban Services Department. Sometime before the Taxpayer closed the cooked food stall, he learned that the Urban Services Department was due to close it down. He purchased a shop so that he could continue his cooked food business and, when the Urban Services Department closed his unlicensed stall, he opened a new cooked food business at the shop.
3. The Business Registration Ordinance exempted licensed hawkkers from the requirement to be registered. Because the Taxpayer was not licensed by the Urban Services Department, the exemption from the provisions of the Business Registration Ordinance did not extend to the Taxpayer.
4. After the unlicensed food stall had been closed, the Inland Revenue Department made enquiries into the affairs of the Taxpayer and found out about the unlicensed and unregistered business which he had been conducting since 1970.
5. On 31 January 1985, profits tax returns for the years of assessment 1978/79 to 1983/84 inclusive were issued to the Taxpayer in respect of the unlicensed food stall business.
6. On 9 April 1985, the profits tax returns with supporting profit and loss accounts were returned by the Taxpayer disclosing the following profits:

| <u>Year of Assessment</u> | <u>Profits Returned</u> |
|---------------------------|-------------------------|
| | \$ |
| 1978/79 | 155,350 |
| 1979/80 | 169,160 |
| 1980/81 | 176,515 |
| 1981/82 | 192,810 |
| 1982/83 | 201,150 |
| 1983/84 | 176,300 |

7. The Inland Revenue Department was of the opinion that the returned profits were not sufficient to finance the acquisition of properties owned by the Taxpayer and made further enquiries.
8. In the course of the enquiries, it became known that the Taxpayer had not kept any accounts or records and that the profits as set out in the tax returns filed by him might not be correct. This was admitted by the Taxpayer and the Inland

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Revenue Department embarked upon the assets betterment approach to determine the Taxpayer's liability to tax.

9. On 8 June 1987, the Taxpayer agreed with the assessor to total additional assessable profits of \$850,000 for the years of assessment 1978/79 to 1983/84 as follows:

| <u>Year of Assessment</u> | <u>Profit per Return</u> \$ | <u>Agreed additional Profits</u> \$ | <u>Total Revised Assessable Profits</u> \$ |
|---------------------------|--------------------------------|--|---|
| 1978/79 | 155,350 | 150,000 | 305,350 |
| 1979/80 | 169,160 | 150,000 | 319,160 |
| 1980/81 | 176,515 | 150,000 | 326,515 |
| 1981/82 | 192,810 | 150,000 | 342,810 |
| 1982/83 | 201,150 | 150,000 | 351,150 |
| 1983/84 | <u>176,300</u> | <u>100,000</u> | <u>276,300</u> |
| | <u>\$1,071,285</u> | <u>\$850,000</u> | <u>\$1,921,285</u> |

On 16 July 1987, revised profits tax assessments for the years in question were duly issued by the assessor.

10. On 27 August 1987, the Commissioner of Inland Revenue gave notice to the Taxpayer that he proposed to assess additional tax by way of penalty under section 82A in respect of the failure by the Taxpayer to inform the Commissioner that he was chargeable to tax for the years of assessment 1978/79 to 1983/84 inclusive.
11. After taking into account representative made by the Taxpayer, the Commissioner on 11 September 1987 imposed the following additional tax by way of penalty under section 82A:

| <u>Year of Assessment</u> | <u>Tax Undercharged</u> \$ | <u>Section 82A Penalty Tax</u> \$ | <u>Percentage of Penalty to Tax Undercharged</u> \$ |
|---------------------------|-------------------------------|--------------------------------------|--|
| 1978/79 | 45,802 | 61,800 | 135% |
| 1979/80 | 47,874 | 64,600 | 135% |
| 1980/81 | 48,135 | 65,000 | 135% |
| 1981/82 | 47,577 | 62,600 | 132% |
| 1982/83 | 49,162 | 60,600 | 123% |
| 1983/84 | <u>31,450</u> | <u>36,300</u> | <u>115%</u> |

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\$270,000

\$350,900

130%

12. On 7 October 1987, the Taxpayer appealed against these penalty tax assessments.

Taxpayer's submissions

At the hearing of the appeal, the Taxpayer appeared in person and submitted that the penalties were excessive.

He said that he had operated his food stall for 15 years and that, when the assessor approached him and asked him where he had obtained his moneys for the properties which he owned, he honestly told the assessor that he had obtained the moneys from the unlicensed food stall business which he had been operating. He said that, being a hawker, he did not know that he had to pay tax but, when the Inland Revenue Department asked him, he honestly told them everything he knew. He said that he used the profits which he made from the business to buy gold and then sold the gold afterwards to make profits, and that he could not substantiate the gold transactions because he did not have any receipts. He said that he informed the Inland Revenue Department that he had earned a total profit of over \$1,000,000 in the last six years that he had been operating the business. He said that he had only received form 3 education and knew nothing about taxation. He stressed that, after the Inland Revenue Department has started making enquiries, he did not attempt to conceal anything or hide the truth. He said that, after he had started his new business in the shop which he bought, he had registered the business because he knew that it was necessary to pay tax. He maintained that he thought that, because the cooked food stall was unlicensed, he therefore did not have to register it as a business and was not subject to the provisions of the Inland Revenue Ordinance.

Commissioner's submissions

The representative for the Commissioner pointed out that ignorance of the law was no excuse for not paying tax. He pointed out that, though the Taxpayer had made disclosure of the fact that he had made profits, he did not voluntarily disclose this but only after enquiries had been made by the Inland Revenue Department. Furthermore, he pointed out that, in the course of the enquiries, the Taxpayer had filed tax returns which substantially under-declared the amount of his taxable profits as eventually agreed.

Decision

Having carefully considered all of the facts before the Board and the submissions made by the Taxpayer both in the course of the hearing and in writing prior to the hearing, this Board takes a serious view of this case and confirms the amount of the penalties as imposed by the Commissioner.

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The amount of the penalties are large and exceed the norm of 100% of the tax undercharged, but we do not find the penalties to be excessive. In the course of the Taxpayer's submission, he stated that he knew when he opened his new business in the shop which he bought that he must register under the Business Registration Ordinance and pay tax. Apparently he thought, not unreasonably, that he did not have to register as a business under the Business Registration Ordinance when he was carrying on an unlicensed cooked food stall. We say 'not unreasonably' because, in the Taxpayer's mind, he may not have understood the distinction between a licensed and an unlicensed cooked food stall. Indeed, it would not be possible for the law to provide that what is in reality an illegal business need not be registered under the Business Registration Ordinance because this would give de facto recognition to something which is illegal. However, the fact that the Taxpayer may have ignored the licensing laws and regulations of the Urban Services Department and misunderstood the law as to business registration does not entitle him to ignore the Inland Revenue Ordinance. The legislature, in its wisdom, has provided for very heavy penalties of up to three times the amount of the tax undercharged to protect the public purse against people who seek to ignore their obligations and not pay tax. Everyone in Hong Kong who carried on business for their own account must or should know that the profits which they make are subject to tax. This applies to all businesses and not just to licensed businesses. The fact that the Taxpayer chose to ignore his obligations in relation to the Urban Services Department does not mean that he can likewise ignore his obligations to the Inland Revenue Department.

As stated, in all of the circumstances of this case we do not find the penalties imposed excessive. Accordingly we dismiss this appeal and confirm the section 82A penalty tax assessments which are the subject matter of this appeal.