

## **Field audit and tax investigation**

To pave the way for self-assessment, the Inland Revenue Department (IRD) has taken an aggressive stance to combat tax evasion. Over the past decade, it has augmented its resources for field audit and tax investigation. In 1999, the Field Audit and Tax Investigation Units were merged to improve efficiencies in their quest to find tax evaders. Field audit and tax investigation activity has therefore increased substantially.

As the tax and penalty amounts from field audit and investigation exercises are usually very substantial, sufficient experience and knowledge of the IRD's practice is of utmost importance in resolving the problem with the IRD. If you do not know the law and practice in this area, it might be difficult for you to achieve the best terms.

## **How does the IRD select field audit or tax investigation targets?**

A field audit or investigation is normally initiated where there are indications of suspected non-compliance.

Some of the indicators may be:

- 1. A heavily qualified auditors' report**
- 2. Unreasonably low turnover or profit percentage as**
- 3. compared with the industry average or businesses of similar scale and operation**
- 4. Persistent failure to submit or late submission of tax returns**
- 5. Failure to keep proper business records**
- 6. Failure to provide material information requested by the IRD**
- 7. Capital injection or acquisition of private assets of significant amounts from unknown sources .**
- 8. Estates of deceased .**
- 9. An informer**
- 10. Media stories featuring people with new wealth**

## **What to expect during a field audit or tax investigation**

The IRD officers conducting a field audit or tax investigation will carefully examine your business records and personal financial affairs, and possibly those of your close relatives for the latest one to six years of assessment so as to satisfy themselves that your tax returns are in order.

In the course of examination, the IRD may also contact third parties such as your customers, suppliers, bankers, brokers, solicitors, relatives, friends, etc, to obtain additional information and verify your claims regarding your business and personal financial dealings.

Apart from your time and efforts required in attending to the matter, you may be inconvenienced by possible disruptions to the day to day running of your business, possible adverse effects on your reputation, as well as your business associates being drawn into the probe.

## **Consequences of being found in violation of the law**

The IRD will issue tax assessments to recover the amount of tax undercharged, if a taxpayer is found to have

1. made an incorrect return
2. made an incorrect statement in connection with a claim
3. for any deduction or allowance
4. given any incorrect information which affects his/her own tax liability or the liability of any person
5. failed to comply with the requirements to furnish a return .failed to notify the IRD that he/she is chargeable to tax

In addition, the taxpayer may be liable to PENALTY under Section 80(2) of the Inland Revenue Ordinance (IRO) by way of a fine of HK\$10,000 and a further fine of treble the amount of tax undercharged.

In those cases in which sufficient evidence suggests a taxpayer evades tax willfully with intent, prosecution may be instituted under Section 82(1) of the IRO. Upon conviction, the taxpayer could face a fine of HK\$50,000 and a further fine of treble the amount of tax undercharged and imprisonment for three years.

Alternatively, the Commissioner of Inland Revenue or his deputy may assess the taxpayer to additional tax under Section 82A(1) of the IRO a total not exceeding treble the amount of tax undercharged if no prosecution under Section 80(2) or 82(1) has been instituted.

Furthermore, any taxpayer who without reasonable excuse fails to comply with the requirements of Section 51 C of the IRO for keeping sufficient business records, may be fined up to HK\$100,000 under Section 80(1A) of the IRO.

## **How to respond to a field audit or tax investigation**

You should seek professional advice as soon as you are aware of any tax probe. It is important to be well prepared and have a thorough and prior understanding of the whole process as well as the potential consequences of a field audit or tax investigation.

The initial interview with the IRD officers will usually involve a detailed questioning of both your business and personal affairs. We recommend you allow a professional adviser to accompany you to the initial interview.

Also, it is advisable to conduct a preliminary review of your business records and personal financial affairs to identify potential areas of suspicion. On this basis, you may be able to establish with the IRD an acceptable approach at an early stage. This may help in limiting the scope of work and shortening the duration of the field audit or tax investigation. With professional assistance, it is often possible to speed up the preparation of the proposal to the IRD for an early settlement. This may help to enhance the IRD's perception of your sincerity and co-operation.

## **How we can help**

We include a team of specialists who dedicated to research on the IRD procedures and tactics as well as consultation on tax legislation. Our professionals are prepared to assist in your response to the IRD field audit and tax investigation to achieve the most beneficial outcome on your behalf.

We will:

1. conduct a preliminary review of your business and personal financial records
2. negotiate with the IRD on an approach that is of greatest benefit for you
3. accompany you in attending interviews with the IRD officers
4. prepare replies to queries from the IRD on your behalf
5. prepare proposals for settlement and negotiation with the IRD officers to resolve areas of contention
6. help you to demonstrate your full cooperation with the IRD, corroborate reasons for understatement and explain mitigation circumstances
7. negotiate with the IRD for a reduced penalty
8. advise and assist on improvements in business record-keeping, business operations and compliance of tax obligation