

Press release

LCQ7: Depreciation allowances on machinery or plants

Wednesday, March 9, 2011

Following is a question by the Dr Hon Lam Tai-fai a written reply by the Secretary for Financial Services and the Treasury, Professor K C Chan, in the Legislative Council today (March 9):

Question:

Some operators of industrial and commercial enterprises have relayed to me that when the Inland Revenue Department (IRD) recovers from the enterprises depreciation allowances on machinery or plants granted years ago under section 39E of the Inland Revenue Ordinance (Cap. 112) (section 39E), and if such enterprises object and appeal against the recoveries, IRD will issue "Conditional Standover Order" to them requiring them to purchase before a certain deadline Tax Reserve Certificates (TRCs) in an amount equivalent to the amount of taxation to be recovered. The operators have pointed out that as the amount of money needed for purchasing TRCs may be as high as a million, or even over 10 million, the Orders will exert intolerable pressure on cash flow and may cause the enterprises to close down immediately, yet the assessors often do not accept the explanations given by the enterprises, and also warn that if they do not purchase TRCs as instructed, IRD will issue notices to the banks or clients of the enterprises concerned to notify them of the enterprises' situation. Such operators have also pointed out that IRD's action may cause the banks to immediately tighten the credit lines to the enterprises concerned, and deal a direct blow to order negotiations of the enterprises, and that some enterprises may eventually be forced to close down before the tax disputes can be settled. In this connection, will the Government inform this Council:

(a) of the justifications and legal basis for IRD to require the enterprises concerned to purchase TRCs before the tax disputes are settled;

(b) whether it has assessed that requiring the enterprises concerned to purchase huge amount of TRCs will deal a severe blow to their cash flow, which can cause them to close down immediately; if it has, of the details; if not, the reasons for that;

(c) whether the authorities will issue the aforesaid notices to the banks or clients of the enterprises concerned which do not purchase TRCs as instructed; if it will, of the purposes and legal basis of such action; if not, whether they will take other actions;

(d) whether it has assessed if it is sensible, reasonable and lawful for the authorities to issue the aforesaid notices to the banks or clients of the enterprises concerned, thus causing the banks to immediately tighten the credit lines to such enterprises and dealing a direct blow to their order negotiations; if it has, of the details; if not, the reasons for that;

(e) of the number of aforesaid notices issued by the authorities to the banks and clients having business connection with the enterprises concerned in each of the past three years;

(f) if IRD considers that the enterprises concerned could not claim depreciation allowances on some machinery or plants in the past, of the detailed reasons for it to keep on allowing the enterprises to make such claims for years in the first place, and whether any maladministration or mistakes have been involved;

(g) as some members of the trade have pointed out that the one-off tax recovery by IRD after allowing enterprises to claim depreciation allowances on machinery or plants for years will create a snow-ball effect on their tax burden, whether the authorities have assessed if this is true; and why the authorities did not immediately reject the claims of the enterprises in the past;

(h) whether it plans to make any relief arrangements for enterprises which cannot afford to purchase huge amount of TRCs; if so, of the details; if not, the reasons for that;

(i) whether it has assessed if the forced closure of enterprises before the tax disputes are settled because they cannot afford the TRCs expenses is tantamount to depriving the lawful rights of such enterprises to raise objections or lodge appeals in relation to the disputes; if it has, of the details; if not, the reasons for that;

(j) whether it plans to conduct a comprehensive review of the practice of requiring the enterprises concerned to purchase huge amount of TRCs and other related arrangements; if so, of the details; if not, the reasons for that; and

(k) of the total number of "Conditional Standover Orders" issued by IRD to enterprises in each of the past five years arising from matters related to section 39E; if such statistics are not available, why the authorities have not managed properly the data storage system concerned?

Reply:

President,

(a) to (d) and (h) to (j) Section 71(1) of the Inland Revenue Ordinance (IRO) requires that taxpayers shall make payment of tax in the manner directed in the notice of assessment on or before a date specified in such notice. If a taxpayer disagrees with a tax assessment, he/she could lodge an objection and appeal. However, according to section 71(2) of the IRO, despite the fact that the taxpayer has lodged a notice of objection or appeal, he/she is still required to make payment of tax on or before the date specified in the notice of assessment, unless the Commissioner of Inland Revenue (the Commissioner) orders that any payment of tax or any part thereof be held over pending the result of such objection or appeal.

The Commissioner will take into account individual circumstances in considering whether to allow the taxpayers to hold over the payment of tax involved in objection or appeal cases. If it is the opinion of the Commissioner that the objection has little chance of success, or that the tax involved in the objection or appeal case is likely to become irrecoverable, or that the person objecting or appealing is unreasonably delaying the processing of his/her objection or appeal, the Commissioner will not allow the taxpayer to hold over the payment of tax. The taxpayer is required to make payment of tax on or before the due date(s) specified in the notice of assessment.

If it is obvious to the Commissioner that the objection or appeal should be allowed forthwith, an unconditional stand-over will be ordered pending revision of the tax assessment. However, if the Commissioner considers that the objection or appeal has some merits but that the balance of probability, based on the facts known to exist at the date of the objection or appeal, does not weigh definitely in favour of the taxpayer, the Commissioner will issue, as empowered by section 71(2) of the IRO, a "conditional stand-over order" requiring the taxpayer to purchase tax reserve certificates (TRCs) in the amount of the tax held over, or to furnish a banker's undertaking. For most of the objection or appeal cases with "conditional stand-over orders" issued, the purchase of TRCs will be required. Nevertheless, the Commissioner may accept the taxpayer to furnish a banker's undertaking in lieu of purchase of TRCs if the taxpayer could demonstrate that he/she could not afford to purchase TRCs due to financial difficulties.

Taxpayers that encounter financial difficulties in making payment of tax on time may approach the Inland Revenue Department (IRD) to resolve the problem under the established mechanism, including application to IRD for payment of tax by instalments. If taxpayers fail to make payment of tax on or before the specified due date(s) and have not made any instalment arrangements in respect of their overdue taxes, the Commissioner will immediately take various recovery actions against them, including the imposition of surcharges, the issuance of recovery notices to the relevant taxpayers' employers, bankers, debtors and the persons in custody of the assets of the relevant taxpayers, as well as the institution of civil proceedings at the District Court. The Commissioner is empowered by law to recover tax in default so as to protect government revenue.

(e) and (k) Each objection or appeal case may involve multiple grounds of objection. IRD does not have breakdown of statistics on individual objection grounds, nor breakdown of statistics on number of recovery notices issued to the bankers or business clients of the taxpayers.

(f) and (g) According to the IRO and IRD's current practice of "Assess First Audit Later", IRD will first make assessment based on the information furnished by the taxpayers in their tax returns and issue notices of assessment.

If it is discovered subsequently in the course of reviewing the tax returns that the information provided by a taxpayer is not true, IRD may, within the statutory time limit, raise additional assessment on the taxpayer and recover the tax payable. IRD merely acts according to the law. There is no unfair treatment. Nor has IRD changed its usual practice.

Ends