Case No. D68/94

Penalty tax – late filing of return – quantum of penalty – section 82A of the Inland Revenue Ordinance.

Panel: Howard F G Hobson (chairman), Nicholas Ian Billingham and Manuel Rosas Woo.

Date of hearing: 14 December 1994.
Date of decision: 27 January 1995.

The taxpayer was a company which had repeatedly filed its tax return late. In respect of the year in question it was 340 days late. The Commissioner imposed a penalty of 48.16% of the tax involved. The taxpayer appealed on the ground that the amount was excessive.

Held:

The taxpayer had been repeatedly late in filing its tax returns and on certain occasions the delay was years rather than months. A penalty of approximately 48.16% of the tax involved was not excessive.

Appeal dismissed.

Cases referred to:

D2/92, IRBRD, vol 7, 56
D5/92, IRBRD, vol 7, 84
D11/93, IRBRD, vol 8, 143
D22/93, IRBRD, vol 8, 168
D42/93, IRBRD, vol 8, 318
D53/93, IRBRD, vol 8, 383
D6/94, IRBRD, vol 9, 88
D105/89, IRBRD, vol 6, 384
D61/90, IRBRD, vol 5, 444

Woo Sai Hong for the Commissioner of Inland Revenue.
Chiu Sui Ning of Messrs D P Lau & Co for the taxpayer.

Decision:

This decision concerns an appeal against an additional tax assessment of $170,000 made pursuant to section 82A of the Inland Revenue Ordinance (the IRO) for the year of assessment 1992/93 for the company's failure to file a timely profits tax return in accordance with a section 51 notice.

Mr Chiu Sui Ning who appeared for the Taxpayer called no witnesses. Mr Woo Sai Hong appeared for the Commissioner.

FACTS

The following facts are not in dispute.

The Taxpayer closed its accounts for the year of assessment 1992/93 on 30 June 1992, consequently the Taxpayer was not entitled under the Revenue's block extension scheme for the year of assessment 1992/93 to any extension of the one month laid down by the section 51 notice.

On 18 August 1993 an estimated assessment of $420,000 was raised, based on the previous year's return plus a small percentage increase. The Taxpayer did not object and paid $73,000 being the tax concerned on 18 November 1993. On 11 April 1994 the Taxpayer's tax representative filed the overdue return which disclosed taxable profits of $2,017,083 whereupon an additional assessment was raised on the $1,597,083 by which the estimated assessment fell short of the returned amount. The tax thereon was $279,489 which was duly paid. The total tax was $352,489.

On 24 May 1994 the Commissioner gave notice as required by section 82A(4) inviting the Taxpayer to show whether he had any reasonable excuse for avoiding the imposition of additional tax. The Taxpayer's tax representative made representations, having considered these the Commissioner made the additional tax assessment mentioned above.

GROUNDS OF APPEAL & SUBMISSIONS

The Taxpayer's main ground of appeal was that there was a reasonable excuse for its failure to respond timeously to the section 51 notice. The excuse put forward was a combination of the following:

First, the Taxpayer's own accounting staff left abruptly in early 1992, secondly the Taxpayer and other companies within its 'group' used a complicated accounting system and due to the large number of inter-group transactions, extensive adjustments were required to reconcile the books before the accounts could be finalized, thirdly the new staff were faced with coping with the complicated computer system and re-construction of the books from accounting records left incomplete by their predecessors. In the result it was only in late 1993 that the Taxpayer's accounts for the year of assessment 1992/93 were ready for audit. The grounds went on to suggest that as a result of the loss or liquidation of

some of the group's customers during 1992 and 1993 the directors' attention was directed to soliciting new customers outside Hong Kong which resulted in 'the taxation matters of all the group companies being overlooked'. In contrast the Commissioner's representative argued that in effect it was self-evident that this neglect to give adequate attention to taxation matters could not per se amount to a reasonable excuse and we entirely agree with him – anyhow even if other excuses might otherwise be capable of being characterized as 'reasonable', the neglect would seriously diminish their value.

Though the grounds themselves did not expressly argue that the additional assessment was 'excessive having regard to the circumstances' (section 82B(2)(c)) we treated that argument to be implicit from the following reference. The grounds referred to an additional assessment of $100,000 raised on Company A, said to be another 'group' company, for the year of assessment 1990/91 which in his oral submissions to us the tax representative said represented 19.75% of the tax undercharged due to a failure to file a return for 759 days. In the instant case the penalty of $170,000 represented 48.16% of the $352,989 undercharged tax for a failure of 340 days by comparison was excessive.

Although Mr Chiu referred to Company A as a 'group company' he later confirmed that it was not a parent nor a subsidiary nor an associate of the company – but it did have the same directors and shareholders.

The tax representative in further support of his oral argument that the $170,000 was excessive submitted a comparative table which we reproduce verbatim:

Case No.	**Approxi-mate No. of days late**	**Tax under-charged**	**Penalty**	**%**	**Winner**
D2/92, IRBRD, vol 7, 56	320	351,946	35,000	9.94	IRD
D5/92, IRBRD, vol 7, 84	300	358,639	120,000	33.46	IRD
D11/93, IRBRD, vol 8, 143	290	687,418	140,000	20.37	IRD
D22/93, IRBRD, vol 8, 168	290	617,924	100,000	16.18	IRD
D42/93, IRBRD, vol 8, 318	310	166,435	30,000	18.03	taxpayer Penalty reduced to $16,000 (that is, about 10%)

D53/93, IRBRD, vol 8, 383	85	722,621	100,000	13.84	IRD
D6/94, IRBRD, vol 9, 88	390	373,265	150,000	40.19	IRD
The Taxpayer	340	352,989	170,000	48.16	-

He referred us the following passage from D42/93 at page 321:

'It appears to us that the range of penalties in cases of this nature are somewhere between the minimum of the 5% imposed where a person is late in paying tax duly assessed to 25% where there are more aggravating circumstances. In practice the penalty is likely to fall between the limits of 10% to 20% of the amount of tax involved.'

He went on to draw our attention to the reduction in that case and implied a similarity to the present case.

In his further submissions the representative suggested that the Taxpayer's problems were exacerbated by a change of directors in October 1992: no evidence was called in support, we therefore treat the submission as being without merit. He also said that proviso (b) to section 64(1) stipulates that an appeal against a section 59(3) assessment is only valid if a return is submitted within one month supported by audited financial statements. Since, so he claimed, such statements were not available to Company A in time no objection could be lodged against estimated assessments raised on Company A respectively for the years of assessment 1991/92 and 1992/93. The consequence was that the assessments became final under section 70, yet in the final analysis (that is, after the returns were submitted) the estimated assessments were greater than what otherwise would have been the taxable profit by $74,495 for the year of assessment 1991/92 and by $430,673 for the year of assessment 1992/93.

REVENUE'S RESPONSE

Our attention was drawn to the following:

In D2/92, IRBRD, vol 7, 56 at page 58:

'With due respect to the representative we are unable to accept his submission that there was a reasonable excuse. The Inland Revenue Ordinance imposes an obligation upon all taxpayers to file their tax returns on time. In this case the Taxpayer was able to carry on its business, paying its bills and collecting its accounts receivable from its customers. It is well known that problems can arise when accounts are changed from a manual system to a computer system. The Taxpayer chose to computerize its accounts and chose the computer and

the software. We have no doubt that if the Taxpayer had really wanted to fulfil its obligations under the Inland Revenue Ordinance it could have done so.'

The problems resulting from the Taxpayer's own choice of a complicated accounting system could not constitute a reasonable excuse.

It was pointed out that the papers showed that the auditor's report to the financial statements in question is dated 22 December 1993 yet no explanation was offered as to why the return was not filed until 11 April 1994 – some 4 months after the audit report, and 11 months after the due date for filing namely 1 May 1993.

The Taxpayer had a history of late filing:

Year of Assessment	**Expiry Date for Submission**	**Date of Submission**	**Overdue Period**
1987/88	30-4-1988	19-9-1988	4½ months
1988/89	30-4-1989	28-6-1994	5 years 2 months
1989/90	30-4-1990	28-6-1994	4 years
1990/91	30-4-1991	31-1-1992	9 months
1991/92	30-4-1992	19-12-1992	6½ months

Taking into account such prior record (see for example D6/94, IRBRD, vol 9, 88 at page 90) and in the light of the foregoing, the penalty of $170,000, representing 48.16% of the tax involved, was not excessive.

It was the Commissioner's representative's contention that the Board should disregard remarks made by Mr Chiu concerning both the $100,000 penalty imposed on Company A and the alleged over payments because Company A was a distinct and separate taxpayer and no evidence was led as to the circumstances relating to the 759 days delay or that Company A indeed paid too much profits tax.

In the course of his submission, the Commissioner's representative advised us of two practical aspects which had not been referred to in the Commissioner's bare statement of facts and which are worth mentioning. First, as already mentioned, the Revenue block extension scheme did not apply. Tax representatives were advised of this fact by letter dated 9 March 1993 which also asked the addressee to remind their clients of the penalty provisions. The Taxpayer's representative in response to this remark volunteered that he had reminded his client.

Secondly, the Revenue take the view that additional tax assessments raised after the end of the year of assessment in question can only be imposed by reference to the tax for the year in question hence provisional tax is ignored when assessing an amount 'not exceeding treble the amount of tax which … (ii) has been undercharged …' under section 82A(1).

CONCLUSION

With regard to D42/93 in that case the Board felt a reduction of the additional tax assessment to be in order due to the taxpayer having paid an estimated assessment which was in excess of the proper liability as established when the taxpayer eventually filed its return. In determining the reduced penalty the Board directed its attention to the tax to which the taxpayer would have been assessed if it had filed its return in time and not to the tax on the estimated assessment. So far as the Taxpayer is concerned there is no overpayment of tax for the year of assessment 1991/92. With respect to Company A its additional tax of $100,000 was imposed for the year of assessment 1990/91 whereas the alleged overpayments are attributable to two subsequent years of assessment. These distinguishing features suffice to put the present case outside the ambit of the principle considered in D42/93.

We can find nothing whatsoever in the submissions made on behalf of the Taxpayer which bears any resemblance to a reasonable excuse for this the sixth successive failure to file requisite returns in time. As no testimony was offered to explain it away we must treat the Taxpayer's abysmal record at its face value. The catalogue set out above shows months and even years of delay. As mentioned no reason was given for the 4 months delay after the auditor's report. We are therefore of the view that the penalty is not excessive in the circumstances, accordingly we dismiss this appeal and confirm the additional tax assessment of $170,000.

For the sake of completeness we should make the following further remarks:

(a) We were referred to and carefully considered comments addressed to us regarding D105/89, IRBRD, vol 6, 384, and D61/90, IRBRD, vol 5, 444 in addition to those referred to earlier.

(b) We do not agree with the Commissioner's representative's argument that as a matter of principle the Board is debarred from taking into account the matters of Company A referred to simply because it is a separate taxpayer. It is the directors of a company who are responsible for filing returns on time, we therefore feel that where the boards of two or more companies have the same directors evidence – favourable or otherwise – may be adduced to show how they have behaved in similar circumstances regarding the company or companies which is or are not the subject of the appeal. In the instant case the subject of the Company A's penalty was introduced by the Taxpayer's representative to compare its penalty with the present penalty. By doing so he ran the risk of the riposte that since Company A's penalty had not proved a

sufficient deterrent a greater penalty was called for. As it happened there were only Mr Chiu's own bare assertions – no evidence was adduced – accordingly we were in no position to draw any inferences, favourable or otherwise.

(c) The onus is upon taxpayers to prove on the balance of probabilities that any assessment appealed against is excessive or incorrect (section 68(4)) and though certain of the strict provisions concerning the admission of evidence do not apply (section 68(7)) in cases such as the present one it is reasonable to expect that a responsible person from the taxpayer will come forward to give supporting testimony and expose himself to cross examination.