Case No. D67/03

Penalty tax – whether or not reasonable excuse for filing late returns – penalty tax was assessed regardless of whether tax was assessed and duly paid under estimated assessments raised on the appellant – penalty tax need not be restricted to compensation or commercial restitution for late payment – whether or not appellant's ability to pay penalty tax is relevant to the level of penalty assessed – whether or not 14% is well within the norm of penalty cases for persistent delays in lodging profits tax returns – whether or not good faith of appellant by submitting fairly accurate management accounts to the assessor within ten days of the due date for filing profits tax returns before any estimated assessment was issued by the assessor is a mitigating circumstance.

Panel: Andrew J Halkyard (chairman), Krishnan Arjunan and Douglas C Oxley.

Date of hearing: 17 September 2003.
Date of decision: 15 October 2003.

The appellant filed its profits tax returns later than the due date. The periods of delay were 127, 117 and 42 days respectively for the years of assessment 1999/2000, 2000/01 and 2001/02. The Commissioner imposed penalty tax and the total penalty tax assessed represented 14.64% of the tax that would have been undercharged if the appellant's failure to file its profits tax returns in time had not been detected.

The appellant argued that penalty tax assessments were excessive because there was no underpayment but just late payment and the appellant was prepared to pay interest for the late payment. Secondly, the appellant was currently in difficult financial straits and could not afford to pay the assessed penalty tax. Thirdly, the appellant cooperated with the Inland Revenue Department ('IRD').

Held:

1. The appellant clearly has no reasonable excuse for filing late returns. All previous cases proceeded on the basis that tax has or would have been undercharged within the terms of section 82A as a result of the late filing of profits tax returns, regardless of whether tax was assessed and duly paid under estimated assessments raised on the taxpayer. It is also clear that penalty tax in these cases need not be restricted to compensation or commercial restitution for late payment. Speaking very generally, the trend of these cases shows that an appropriate level of penalty tax for late filing

is 10% (for ' normal' cases to 20% for more egregious cases) (D53/88, IRBRD, vol 4, 10; D11/93, IRBRD, vol 8, 143 and D125/98, IRBRD, vol 13, 574 followed).

2. In relation to the appellant's ability to pay the penalty tax assessed, this is a matter for the appellant to discuss with the Collection Section of the IRD to see whether payment by instalments, or some other payment option, is appropriate in its circumstances. This consideration should not affect the level of penalty assessed in earlier years of assessment. This is a matter that should be judged on its own merits relevant to each particular year of assessment for which penalty tax is raised.

3. The Board agrees that the level of penalty tax assessed for each year of assessment in this case (around 14%) is well within the norm of penalty cases for persistent delays in lodging profits tax returns. The Board agrees that the Board should look at the year of assessment 1999/2000 separately from the succeeding years of assessment and pay particular attention to the fact that the appellant showed good faith by submitting fairly accurate management accounts to the assessor within ten days of the due date for filing its profits tax return before any estimated assessment was issued by the assessor and apparently without prompting by the assessor. This fact deserves a greater discount than that apparently accorded by the Commissioner. The Board has focused on this factor as a mitigating circumstance.

4. On the facts found, and the circumstances referred to above, the Board decided to reduce the penalty tax assessment for the year of assessment 1999/2000 from 14.93% to approximately 10% of the tax that would have been undercharged if the appellant's delay in filing its profits tax return had not been detected.

Appeal allowed in part.

Cases referred to:

D53/88, IRBRD, vol 4, 10
D11/93, IRBRD, vol 8, 143
D125/98, IRBRD, vol 13, 574

Garry Laird for the Commissioner of Inland Revenue.
Taxpayer represented by its accountant.

Decision:

1. This is an appeal under section 82B of the Inland Revenue Ordinance against the additional or penalty tax assessments raised on the Appellant under section 82A for the years of assessment 1999/2000 to 2001/02 inclusive.

The facts

2. The agreed facts, which we so find, are set out in paragraphs 1 to 26 inclusive of a document produced to us by the IRD entitled 'Statement of Facts'. For convenience, we summarise below the key facts.

(a) For each of the years of assessment under appeal the Appellant filed its profits tax returns later than the due date (the due date being 15 November for each year of assessment). The periods of delay were 127 days (1999/2000), 117 days (2000/01) and 42 days (2001/02).

(b) As a result of those delays, the Commissioner imposed penalty tax under section 82A in the following amounts: $260,000 (1999/2000), $190,000 (2000/01) and $150,000 (2001/02). The total penalty tax assessed ($600,000) represents 14.64% of the tax that would have been undercharged if the Appellant's failure to file its profits tax returns in time had not been detected.

The hearing before us

3. The Appellant did not adduce any evidence before us. Instead, the Appellant's representative (its accountant, Mr A) argued that the penalty tax assessments were excessive in all the circumstances because:

(a) There was no underpayment of tax, just late payment. In this regard, Mr A noted that the Appellant was prepared to pay the IRD an appropriate amount of interest for late payment.

(b) The Appellant was currently in difficult financial straits and could not afford to pay the assessed penalty tax.

(c) The Board of Review should take into account the fact that the Appellant co-operated with the IRD. In this regard, Mr A particularly noted that for the first year of assessment (1999/2000) the Appellant lodged a draft management

profit and loss account with the assessor on 25 November 2000, a date very close to the 15 November date for filing its return, and that the profits disclosed in this account ($10,419,993) approximated the profits ultimately assessed for that year of assessment ($10,887,629). Mr A also noted that for the second year of assessment (2000/01) the Appellant signed a compound offer to pay an amount of $3,000 to the Commissioner when requested to do so.[1]

Analysis

4. The Appellant clearly has no reasonable excuse for filing late returns. Previous Board of Review decisions illustrate this conclusion, including: D53/88, IRBRD, vol 4, 10 (problems in retaining accounting personnel leading to delay in lodging a return was not a reasonable excuse; the fact that estimated assessments were raised and paid was irrelevant); D11/93, IRBRD, vol 8, 143 (the fact that the assessor has raised an estimated assessment in the absence of a return does not mitigate the taxpayer's delay in filing a return; this fact is immaterial when assessing the quantum of additional tax); D125/98, IRBRD, vol 13, 574 (intention to defraud or delay payment of tax is an aggravating factor; its absence is not a mitigating factor; the fact of improved compliance does not itself constitute a reasonable excuse).

5. All these cases proceeded on the basis that tax has or would have been undercharged within the terms of section 82A as a result of the late filing of profits tax returns, regardless of whether tax was assessed and duly paid under estimated assessments raised on the taxpayer. It is also clear that penalty tax in these cases need not be restricted to compensation or commercial restitution for late payment. Speaking very generally, the trend of these cases shows that an appropriate level of penalty tax for late filing is 10% (for 'normal' cases to 20% for more egregious cases). We agree with those decisions and there is no reason for us to depart from them. This answers Mr A's first argument.

6. Mr A's second argument relates to the Appellant's inability to pay the penalty tax assessed. We have no evidence before us as to the Appellant's current financial resources. In any event, this is a matter for the Appellant to discuss with the Collection Section of the IRD to see whether payment by instalments, or some other payment option, is appropriate in its circumstances. This consideration should not affect the level of penalty assessed in earlier years of assessment. This is a matter that should be judged on its own merits relevant to each particular year of assessment for which penalty tax is raised.

7. Turning generally to whether the penalty tax assessed was excessive in the circumstances, we agree with the Commissioner's representative, Mr Garry Laird, that the level of

[1] The compound offer was not proceeded with, and the amount of $3,000 was not demanded from the Appellant, since the conditions set out therein were not satisfied. In the event, the Commissioner decided to take action under section 82A.

penalty tax assessed for each year of assessment in this case (around 14%) is well within the norm of penalty tax cases for persistent delays in lodging profits tax returns.

8. Notwithstanding this conclusion, we find, albeit with no little hesitation, that the penalty tax for the first year of assessment (1999/2000) appears excessive in all the circumstances. In this regard, we agree with Mr A that we should look at this year of assessment separately from the succeeding years of assessment and pay particular attention to the fact that the Appellant showed good faith by submitting fairly accurate management accounts to the assessor within ten days of the due date for filing its profits tax return for that year of assessment. This action took place before any estimated assessment was issued by the assessor and apparently without prompting by the assessor. In our view, this fact deserves a greater discount than that apparently accorded by the Commissioner.

9. Various Board of Review cases, not cited before us, have focused on this factor as a mitigating circumstance. The Appellant should, however, consider itself fortunate that we also have focused upon this matter in a sympathetic way since we have not neglected Mr Laird' s observation that the assessor raised two estimated assessments before the Appellant finally lodged an objection and filed its profits tax return on 22 March 2001.

10. On the facts found, and the circumstances referred to above, we have decided to reduce the penalty tax assessment for the year of assessment 1999/2000 from 14.93% to approximately 10% of the tax that would have been undercharged if the Appellant' s delay in filing its profits tax return had not been detected. We thus order that the penalty tax assessment for the year of assessment 1999/2000 be reduced from $260,000 to $180,000. There is no compelling reason to reduce the penalty tax assessments for the years of assessment 2000/01 and 2001/02, and these are hereby confirmed.