

Preface to the First Edition

The purpose of this book is to provide materials for students to prepare for Paper 11(H) of Tax Planning (Module E of Professional Stage) of the HKSA/ACCA Joint Scheme Examination (now Paper P6 (HKG) Advanced Taxation (Hong Kong) of the ACCA Examination). This book covers in full Paper 11(H) (now Paper P6 (HKG) Advanced Taxation (Hong Kong)) and Paper 7(H) of Tax Framework (now Paper F6 (HKG) Taxation (Hong Kong)).

At the end of each chapter, there are past ACCA/HKSA examination questions with suggested answers. In addition, there are a number of discussion questions; answers are not provided for these questions. The purpose of these questions is to enable course tutors to use them as exercises or for class discussion.

The materials in this book are based on those prepared for revision courses for Paper 11(H) (now Paper P6 (HKG) Advanced Taxation (Hong Kong)) which have been taught by the authors for a number of years. The authors are grateful to the students of these courses for their helpful suggestions and support.

This book includes relevant legislation and cases up to 1 May 1994.

Acknowledgements are due to the Hong Kong Society of Accountants for permission to reproduce the examination questions from their past papers. The answers to some of these questions are reproduced from the answers published by the Society. Finally, the families of the authors are acknowledged for their moral support and forbearance.

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Preface to the Sixteenth Edition

Since the publication of the fifteenth edition, there have been some changes in tax law and practice. Some of the significant developments are summarised below for ease of reference:

Court Cases

The Court of Final Appeal (CFA) dismissed the taxpayer's application for leave to appeal to the CFA in *Chan Chun Chuen v CIR* (2012) FAMV 23/2012 in respect of the decision of the Commissioner of Inland Revenue (CIR) to reject the late objection lodged.

The Court of Appeal has decided the following case:

- *CIR v Li & Fung (Trading) Limited* (2012) CACV 86/2011 — dismissed the CIR's appeal and held that the commission income was offshore.
- *CIR v Nice Cheer Investment Ltd* (2012) CACV 135/2011 — dismissed the CIR's appeal and held that the unrealized gain in respect of shares held for trading was not taxable. The CIR has obtained leave to appeal to the CFA.
- *Aviation Fuel Supply Company v CIR* (2012) CACV 150/2011 — dismissed the CIR's appeal and held that the lump sum received by the taxpayer was not taxable and should not be used to calculate the balancing charge. The CIR has applied for leave to appeal to the CFA.
- *Braitrim (Far East) Ltd v CIR* (2012) CACV 45/2012 — dismissed the taxpayer's appeal and held that the capital expenditure on moulds was not deductible. The taxpayer applied to the CFA for leave to appeal.
- In *Turner Entertainment Networks Asia, Inc. for Muse Communication Co., Ltd v CIR* (2012) HCIA 4/2010, the Court of First Instance (CFI) held that:
 - the licence fees received for granting the right to exhibit TV programmes outside Hong Kong were taxable; while
 - the technical costs received for providing subtitled tracks for the TV programmes were not taxable.

The taxpayer has appealed to the Court of Appeal.

Departmental Interpretation and Practice Notes (DIPNs)

The Inland Revenue Department (IRD) has updated:

- *DIPN 5* Profits tax deductions for expenditure on
 - (A) Research and development
 - (B) Technical education
 - (C) Patent rights, etc.
 - (D) Building refurbishment

- (E) Prescribed fixed assets
- (F) Environmental protection facilities
- *DIPN 20* Mutual funds, unit trusts and similar collective investment schemes
- *DIPN 21* Locality of profits

The IRD has also issued the following new DIPNs:

- *DIPN 48* Advance Pricing Arrangement
- *DIPN 49*
 - Part A: Profits tax deduction of capital expenditure on relevant intellectual property rights
 - Part B: Taxation of royalties derived from licensing of intellectual property rights

Legislative Changes

2011/12 Budget Proposals Enacted into Law

Affecting the assessments for 2011/12 only

75% of the final tax payable in respect of salaries tax, profits tax and tax payable under personal assessment would be waived, subject to a ceiling of \$12,000 per case.

Affecting the assessments for 2012/13 and thereafter

The changes to personal allowances and concessionary deductions have been incorporated in the table "Summary of Deductions, Tax Rates and Personal Allowances" on page xvi.

2013/14 Budget

Inland Revenue (Amendment) Ordinance 2013

The Amendment Ordinance was gazetted on 5 July 2013 to:

- provide for the reduction of salaries tax, profits tax and tax under personal assessment payable for the year of assessment (YA) 2012/13 by 75%, subject to a maximum of \$10,000 in each case;
- increase the maximum amount deductible from assessable income for the expenses of self-education from \$60,000 to \$80,000 for the YA 2013/14 and subsequent YAs;
- increase
 - the amount of child allowance in respect of a child from \$63,000 to \$70,000 and
 - the maximum amount of those allowances granted to a person from \$567,000 to \$630,000 for the YA 2013/14 and subsequent YAs;
- increase the amount of additional child allowances in respect of a child in the YA in which the child is born from \$63,000 to \$70,000 for the YA 2013/14 and subsequent YAs.

The above changes have been incorporated in the table "Summary of Deductions, Tax Rates and Personal Allowances" on pages xvi to xvii.

Proposed Legislative Changes

Stamp Duty (Amendment) Bill 2012 (gazetted on 28 December 2012)

The object of the Bill is to impose:

- a higher rate of special stamp duty (SSD) on certain agreements for sale and conveyances on sale of residential properties that are:
 - acquired on/after 27 October 2012 and
 - disposed of within 36 months of acquisition; and
- a new duty, known as the buyer's stamp duty (BSD), on certain agreements for sale and conveyances on sale of residential properties executed on/after 27 October 2012.

Inland Revenue and Stamp Duty Legislation (Alternative Bond Schemes) Bill 2012 (gazetted on 28 December 2012)

The object of the Bill is to amend:

- *the Inland Revenue Ordinance and*
- *the Stamp Duty Ordinance*

to treat as debt arrangements, for profits tax, property tax and stamp duty purposes, particular type of arrangements that are economically equivalent to debt arrangements.

Stamp Duty (Amendment) Bill 2013 (gazetted on 5 April 2013)

The object of the Bill is:

- to adjust the *ad valorem* stamp duty (AVD) rates and
- advance the charging of AVD on non-residential property transactions from the conveyance on sale to the agreement for sale
- as from 23 February 2013.

Inland Revenue (Amendment) Bill 2013 (gazetted on 12 April 2013)

The object of the Bill is to enable Hong Kong to enter into tax information exchange agreements (TIEAs) with other jurisdictions where necessary and to enhance the existing exchange of information (EoI) arrangements under comprehensive avoidance of double taxation agreements (CDTAs).

Comprehensive Double Taxation Agreements (CDTAs)

Hong Kong has signed new CDTAs with Mexico, Canada, Italy, Guernsey and Qatar.

Some readers and friends have been very helpful and provided feedback on errors or omissions in the past editions. I am grateful to them. Last but not least, I would also like to express my thanks to Mr Ho Chi Ming, Mr Alvin Chan and Ms Lisa Wong for giving valuable advice on the contents of this book.

be made in writing at least 14 days in advance of the relevant expiration date of the block extension. An explanation of why lodgement cannot be made in a timely manner, together with supporting evidence, must accompany the application.

11. For newly registered businesses, the IRD usually issues the first profits tax return some 18 months after the date of incorporation or the date of commencement of a new business. However, where circumstances warrant, the IRD may issue a provisional profits tax return for completion at an earlier date.

Powers of the IRD to Obtain Information

FURTHER RETURNS (S 51(3))

12. An assessor can give written notice to a taxpayer requiring him to supply a further or fuller return in support of his return (s 51(3)). This power will only be exercised after a return has been submitted.

POWERS TO COLLECT INFORMATION/DOCUMENT FROM THE TAXPAYER OR THIRD PARTY (S 51(4)(a))

13. An assessor or inspector is empowered to obtain any information or document from a person whom he considers may be in possession of such information or document that may affect the tax liability or obligation of any person from that person or from any other person. A written notice must be given by the assessor or inspector for such purpose. A reasonable time must be given for compliance.
14. Documents which may be requested include any deeds, plans, instruments, books, accounts, trade lists, stock lists, vouchers, bank statements or other documents which the assessor or inspector considers, are or may be relevant for such purpose.
15. A barrister or solicitor can refuse to comply with a s 51(4)(a) notice in respect of any privileged information or communication given or made to him in that capacity apart from a request for information relating to land and property transactions under s 51(4A).

POWER TO SUMMON A PERSON FOR EXAMINATION (S 51(4)(b))

16. An assistant commissioner is empowered to summon any person to attend and be examined in regard to any matter which may affect his tax liability/obligation or another person's tax liability or obligation.

POWER TO OBTAIN INFORMATION RELATING TO PARTICULAR LAND AND PROPERTY TRANSACTIONS

17. The following persons may be required by an assessor/inspector (under s 51(4)(a)) or the assistant commissioner (under s 51(4)(b)) to supply information/documents or attend an interview in relation to a particular land and property transaction:
- parties to a particular land and property transaction (e.g., vendor, purchaser and confirmor) and their employees (s 51(4A)(a));
 - agents (s 51(4A)(b));
 - any person who either paid or received commission or fee in connection with that particular transaction (e.g., estate agent, solicitor) (s 51(4A)(c)); and
 - banks, solicitors and their employees.

Legal professional privilege not available

18. Legal professional privilege is not available to a barrister or solicitor in respect of a request for information under s 51(4A).

Statements of Assets and Liabilities and Search Warrants

19. In a suspected tax evasion case, the CIR is given powers to obtain:

- a statement of assets and liabilities with the consent of the BoR (s 51A); and
- a search warrant upon application to a magistrate for seizing documents (s 51B).

For details, please refer to Chapter 21.

POWER TO OBTAIN INFORMATION FROM OFFICERS EMPLOYED BY THE GOVERNMENT OR A PUBLIC BODY (S 52(1))

20. The CIR is empowered to give written notice to an officer in the employment of:
- the government; or
 - any public body

requiring him within a reasonable time to furnish any particulars, for the purposes of the IRO, which may be in the officer's possession.

21. The above officer is not obliged to disclose any particulars which he is under an express statutory obligation to observe secrecy (s 52(1)).

Obligations of Taxpayer

NOTIFICATION OF CHARGEABILITY TO TAX (S 51(2))

22. Every person who is liable to tax for any YA is required by s 51(2) to inform the CIR in writing, not later than four months after the end of the basis period for that YA, that he is chargeable to tax, unless he is already required to furnish a return under s 51(1).

▶▶ Example 1

Mr Chan, after graduating from a university, joined an accountancy firm on 1 July 2012 with a monthly salary of \$15,000. He is single and has no dependants. He does not have other income. As his total salary of \$135,000 (i.e., \$15,000 per month × 9 months) for the period from 1 July 2012 to 31 March 2013 exceeds his personal allowance, he is liable to pay salaries tax for the YA 2011/13.

He is required under s 51(2) to inform the CIR of his chargeability to salaries tax not later than 31 July 2013 (i.e., the last day of the fourth month after the YA 2011/13) unless he has already been sent a s 51(1) return for reporting his salaries income.

NOTIFICATION OF CESSATION

23. Every person whose source of chargeable income/business/rental income ceases, is required by s 51(6) to inform the CIR in writing within one month of cessation of a source of chargeable income.

▶▶ Example 2

Mr Cheung ceased to work for A Ltd. as from 1 October 2012 and began to study full-time in a tertiary institution in Hong Kong. Mr Cheung was required to inform the CIR in writing that he had ceased his source of salaries income not later than 1 November 2012.

NOTIFICATION OF DEPARTURE FROM HONG KONG (S 51(7))

24. Any person chargeable to tax who is about to leave Hong Kong for over one month is required by s 51(7) to give written notice to the CIR of his expected date of departure, not later than one month before the expected date of departure.

25. Notification is not required if the taxpayer is required in the course of his employment, business or profession to leave Hong Kong at frequent intervals (s 51(7) proviso (b)).

▶▶ Example 3

Mr Lee is the proprietor of a business in Hong Kong. He plans to cease his business on 30 June 2013 and leave Hong Kong for good. Mr Lee is required to inform the CIR in writing on or before 31 May 2013 of his expected date of departure.

NOTIFICATION OF CHANGE OF ADDRESS (S 51(8))

26. Every person chargeable to tax who changes his address is required by s 51(8) to inform the CIR in writing of the particulars of the change within one month.

KEEPING OF BUSINESS RECORDS (S 51C)

27. Every person carrying on a business or profession in Hong Kong is required to keep sufficient records in English or Chinese to enable the assessable profits of such business or profession to be readily ascertained.

28. For the purpose of s 51C, 'record' (記錄) means:

- books of account (whether legible or in a computer or otherwise) recording receipts and payments, or income or expenditure; and
- vouchers, bank statements, invoices, receipts and such other documents as are necessary to verify the entries in the books of account.

29. The records required to be kept and retained include:

- a record of the assets and liabilities of the person who carries on the trade, profession or business;
- a record of all entries from day to day of all sums of money received and expended by the person in relation to that trade, profession or business; and
- for a business dealing in goods:
 - a record of all purchases and sales (except those sold in the course of cash retail trade), showing the goods, sellers and buyers in sufficient detail to enable the CIR to readily verify the quantity and value of goods and the identities of the sellers and buyers;
 - all invoices in relation to the above;
 - stock list (including quantities and values) of trading stock at the end of the accounting period and all records of stocktakings from which such stock list has been prepared;

- for a business providing services — records of services provided in sufficient detail to enable the CIR to readily verify the entries noted above.
30. Such records must be retained for no fewer than seven years after completion of the related transaction. There is no need to retain such records if:
- the CIR has specified that the records need not be preserved; or
 - in the case of a corporation, the corporation has been dissolved.
31. The penalty for failing to comply with s 51C without reasonable excuse is a fine at level 6 (\$100,000). In addition, the court may order the person who has been convicted to perform the act which he had failed to perform within a specified time. Failure to comply with the court order results in a fine at level 6 (\$100,000) (see Chapter 21).

KEEPING OF RENTAL RECORDS

32. Chapter 6 details the rental records required to be maintained by the taxpayer.

SUMMARY OF TAXPAYER'S OBLIGATIONS

33.

Obligations of taxpayer	Time limit	IRO ref
Obligation to notify the CIR of his being chargeable to tax	Within four months from the end of that YA	s 51(2)
Obligation to notify the CIR of the cessation of source of income	Within one month of cessation	s 51(6)
Obligation to notify the CIR if about to leave Hong Kong (other than business trips)	One month before the date of departure	s 51(7)
Obligation to notify the CIR of any change of address	Within one month of change	s 51(8)
Obligation to keep records		
• business records	No fewer than seven years	s 51C
• rent records	No fewer than seven years	s 51D

Obligations of Employer

OBLIGATION TO FURNISH EMPLOYER'S RETURN (S 52(2))

34. An employer, on receipt of an employer's return (*BIR 56A* and *IR 56B*) issued by an assessor, is required by s 52(2) to furnish the return within the time stated in the return, giving:
- personal particulars and the full amount of the remuneration of all persons employed by him in receipt of remuneration in excess of a minimum figure as fixed by the assessor (s 52(2)(a)); and
 - any other person employed by him named by the assessor (s 52(2)(b)).

If an employer has paid remuneration to local persons (not a corporation) other than employees (e.g., a subcontractor) he should also file *IR 56M* together with *IR 56A*.

OBLIGATION TO NOTIFY COMMENCEMENT OF EMPLOYMENT (S 52(4))

35. A person who commences to employ an individual in Hong Kong who is:
- likely to be chargeable to salaries tax; or
 - a married person

is required by s 52(4) to give written notice (*IR 56E*) to the CIR no later than three months after the date of commencement of such employment.

OBLIGATION TO NOTIFY CESSATION OF EMPLOYMENT (S 52(5))

36. An employer is required to notify the CIR in writing (*IR 56F*) of cessation of employment in Hong Kong of an employee no later than one month before cessation.

▶▶ Example 4

On 28 January 2013, Mr Fong gave notice of resignation to his employer, X Ltd., stating that he would resign as from 1 March 2013. Mr Fong earned \$30,000 per month and was likely to be chargeable to salaries tax for the YA 2012/13. X Ltd. was required by s 52(5) to inform the CIR in writing no later than 1 February 2013 of Mr Fong's expected date of cessation of employment. If Mr Fong had given notice of resignation to X Ltd. later than 1 February 2013 so that X Ltd. was unable to inform the CIR earlier, it is likely that the CIR would have accepted shorter notice provided X Ltd. had acted promptly.

If an employer has reasonable grounds for believing that neither the married employee nor his/her spouse are, or are likely to be chargeable to salaries tax, he is not required to give a notice of cessation to the CIR (s 52(8)).

69. The deduction is not applicable to expenditure incurred in the acquisition of rights in R&D.

Deduction under s 16B before 1 April 2004

70. Before 1 April 2004, s 16B allowed the deduction of expenditure on scientific research. As from 1 April 2004, s 16B is amended to grant deduction of expenditure on R&D.

Deduction under s 16B as from 1 April 2004

71. A deduction is granted to a trade, profession or business for payments made to an approved research institute for R&D in relation to that trade, profession or business. Capital expenditure may also be deducted except expenditure in relation to land and/or buildings.

➤➤ Example 3

A Ltd. is carrying on business in Hong Kong and prepares its accounts to 31 March each year. In the year ended 31 March 2012, it paid the following expenditure relating to its business:

- \$500,000 on purchase of plant and machinery for carrying out scientific research; and
- \$15 million on construction of a laboratory for carrying out scientific research (land cost = \$10 million; construction cost = \$5 million).

A Ltd. can claim a deduction of \$500,000 under s 16B in respect of the plant and machinery used for carrying out scientific research under s 16B. It can only claim an industrial building allowance in respect of the cost of construction of the laboratory (see Chapter 18). It cannot get a deduction for the cost of the land.

72. Expenditure which is met by the Government or public or local authority, whether in Hong Kong or elsewhere or by any other person, shall not be regarded as being incurred.

73. Where:

- any plant or machinery for which R&D expenditure of a capital nature has been allowed under s 16B; and
- the asset is subsequently sold,

the sales proceeds shall (up to the amount previously deducted), be treated as a taxable receipt.

74. Likewise where:

- there is any right arising from the R&D; and
- the right is sold,

the sales proceeds of the right shall (to the extent of the amount previously deducted under s 16B) be treated as a taxable receipt.

TECHNICAL EDUCATION EXPENDITURE (S 16C)

75. Where a taxpayer carrying on a trade or business in Hong Kong pays any sum for the purpose of technical education related to that trade, business or profession at any university, university college, technical college or other educational institution which has been approved in writing by the director of education, a deduction can be granted.

Capital expenditure may be allowed under this section.

CHARITABLE DONATIONS (S 16D)

76. The payment must be a donation of money, not less than \$100 in total, to an approved charitable institution or trust of a public character or to the government, for charitable purposes.
77. The payment must be pure donation. The donor cannot obtain any benefit from the donation (*Sanford Yung* case).
78. A deduction is limited to 35% (25% for the YAs 2003/04 to 2007/08) of the assessable profits after depreciation allowances but before charitable donations.
79. The sum must not qualify for a deduction as an expense under s 16(1), expenditure on R&D under s 16B, expenditure on technical education under s 16C or an allowable charitable donation for salaries tax purposes.
80. Because of the 35% limit, charitable donations should be added back to the adjusted profits first. The approved donations are then deducted against the adjusted profits after deducting the depreciation allowances.

➤➤ Example 4

A taxpayer has adjusted profits of \$100,000 after the deduction of charitable donations of \$16,000 for the YA 2011/12. He is entitled to a depreciation allowance of \$80,000.

Profits tax computation	
Adjusted profits	\$ 100,000
Add: Charitable donation	16,000
	116,000
Less: Depreciation allowance	80,000
	36,000
Less: Approved charitable donations 35%	12,600
Assessable profits	<u>23,400</u>

If, after disallowance of charitable donations and deduction of the depreciation allowance, the computation yields an adjusted loss, any approved charitable donations will not be allowable.

81. If a donation does not qualify as an approved charitable donation under s 16D, consideration may be given to whether the expense qualifies for deduction under the general rule of s 16(1) (e.g., it is incurred for the purpose of promoting or advertising the taxpayer's product).

INTELLECTUAL PROPERTY RIGHTS (SS 16E, 16EA, 16EB AND 16EC)

82. Tax deductions are available for the purchase of certain intellectual property rights (the relevant IPRs) under ss 16E and 16EA. The tax treatments for different kinds of intellectual property rights (IPRs) are summarised in the following table:

Types of relevant IPRs	• patent rights • rights to any know-how (s 16E (4))	Specified IPRs • copyrights • registered designs • registered trademarks (s 16EA (11))
Commencement	1982/83	2011/12
Conditions for deduction before the YA 2011/12	Expenditure incurred on the purchase of an IPR (other than any amount which is allowable as a deduction apart from s 16E) for use in Hong Kong in the production of chargeable profits (former s 16E(1)). The amount has to be apportioned when the IPR is partly for use in Hong Kong (former s 16E(2)).	N/A

	No deduction is allowable if the IPR is purchased wholly or partly from an associate (former s 16E(2A)).	
Taxation of sale proceeds before the YA 2011/12	Where an IPR in respect of which a deduction has been allowed under s 16E(1) is subsequently sold, the relevant proceeds of sale treated as a trading receipt accruing: <ul style="list-style-type: none"> • at the time of sale; or • if the sale occurs on or after the date on which the trade, profession or business is permanently discontinued, immediately before the discontinuance (former s 16E(3)). The amount deemed to be a trading receipt can exceed the amount of deduction previously allowed.	N/A
General conditions for deduction as from the YA 2011/12	<ul style="list-style-type: none"> • Taxpayers must have acquired the proprietary interest, i.e.; legal and economic ownership of the relevant IPR. • The relevant IPRs are in use for the production of chargeable profits. • Where a relevant IPR is used partly in the production of chargeable profits, deduction is only allowed for the portion of capital expenditure that is relevant to the production of such chargeable profits (ss 16E(2) and 16EA(7)). • Where a relevant IPR is owned by more than one taxpayer, tax deduction for each taxpayer is granted for the amount of capital expenditure that is proportional to his/her share in the relevant IPR. • Legal expenses and valuation fees incurred in connection with the purchase of the relevant IPRs are deductible provided that such expenditure is not deductible under any other provisions of the IRO (s 16E(1A)). 	

MINOR OFFENCES UNDER S 80(1)

45. A fine at level 3 (\$10,000) will be imposed for the various offences committed *without reasonable excuse*, but the CIR may compound the penalty to a smaller amount or apply for a court order. A further fine at level 4 (\$25,000) will be imposed if that person fails to comply with the court order (s 80(2B)). Examples of such offences are:

- a taxpayer failing to supply further information requested by an assessor in support of a return (s 51(3));
- an employer failing to submit an employer's return to the assessor (s 52(2));
- a taxpayer failing to supply information to the CIR in connection with his objection (s 64(2));
- a person failing to notify the CIR of cessation of a source of chargeable income (s 51(6));
- a person chargeable under salaries tax, profits tax or personal assessment failing to inform the CIR of his leaving Hong Kong for a period exceeding one month (s 51(7));
- a person chargeable to income tax failing to notify the CIR of his change in address (s 51(8)); and
- an employer failing to
 - notify the CIR of the following information in respect of his employee:
 - (i) commencement of employment (s 52(4));
 - (ii) cessation of employment (s 52(5));
 - (iii) departure from Hong Kong (s 52(6)); or
 - retain monies owing to the employee (s 52(7)).

MAINTENANCE OF BUSINESS RECORDS (SS 80(1A) AND 80(2C))

46. Any person who, without reasonable excuse, fails to keep proper business records or to maintain them for at least seven years shall be guilty of an offence with a penalty at level 6 (\$100,000) and the court may order the person convicted within the time specified in the order to do the act which he had failed to do (s 80(1A)).

Any person who does not comply with a court order under s 80(1A) is guilty of an offence with a penalty at level 6 (\$100,000) (s 80(2C)).

INCORRECT INFORMATION AFFECTING LIABILITY TO A FOREIGN TAX (S 80(2D) — EFFECTIVE FROM 12 MARCH 2010)

47. A person commits an offence if he, without reasonable excuse, gives any incorrect information in relation to any matter that affects his or another person's liability to a foreign tax covered by an EoI article under a CDTA, and is liable to a fine at level 3 (s 80(2D)).

BREACH OF SECRECY (S 81)

48. Any person appointed or employed to carry out the provisions of the IRO is required by s 4 to preserve secrecy relating to any matters coming to his knowledge in the performance of his duties. Any person who does not reserve secrecy required by s 4 is guilty of an offence and liable to a penalty at level 5 (\$50,000) (s 81(1)). The limitation period for prosecution of the offence was extended from six months to six years for an offence committed on or after 11 February 2010 (ss 81(2) and (3)).

TAX UNDERCHARGED — OFFENCES WITHOUT REASONABLE EXCUSE (S 80(2))

49. A fine at level 3 (\$10,000) plus treble the amount of tax undercharged or which would have been undercharged had the offence not been detected, will be imposed on any person who commits the following offences *without reasonable excuse*:

- making incorrect returns either on behalf of himself or other persons;
- making any incorrect statement in connection with a claim for any deduction or allowance;
- giving any incorrect information affecting the tax liability of himself or any other persons;
- failing to submit returns within the time limit (s 51(1)); or
- failing to notify the chargeability to tax (s 51(2)).

The CIR may compound the penalty to a smaller amount.

50. The IRD has in recent years prosecuted employers for submitting an incorrect employer's return in respect of their employees under s 80(2). The penalty at level 3 plus three times of the tax undercharged will be much higher than the penalty under s 80(1) (level 3).

TAX UNDERCHARGED — SECTION 82A ADDITIONAL TAX

51. A penalty under s 82A is only imposed if no prosecution has been instituted under ss 80(2) and 82 in respect of the same facts.

52. Section 82A additional tax may be imposed on any person who, without reasonable excuse:

- makes an incorrect return, either on his behalf or on behalf of another person;

- makes an incorrect statement in connection with a claim for any deduction or allowance;
- gives incorrect information;
- fails to submit a return in accordance with s 51(1), either never submitting a return or delaying to submit the return; or
- fails to notify the chargeability to tax in accordance with s 51(2).

53. The maximum amount of additional tax is treble the amount of tax undercharged or which would have been undercharged had the offence not been detected. Section 82A additional tax can only be imposed by the CIR or a dCIR personally.

Additional tax under s 82A should not be confused with an additional assessment under s 60. The latter is not a penalty, but is raised to collect any tax not yet assessed.

The meaning of 'detected'

54. In *D 34/07*, T was late in informing its chargeability to profits tax and was assessed to s 82A additional tax. T appealed against the assessment and argued that the failure to comply with s 51(2) was not detected. The BoR ruled that 'detection' includes discovery based on information supplied by T.

Whether a return is incorrect

55. In *D 17/08*, following an audit of T's tax returns and an investigation into its tax affairs, the CIR raised on T profits tax assessments for the YAs 1994/95 to 2000/01 after disallowing the deductions of interest expenses, bank charges and legal fees relating to a bank loan under ss 16, 61 and 61A (see Chapter 22). The purported deductions were related to a tax avoidance scheme that T and others had entered into. T appealed to the BoR against the CIR's assessments. The BoR dismissed the appeal in 2005 (*D 94/04*, see Chapter 22). T appealed but later abandoned the appeal and the assessments thereby became final and conclusive under s 70. T appealed to the BoR against the s 82A additional tax assessments subsequently made by the CIR for the YAs concerned. One of T's grounds of appeal was that T had not made incorrect returns. T argued that:

- in accordance with s 51(1), a taxpayer was required to file the return in accordance with the provisions of Part IV 'Profits Tax' of the IRO;
- s 16 fell under Part IV while ss 61 and 61A fell under Part X 'Assessments'; and
- it was commonly believed that an assessment raised under s 61 and/or s 61A could not in itself justify the conclusion that T had made an incorrect return.

The BoR rejected T's arguments for the following reasons:

- The BoR in *D 94/04* decided against T on the s 16 point as s 16 is in Part IV. The decision is final and conclusive under s 69.
- Whether a return is incorrect is a question of fact, not a question of belief. Common belief, even if established, is irrelevant.
- By virtue of the BoR's previous decision and the agreed facts in the present appeal, T had clearly not reported the correct amounts of assessable profits.
- Section 51(1) did not and does not provide for the filing of a profits tax return by a taxpayer 'in accordance with the provisions of Part IV'.

Section 82A(4) notice

56. Before imposing such an additional tax, the CIR or a dCIR has to issue a written notice to the taxpayer concerned. The notice must:

- be issued by the CIR or a dCIR personally;
- specify the offence;
- inform the taxpayer of his right to submit written representation; and
- specify a date (no fewer than 21 days from the date of issue of notice) by which representation must be received.

The above notice can be dispensed with where the taxpayer is about to leave Hong Kong. The CIR or a dCIR may assess the taxpayer to additional tax immediately.

The CIR or a dCIR shall give due consideration to the representations received before raising an assessment to additional tax.

Deceased taxpayer

57. An assessment to s 82A additional tax can be made on the executor of a deceased person (s 82A(6)). The time limit of s 54 proviso (b) does not apply to s 82A additional tax.

Appeals against an assessment to additional tax (s 82B)

58. A taxpayer who wishes to contest the assessment to s 82A additional tax can appeal to the BoR.

59. Requirements for an appeal are:

- the taxpayer must lodge an appeal in writing to the BoR within one month of the notice of assessment being given to him. Before 25 June 2004, the BoR had no power to grant an extension of time for an appeal under s 82B (*Chan Min-ching trading as Chan Siu Wah Herbalist Clinic IRA 6/98*).