

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D89/00

Penalty tax – starting point – record of the taxpayer in preceding years – delay in submitting return.

Panel: Ronny Wong Fook Hum SC (chairman), Winnie Lun Pong Hing and Ng Yin Nam.

Dates of hearing: 18 July and 7 September 2000.

Date of decision: 14 November 2000.

There were persistent delays on the part of the taxpayer in submitting its returns for years of assessment 1992/93 to 1997/98.

The Commissioner imposed additional tax for the above years.

The taxpayer appealed against the additional tax imposed for the years of assessment 1992/93 and 1997/98.

For the year of assessment 1992/93, the taxpayer was more than two years late in submitting its return. No explanation was proffered for the long delay. The additional tax imposed is 96% of the tax undercharged.

For the year of assessment 1997/98, there was also no explanation for the delay. The assessment of additional tax is 86.8% of the tax undercharged.

Held:

1. The starting point for assessing additional tax in cases where it is not alleged that the taxpayer has attempted to evade payment of tax is about 100% of the tax undercharged. Extenuating circumstances, if any, will then be considered (D33/88, D34/88 considered).
2. The Board did not find the assessments of additional tax for the above two years excessive.

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Appeal dismissed and a cost of \$1,000 charged.

Cases referred to:

D33/88, IRBRD, vol 3, 331

D34/88, IRBRD, vol 3, 336

D41/89, IRBRD, vol 4, 472

Yue Wai Kin for the Commissioner of Inland Revenue.

Michael Yu Ping Chuen of Messrs Cliffbrook Limited for the Taxpayer.

Decision:

1. Company A was incorporated in Hong Kong on 29 March 1988. It traded in electrical and electronic goods.
2. Under the block extension scheme offered by the Revenue, Company A had to submit its profits tax return for the year of assessment 1992/93 by 15 November 1993. Company A failed to do so.
3. Messrs Michael P C Yu, Certified Public Accountant [' Mr Yu '], was first appointed auditors of Company A on 1 February 1995. Mr Yu completed the audit of Company A ' s account for the year ended 31 March 1993 on or about 2 November 1995. This was approved on the same day by the Taxpayer in his capacity as a director of Company A.
4. By letter dated 29 December 1995, Mr Yu submitted to the Revenue Company A ' s profits tax return for the year of assessment 1992/93. This was received by the Revenue on 2 January 1996. This submission was late by 778 days computed as from 15 November 1993.
5. There were persistent delays on the part of Company A in submitting its returns.

Year of assessment	Scheduled date for submission of the return	Date when return actually submitted	Delay
1992/93	15-11-1993	31-1-1996	807 days
1993/94	15-11-1994	14-6-1999	1,672 days
1994/95	15-11-1995	17-6-1999	1,310 days
1995/96	15-11-1996	17-6-1999	944 days
1996/97	15-11-1997	7-7-1999	599 days

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1997/98	15-11-1998	24-12-1998	39 days
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6. Due to such reckless disregard of its basic obligation, the Revenue had to issue the following notices of assessment and notices of additional assessment in respect of Company A's profits tax liability.

Year of assessment	Notice of assessment			Notice of additional assessment		
	Date	Assessable profit \$	Tax \$	Date	Additional assessable profit \$	Tax \$
1992/93	26-11-1993	100,000	35,000	18-2-1994 9-2-1996 26-3-1999	100,000 125,842 500,000	35,000 22,022 87,500
1993/94	29-11-1994	220,000	39,800			
1994/95	30-11-1995	250,000	46,200	14-2-1996 4-6-1996	130,000 120,000	42,900 19,800
1995/96	28-11-1996	420,000	75,900	10-2-1997 3-6-1997 22-8-1997	210,000 370,000 500,000	69,300 61,050 82,500
1996/97	28-11-1997	700,000	127,050	13-2-1998	350,000	115,500
1997/98	27-11-1998	1,160,000	203,750			

7. The Revenue carried out a field audit in respect of the accounts of Company A on 1 March 1999. The Taxpayer informed the Revenue that he was the only person in charge of the Taxpayer's affairs since 1995. He was asked by the Revenue to produce accounting records and financial statements in respect of the affairs of Company A.

8. By an agreement dated 12 October 1999, the Taxpayer on behalf of Company A agreed that the assessable profits of Company A for the relevant years of assessment should be as follows:

Year of assessment	Profits already reported/assessed	Agreed assessable profits \$	Assessable profits understated \$
1992/93	Nil	355,525	355,525
1993/94	Nil	454,712	454,712
1994/95	Nil	776,925	776,925
1995/96	Nil	1,500,000	1,500,000
1996/97	Nil	1,050,000	1,050,000
1997/98	Nil	465,513	465,513
Total	Nil	4,602,675	4,602,675

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The Taxpayer expressly acknowledged that acceptance of these assessable profits does not conclude the whole matter and if additional tax is imposed, the maximum amount could be treble the amount of tax undercharged.

9. As a result of the agreement reached on 12 October 1999, the Revenue sent to the Taxpayer various notices of revised assessment dated 27 October 1999 for the years of assessment in question.

10. By notice dated 29 December 1999, the Commissioner informed the Taxpayer of his intention to impose additional tax by virtue of the Taxpayer's failure to comply with the requirement of section 51(1) of the Inland Revenue Ordinance ['IRO'] (Chapter 112) to furnish tax returns for the six years between years of assessment 1992/93 and 1997/98. The Taxpayer was invited to submit representations with regard to such proposed assessment.

11. By letter dated 25 January 2000, Cliffbrook Limited ['Cliffbrook'], tax representative of the Taxpayer, made the following representations for consideration by the Commissioner:

- (a) ' ... the company's former director, Mr B was involved in civil jurisdiction during the year 1995 ... our client ... remained unable to complete the accounts for the subject year without the co-operation of the former director.'
- (b) ' Our client paid all tax amounts due under your estimated assessments. By misunderstanding, our client believed that once the amount of tax due under your estimated assessments exceeds the actual tax amount which should have been assessed if tax return had been duly filed had been paid, could mean that no tax are under charged and your department would not take any action against the tax payer.'
- (c) ' In fact our client had overpaid tax for the year 1995/96 and 1996/97 in the amount of \$97,505 ...' .

12. By notices of assessment dated 25 February 2000 and addressed to the Taxpayer as director of Company A, the Commissioner imposed additional tax in the following amounts:

Year of assessment	Assessable profits understated \$	Amount of tax undercharged \$	Additional tax imposed \$	Relationship between additional tax and the amount of tax undercharged

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1992/93	355,525	62,216	60,000	96%
1993/94	454,712	79,574	83,000	104%
1994/95	776,925	128,192	130,000	101%
1995/96	1,500,000	169,814	80,000	47%
1996/97	1,050,000	153,431	120,000	78%
1997/98	465,513	69,128	60,000	86%
	4,602,675	662,355	533,000	80%

13. This is the Taxpayer's appeal against the additional tax imposed for the years of assessment 1992/93 and 1997/98.

14. In respect of the year of assessment 1992/93, the Taxpayer submitted as follows:

- (a) 'It was not a common practice for the Inland Revenue Department to raise additional tax during the year 1992/93 ... The Commissioner should not apply current practice and measure of assessing additional tax to a case of prior period.'
- (b) Company A did not have a history of late filing of return prior to the year of assessment 1992/93 and the Commissioner should not take Company A's subsequent performance into account in assessing its liability for this year of assessment.
- (c) The Commissioner simply put '100% on assessed profits tax as the additional tax' without considering the number of days whereby the return was delayed.

15. In respect of the year of assessment 1997/98, the Taxpayer submitted as follows:

- (a) The return was only 39 days late.
- (b) The range of penalty in decided cases for similar delay was 5% to 15% of the amount of tax undercharged. 86.8% of the amount of tax undercharged is grossly excessive.
- (c) The Commissioner was again criticised for a mechanical application of the rate of 100%.

The hearings before us

16. Mr Michael Yu Ping Chuen of Cliffbrook appeared on behalf of the Taxpayer at the hearing before us. We presume he is the same Michael Yu who handled Company A's affairs in

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1995. His lack of courtesy is matched by his failure to display any measure of professionalism. The hearing on 18 July 2000 was adjourned in order to enable him to produce before us authorities in support of his propositions. He was late for the hearing on 7 September 2000. He did not tender any apology for keeping the Board waiting. The first 10 minutes of this second session was spent sorting out his submissions. We deprecate this sort of behaviour.

Our decision

17. In relation to the year of assessment 1992/93, the Revenue tendered before us D33/88, IRBRD, vol 3, 331; D34/88, IRBRD, vol 3, 336 and D41/89, IRBRD, vol 4, 472 in order to demonstrate that the penalty imposed for that year is in accordance with the level of penalties regularly upheld by the Board in 1988 and 1989. The Revenue further drew our attention that Company A was late in submitting its returns for years of assessment 1988/89 and 1989/90. Mr Yu did not produce any authority to support his original contention that the penalty imposed for the year of assessment 1992/93 was not in line with the then applicable practice. Instead he sought to distinguish the cases cited by the Revenue on their facts. Contrary to the approach as suggested by the Taxpayer's notice of appeal, he invited us to look at the whole course of dealings between the Revenue and the taxpayers in those cases. No attempt was made to home in on any specific year of assessment. Mr Yu did not explain why the Taxpayer submitted previously that Company A had an unblemished record prior to the year of assessment 1992/93. He argued that Company A's conduct before the year of assessment 1992/93 should not be taken against the Taxpayer as he did not become a director of Company A until 5 August 1991.

18. We are not impressed by any of these arguments. In D33/88, which was decided on 23 August 1988, the Board clearly pointed out that:

' It would appear that the starting point for assessing penalties in cases of this nature where it is not alleged that the Taxpayer has attempted to evade payment of tax is a penalty of approximately one times the amount of tax undercharged or one-third of the total maximum penalty of three times. This is not a hard and fast rule but is a useful starting point.'

19. This was echoed by the Board in D34/88 decided on 24 August 1988. The Board said this:

' As previous Boards have stated in cases of this nature, the starting point for assessing an appropriate penalty would appear to be approximately 100% of the tax undercharged. In effect, this means that, for completely ignoring one's tax obligations, one can assume that one is likely to have to pay about double the tax which other citizens who handle their tax affairs properly are required

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to pay. This is not unreasonable when it is borne in mind that the tax rates in Hong Kong are comparatively low and that the system of taxation in Hong Kong relies upon individual taxpayers making full and frank disclosures of all their taxable income on a voluntary basis. If this is taken as the starting point for cases of this type, the question then to be decided is whether on the particular facts of this case there are any extenuating circumstances which would merit a decrease in the amount of the penalties ...'

20. Company A was more than two years late in submitting its return for the year of assessment 1992/93. The Taxpayer became Company A's director on 5 August 1991. It was his responsibility to ensure due compliance. No explanation was proffered for the long delay. The penalty imposed is 96% of the tax undercharged. This penalty is on the low side bearing in mind the level of penalties as reflected in the authorities for the relevant period and the total lack of any mitigating circumstances.

21. We turn now to the year of assessment 1997/98. Despite the benefit of an adjournment, Mr Yu did not produce any authority to support the Taxpayer's contention that in similar Board of Review cases, 'the additional tax ranged from 5% to 15%'. In relation to this year of assessment, the Commissioner is obviously entitled to take into account the poor record of Company A/the Taxpayer in the preceding years of assessment. Once again, there is no explanation for the delay. It is said that the Taxpayer co-operated with the Revenue during its field audit. We are satisfied that the Revenue had sufficiently catered for this factor when they departed from the 100% mark. We cannot detect any error in principle as to justify our interference.

22. We are of the view that the Board's time was wastefully incurred as a result of the conduct of the Taxpayer's representative. The appeal should have been properly prepared for full argument on 18 July 2000. A further session was held on 7 September 2000 so that Mr Yu could justify his reckless assertions. We order the Taxpayer to pay costs in the sum of \$1,000. It is a matter between the Taxpayer and Mr Yu whether the Taxpayer should be indemnified by Mr Yu in respect of this order.

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