

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D59/01

Penalty tax – agreement on income tax undercharged – the taxpayer not in possession of the necessary books and accounts – sections 51(2), 68(4) and 82A of the Inland Revenue Ordinance (‘IRO’).

Panel: Patrick Fung Pak Tung SC (chairman), Charles Chiu Chung Yee and Patrick Ho Pak Tai.

Date of hearing: 23 March 2001.

Date of decision: 27 July 2001.

The taxpayer and his wife were the two directors of Company C which carried on the business of second-hand cars. In 1991, the taxpayer acquired Company G and took in new partners. During the relevant period, the taxpayer was a director of both companies which carried on the same kind of business at the same address. In April 1994, partners of the taxpayer decided to sell their shares in Company G to the taxpayer and his wife. Consequently the business of Company G was transferred to Company C to be carried on by that company.

Subsequently the taxpayer was queried by the Revenue regarding the accounts of his business. After a number of interviews between the Revenue and the taxpayer, agreement was arrived at between the two sides about the particulars of additional assessable income on which income tax was payable. The taxpayer signed a document dated 15 August 2000 confirming the agreement. It was stated in paragraph 3 of the document that ‘[the taxpayer] understand that acceptance of the abovementioned assessable income does not conclude the whole matter and that the case will be put up to the Commissioner or Deputy Commissioner for consideration of penal actions’.

Subsequently, the Commissioner gave notice under section 82A(4) of the IRO that he was of the opinion that the taxpayer had, without reasonable excuse, failed to inform the Commissioner in writing that he was chargeable to tax for the particular years and that the taxpayer was liable to be assessed to additional tax. Consequently, the Commissioner issued the Notices of Assessment. The additional tax assessed amounts to 107% of the total amount of tax undercharged for the particular years.

The taxpayer’s case was that at the material time, the accounts of his business were handled by his partner and the accountant of the company. As a result of the breakdown of the partnership, he was no longer able to obtain the necessary record and could only answer the queries raised by the Inland Revenue Department (‘IRD’) from recollection. He had no intention

INLAND REVENUE BOARD OF REVIEW DECISIONS

of cheating the IRD. He signed the document dated 15 August 2000 only because he was under great pressure and he only learnt subsequently that he would be subject to an assessment for additional tax.

Held:

1. The taxpayer cannot resile from the document dated 15 August 2000 which he signed because in paragraph 3 thereof he plainly acknowledged that he understood that acceptance by him of the particulars of the assessable income would not conclude the whole matter and that he might be subject to an imposition of additional income tax.
2. It is well established that illiteracy and lack of knowledge is no excuse, nor is it an excuse for a taxpayer to say that he is unable to keep proper records and accounts and that he co-operated with the IRD when being investigated.
3. The Board does not think that additional tax charged on average at 107% of the tax underpaid is excessive. It is well established that the starting point for assessing penalty is 100% of the tax underpaid.

Appeal dismissed.

Cases referred to:

D34/88, IRBRD, vol 3, 336
D81/97, IRBRD, vol 12, 475
D52/93, IRBRD, vol 8, 372

Tsoi Chi Yi for the Commissioner of Inland Revenue.
Taxpayer in person.

Decision:

1. This is an appeal by the Taxpayer against the issue by the Commissioner of four notices of assessment and demand for additional tax all dated 14 December 2000 (‘the Notices of Assessment’) pursuant to section 82A of the IRO.

INLAND REVENUE BOARD OF REVIEW DECISIONS

2. The Notices of Assessment demanded payment of additional tax by the Taxpayer for the relevant years of assessment as follows:

	\$
(i) 1991/92	22,000
(ii) 1992/93	98,000
(iii) 1993/94	106,000
(iv) 1994/95	<u>15,000</u>
	<u>241,000</u>

The relevant facts

3. In August 1986, the Taxpayer started his sole proprietorship business in dealing in second-hand cars under the name of ' Company A' . On 11 April 1987, the Taxpayer and his wife, Madam B, acquired a limited company by the name of ' Company C' . They each owned 50% of the company and they injected the business carried on in the name of Company A into the company.

4. In 1991, the Taxpayer and Madam B decided to take in partners to their business. The partners were a Mr D and a Mr E. The Taxpayer and Mr D acquired another company by the name of ' Company F . On 29 August 1991 they changed the name of that company into ' Company G' . The Taxpayer held 65% of the shares in Company G. Out of the 65%, 30% was, however, held by the Taxpayer for Mr E.

5. During the relevant period, Company C and Company G carried on the same kind of business at the same address.

6. The Taxpayer was a director of both Company C and Company G and was responsible for the day-to-day business of the same. He, however, did not make any salaries tax return to the Commissioner in respect of his positions in the two companies at the material time, nor did Madam B.

7. In April 1994, as a result of the downturn in business and problems arising out of the partnership between the Taxpayer and Mr D and Mr E, Mr D and Mr E decided to sell their shares in Company G to the Taxpayer and his wife. Consequently, the business of Company G was transferred to Company C to be carried on by that company.

8. Subsequently, the Taxpayer was queried by officials in the IRD regarding the accounts of his business. He provided some but not all of the information requested.

9. Madam B was also subject to an inquiry by the IRD regarding her income and assets.

INLAND REVENUE BOARD OF REVIEW DECISIONS

10. After the investigation had been completed, the IRD found the position regarding the Taxpayer and Madam B to be as follows:

Year of assessment	Assessable income before investigation	Assessable income after investigation	Assessable income not reported	Amount of income tax underpaid by the Taxpayer	Amount of income tax underpaid by Madam B	Total amount of income tax underpaid by the Taxpayer and Madam B
	\$	\$	\$	\$	\$	\$
1989/90	0	10,000	10,000	-	-	-
1990/91	0	20,000	20,000	-	-	-
1991/92	0	120,000	120,000	10,350	9,476	19,826
1992/93	0	550,000	550,000	82,500	7,251	89,751
1993/94	0	650,000	650,000	97,500	3,113	100,613
1994/95	<u>0</u>	<u>250,000</u>	<u>250,000</u>	<u>14,600</u>	<u>100</u>	<u>14,700</u>
	<u>0</u>	<u>1,600,000</u>	<u>1,600,000</u>	<u>204,950</u>	<u>19,940</u>	<u>224,890</u>

11. After a number of interviews between the officials of the IRD and the Taxpayer and Madam B, agreement was finally arrived at between the two sides about the particulars of the additional assessable income on which income tax was payable. The Taxpayer signed a form dated 15 August 2000 containing words and particulars (in English) which read as follows:

‘ 1. I hereby agree that my assessable income be computed as follows:

Year of assessment	Assessable income	Income already reported/assessed	Additional assessable income
	\$	\$	\$
1989/90	10,000	0	10,000
1990/91	20,000	0	20,000
1991/92	120,000	0	120,000
1992/93	550,000	0	550,000
1993/94	650,000	0	650,000

2. I also agree to accept the following revised assessable/additional assessable income in settlement of the objections against the previous assessments:

Year of assessment	Revised assessable income	Revised additional assessable income
	\$	\$
1989/90	10,000	
1990/91	20,000	

INLAND REVENUE BOARD OF REVIEW DECISIONS

1991/92	120,000
1992/93	550,000
1993/94	650,000

3. I also understand that acceptance of the abovementioned assessable income does not conclude the whole matter and that the case will be put up to the Commissioner or Deputy Commissioner for consideration of penal actions under Part XIV of the Inland Revenue Ordinance, which include prosecution, compounding or imposition of additional tax. If additional tax is imposed, the maximum amount could be treble the amount of the tax undercharged.’

12. By a letter dated 19 October 2000 addressed to the Taxpayer, the Commissioner gave notice under section 82A(4) of the IRO that he was of the opinion that the Taxpayer had, without reasonable excuse, failed to inform the Commissioner in writing that he was chargeable to tax for the years of assessment between 1991/92 and 1994/95 within the period prescribed under section 51(2) of the IRO and that the Taxpayer was liable to be assessed under section 82A of the IRO to additional tax of an amount not exceeding treble the amount stated in the notice, namely, \$224,890. The Commissioner further informed the Taxpayer that he proposed to assess additional tax in respect of the said failure and that the Taxpayer had the right to submit written representations to him.

13. Consequently, on 14 December 2000 the Commissioner issued the Notices of Assessment.

14. The additional tax assessed under section 82A of the IRO for the four relevant years of assessment on average amounts to 107% of the total amount of tax undercharged for those years as particularised below:

Year of assessment	Amount of tax underpaid	Additional tax assessed under section 82A	Percentage of additional tax assessed under section 82A in relation to amount of tax undercharged
	\$	\$	%
1991/92	19,826	22,000	110
1992/93	89,751	98,000	109
1993/94	100,613	106,000	105
1994/95	<u>14,700</u>	<u>15,000</u>	102
	<u>224,890</u>	<u>241,000</u>	107

The case of the Taxpayer

INLAND REVENUE BOARD OF REVIEW DECISIONS

15. The Taxpayer gave evidence on affirmation. He made it plain that he was not trying to re-open the assessment for the additional tax by way of challenging the calculation, because he did not know accounts and he was not in possession of the necessary books and accounts to enable him to do so. He said that at the material time, the accounts of his business were handled by Mr E and the accountant of the company. As a result of the breakdown of the partnership, he was no longer able to obtain the necessary record and could only answer the queries raised by the IRD from recollection. He had no intention of cheating the IRD. He signed the document dated 15 August 2000 only because he was under great pressure and he only learnt subsequently that he would be subject to an assessment for additional tax. He further made the point that as early as in 1994, he had been asked by the IRD to deposit a sum of \$100,000 and that the same should have been taken into account by the Commissioner in assessing any penalty.

16. In the course of giving evidence, the Taxpayer became quite emotional at times. At one point, he even broke down.

Conclusion

17. We tend to believe that the Taxpayer was sincere and truthful in giving his evidence. We appreciate that the business for second-hand car dealers has not been good since what happened in China on 4 June 1989 and at present because of the economic recession. We have no doubt that the Taxpayer and Madam B have been under considerable pressure as a result of the downturn in business, the breakup of the partnership and the investigation by the IRD. Nevertheless, we have to approach this matter in accordance with established legal principles.

18. First of all, we do not think that the Taxpayer can resile from the document dated 15 August 2000 which he signed because in paragraph 3 thereof he plainly acknowledged that he understood that acceptance by him of the particulars of the assessable income would not conclude the whole matter and that he might be subject to an imposition of additional income tax.

19. Secondly, we are of the view that none of the reasons put forward by the Taxpayer constitutes a valid reason for our interfering with the decision of the Commissioner resulting in the issue of the Notices of Assessment. Furthermore, we do not think that additional tax charged on average at 107% of the tax underpaid is excessive.

20. It is well established that the starting point for assessing penalty is 100% of the tax underpaid. See, for example, Board of Review Decisions D34/88, IRBRD, vol 3, 336 and D81/97, IRBRD, vol 12, 475.

21. It is also well established that illiteracy and lack of knowledge is no excuse, nor is it an excuse for a taxpayer to say that he is unable to keep proper records and accounts and that he co-operated with the IRD when being investigated. See, for example, Board of Review Decisions D52/93, IRBRD, vol 8, 372 and D34/88, IRBRD, vol 3, 336.

INLAND REVENUE BOARD OF REVIEW DECISIONS

22. As regards the sum of \$100,000 deposited with the IRD in 1994 (actually by Company C), it appears that by direction of that company given on 9 October 2000, the same has been utilised to satisfy part of the tax payable by the Taxpayer.

23. Section 68(4) of the IRO provides that on appeal the onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.

24. In all the circumstances, we are of the view that the Taxpayer has not satisfied such onus upon him.

25. In the circumstances, despite the fact that we have much sympathy for the Taxpayer, we have no alternative but to dismiss his appeal.