

**Case No. D9/13**

**Salaries tax** – deductions – whether the Appellant could deduct interest payment on instalment loan – whether the Appellant needed to be the borrower of the loan in order to claim deduction – whether the Appellant proved that the instalment loan was used to acquire her property – sections 26E, 26F, 68(4) of the Inland Revenue Ordinance (‘the Ordinance’).

Panel: Albert T da Rosa, Jr (chairman), Chui Pak Ming Norman and Julienne Jen.

Date of hearing: 5 April 2013.

Date of decision: 8 July 2013.

For the 2009/10 year of assessment, the Appellant claimed deductions for her salaries tax on home loan interest she allegedly paid in relation to a property she bought in 2009 (‘the Property’). Upon investigation, it was found that part of the deductions claimed was for interest paid on an instalment loan taken out by the Appellant’s husband. The instalment loan was taken out at a different bank from the mortgage loan, and was secured by a mortgage on another property. The Assessor raised additional assessment by disallowing the deduction for the interest paid on the instalment loan. The Appellant objected on the basis that: (i) section 26E of the Ordinance did not require her to be the borrower of any home loan for claiming deductions; (ii) she used the instalment loan to acquire the Property registered in her name; and (iii) she pooled the majority of her income to her husband’s bank account which was used to pay the interest on the instalment loan. The Deputy Commissioner upheld the Assessor’s assessment. The Appellant thus appealed.

**Held:**

1. Properly construed, section 26E does not require a home loan within the meaning of the section to be taken out by the taxpayer himself. The specific requirement of the section only requires the loan to have been applied wholly or partly for the acquisition of a property which is held by and used by the taxpayer as his residence, and which is secured by a mortgage over the property or any other property in Hong Kong.
2. However, according to section 68(4) of the Ordinance, the Appellant still has the burden of proof to show that the instalment loan was indeed used to acquire the Property, and she paid the interest on the instalment loan. The Appellant failed to discharge the burden to prove these facts.

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3. As to the use of the instalment loan, there is no evidence to directly show how the money was used. Moreover, the instalment loan was taken out after the initial deposits were already due. It was contradictory to the Appellant's case that the initial deposits were paid by the mortgage loan and the instalment loan.
4. The fact that the Appellant and her husband pooled their incomes into the account from which interest on the instalment loan was paid was not the same as the Appellant paying interest on the instalment loan. Since it was the Appellant's husband who took out the instalment loan, he must be treated as the person paying the interest to the lending bank. There is no evidence on which any inference in favour of the Appellant can be drawn.
5. Thus the Appellant failed to show that the instalment loan falls within the meaning of a home loan under section 26E, and the interest paid thereon can be claimed as deductions for calculating her salaries tax.

**Appeal dismissed.**

Taxpayer represented by her husband.

Ng Lai Ying Vivian and Yip Chi Chuen for the Commissioner of Inland Revenue.

**Decision:**

**Introduction**

1. Madam A ('the Taxpayer') the Appellant herein objected to the additional salaries tax assessment raised on her for the year of assessment 2009/10 by the Inland Revenue Department. She was represented by her husband Mr B ('the Husband') at the hearing before us. The Appellant and the Husband are both qualified Certified Public Accountants. While the Appellant works as senior finance analyst at an international chemical company, Company C, the Husband teaches at a university.

2. By the determination ('the Determination') dated 9 November 2012, the Deputy Commissioner of Inland Revenue ('the DCIR') upheld the relevant additional tax assessment for the year of assessment 2009/10 of HK\$32,540 and levied tax in the sum of HK\$5,532 on the Taxpayer.

3. The parties wished to use the Cantonese dialect of the Chinese language for all oral proceedings before the Board but to continue to use English for all written evidence without translation into Chinese. All documents submitted to the Board including all previous correspondence between the Appellant and the Respondent were in English. Thus,

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the parties consented to the following procedural directions and the hearing was conducted on the same basis:

- 3.1. that all oral evidence may be given in the Cantonese dialect of the Chinese language without English interpretation;
  - 3.2. that the clerk be informed as soon as possible if it is proposed that any witness will give oral evidence other than in the Cantonese dialect of the Chinese language so that interpretation into that dialect could be arranged;
  - 3.3. that all oral submissions be given in the Cantonese dialect of the Chinese language without English interpretation;
  - 3.4. that all written submissions be in English;
  - 3.5. that there be no need of any translation of documents in one of the official languages to the other; and
  - 3.6. the decision of the panel will be rendered in English and that the panel reserves the discretion to decide on and change the language of the proceedings and the decision if it should appear at a later stage that the choice is inappropriate in all the circumstances of the case.
4. At the hearing the parties agreed to the facts as stated in paragraphs 1(1) to 1(8)(f) of the Determination ('the Agreed Facts').
5. The Husband gave evidence on oath.

**The agreed facts**

6. The agreed facts are as follows:
- ' (1) [The Taxpayer] has objected to the additional salaries tax assessment for the year of assessment 2009/10 raised on her. The Taxpayer claims that she should be allowed deduction of interest incurred under a bank loan borrowed by her husband.
  - (2) By an assignment dated 11 February 1998, the Taxpayer and [the Husband] completed the purchase of a property known as [Property D].
  - (3) (a) By a preliminary sale and purchase agreement dated 22 March 2009, the Taxpayer agreed to purchase a property known as [Property E] at a consideration of \$3,500,000, which was to be

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paid in the following manner:

<u>Amount</u>	<u>Date of payment</u>
\$	
100,000	Upon signing the preliminary agreement
250,000	Upon signing the formal agreement on 15 April 2009
<u>3,150,000</u>	Upon completion
<u>3,500,000</u>	

The formal sale and purchase agreement was executed on 15 April 2009 and [Property E] was assigned to the Taxpayer as sole owner on 22 May 2009.

- (b) To finance the acquisition of [Property E], the Taxpayer obtained a mortgage loan of \$2,450,000 from [Bank F] ('the Bank F Loan'). [The Bank F Loan] was drawdown on 22 May 2009.
- (4) By a letter dated 27 March 2009, Bank G offered to the Husband an instalment loan of \$1,200,000 ('the Bank G Loan'), with Property D as security. The Husband accepted the offer and designated an account with [Bank G] in name of the Husband ('the Husband's Account') to debit therefrom all instalment repayments. [The Bank G Loan] was drawdown and deposited into the Husband's Account on 14 April 2009.
- (5) (a) In her Tax Return – Individuals for the year of assessment 2009/10, the Taxpayer claimed deduction of, among other things, home loan interest of \$50,331 in respect of [Property E].  
(b) The Assessor raised on the Taxpayer salaries tax assessment for the year of assessment 2009/10 in accordance with the information provided on the Tax Return. The Taxpayer did not object to the assessment.
- (6) The Assessor conducted a review on the Taxpayer's deduction claim of home loan interest. In response to the Assessor's enquiries, the Taxpayer provided the following documents:
  - (a) A bank statement issued by [Bank F] to the Taxpayer which showed a total interest of \$17,791.83 was paid in respect of [the Bank F Loan] for the period from 1 April 2009 to 31 March 2010.

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- (b) An offer letter dated 27 March 2009 issued by [Bank G] to the Husband in respect of [the Bank G Loan].
  - (c) A bank statement issued by [Bank G] to the Husband which showed a total interest of \$32,538.81 was paid in respect of [the Bank G Loan] for the period from 1 April 2009 to 31 March 2010.
- (7) Having regard to the above information, the Assessor considered that the interest paid by the Husband under [the Bank G Loan] should not be deductible as home loan interest. The Assessor raised on the Taxpayer the following 2009/10 additional salaries tax assessment:

	\$
Additional net chargeable income	<u>32,540</u>
Additional tax payable thereon	<u>5,532</u>

- (8) The Taxpayer objected against the assessment in [the facts as set out in paragraph 6(6) and 6(7) herein] on the ground that she should be allowed deduction of home loan interest in respect of both [the Bank G Loan] and [the Bank F Loan]. The Taxpayer also put forward the following contentions and information:
- (a) Section 26E of the Inland Revenue Ordinance (‘the IRO’) merely requires, among other things, the payment of home loan interest by the taxpayer. “Home loan” is defined under section 26E(9) to mean a loan of money which is applied wholly or partly for the acquisition of a dwelling and which is secured over that dwelling or other property in Hong Kong. There is no statutory requirement to restrict the home loan must be borrowed in the name of taxpayer.
  - (b) ‘We... could not find the alleged association between “paying” and related “debt liability being crystallized”. In fact, ... there are plenty of examples where the act of paying for something is not necessarily related to the payer’s own debt liability.’
  - (c) ‘I live with my family, which includes my husband, in the dwelling, ... Like the case for most ordinary people in Hong Kong, acquiring a dwelling, and paying off the respective home loan(s), including the principal and related home loan interest, is a family decision and requires the effort of the whole family. Therefore, it would be so unreasonable, again to most ordinary people, of your Department to have apparently assumed, based on face value, that I am unrelated to (a portion of) the home loans my family has made

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use of in acquiring the dwelling; and/or that I might not have paid for the related home loan interest.’

- (d) “... [The Husband] and I are one family. We share happiness and pay the effort in maintaining the family together, financial and other. Financially, ... every month after the pay day, we pool our income together into a number of bank accounts (which could be in either’s name or a joint account), which would then be spent over different types of expenses (and savings), including but not limiting to the home loans, principal and interest. Nevertheless, if your Department insists, we are obliged to confirm to your Department that, for the purpose of section 26E of the IRD, all the loan payments (including those for interest) have been paid by me, out of the pool of bank accounts as mentioned above, some of which are in [the Husband’s] name.”
- (e) “Indeed, arrangement in respect of our payment to [Bank F] ... in more or less the same as that for [Bank G] ... On the condition that your Department can accept that [the Bank F Loan] has been paid entirely by me (but not paid by others on my behalf), we can’t see why it is not the same case for [the Bank G Loan].”
- (f) A breakdown showing the application of money from [the Bank F Loan] and [the Bank G Loan] as follows:

<u>Date</u>	<u>Nature</u>	<u>Amount</u>
		\$
22 March 2009	Initial deposit	100,000
15 April 2009	Balance of the 10% deposit	250,000
22 May 2009	Balance of the purchase price	3,150,000
22 May 2009	Stamp duty and legal fees	84,750
April and May 2009	Furniture, decoration & miscellaneous	65,250
	Total	<u>3,650,000</u>

**The relevant statutory provisions**

7. The relevant sections of the Inland Revenue Ordinance (‘the IRO’ and references to section numbers herein are to section numbers in the IRO) are set out below:

7.1. The deduction of home loan interest is governed by section 26E of the IRO which provides, among other things, the following:

‘ (1) *Subject to the other provisions of this section and to section 26F, where a person pays during any year of assessment any home loan*

*interest for the purposes of a home loan obtained in respect of a dwelling which is used at any time in that year of assessment by the person exclusively or partly as his place of residence, a deduction in respect of the home loan interest shall be allowable to that person for that year of assessment.*

...

(9) *In this section -*

...

*home loan (居所貸款), in relation to a person claiming a deduction under this section for any year of assessment, means a loan of money which is –*

(a) *applied wholly or partly for the acquisition of a dwelling which -*

(i) *during any period of time in that year of assessment is held by the person as a sole owner, or as a joint tenant or tenant in common; and*

(ii) *during that period of time is used by the person exclusively or partly as his place of residence; and*

(b) *secured during that period of time by a mortgage or charge over that dwelling or any other property in Hong Kong;*

*home loan interest (居所貸款利息), in relation to a person claiming a deduction in respect of a dwelling under this section, means interest paid by the person as a sole owner, or as a joint tenant or tenant in common of the dwelling for the purposes of a home loan to –*

(a) *the Government;*

(b) *a financial institution;*

(c) *a credit union registered under the Credit Unions Ordinance (Cap.119);*

(d) *a money lender licensed under the Money Lenders Ordinance (Cap.163);*

- (e) *the Hong Kong Housing Society;*
- (f) *an employer of the person; or*
- (g) *any recognized organization or association;*
- ...

7.2. Section 26F of the IRO governs nomination for the purposes of section 26E and provides:

‘ (1) *Where-*

- (a) *a deduction is allowable to a person under section 26E for any year of assessment; and*
- (b) *the person has no income, property or profits chargeable to tax under this Ordinance for that year of assessment,*

*the person may nominate his or his spouse, being a spouse not living apart from the person, to claim the deduction for that year of assessment.’*

7.3. Section 68(4) of the IRO places on the taxpayer the burden of proving the assessment appealed against is excessive or incorrect:

*‘ the onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.’*

### **The Taxpayer’s grounds of appeal**

8. It can be made out from the Taxpayer’s grounds of appeal that her grounds are as follows:

8.1. Under general English, section 26E of the IRO could not be interpreted in the way as the Deputy Commissioner did, that is the Taxpayer did not borrow the Bank G Loan and therefore there is no ‘home loan’ and ‘home loan interest’ for the purpose of section 26E.

8.2. Section 26E of the IRO did not stipulate that the ‘home loan’ must be borrowed or drawn in the Taxpayer’s name. Thus, section 26E should not be interpreted in the strictest sense legally and it allows for certain flexibility.



8.3. Despite the Bank G Loan was not borrowed in the name of the Taxpayer, if all other conditions provided in section 26E are met, the interest of the Bank G Loan should be deducted as home loan interest. The Taxpayer claimed that she should be allowed the deduction of home loan interest because:

- (a) She does have an interest in Property D and therefore undeniable liability to the Bank G Loan which is secured by a mortgage over Property D;
- (b) She did actually use the Bank G Loan for the acquisition of Property E which was used as her dwelling; and
- (c) She did pool the majority of her monthly salaries to the Husband's Account to pay for most of the expenses including the interest payment on the Bank G Loan.

#### **Substantive issues**

#### ***Must the Taxpayer be the Borrower for the purposes of 'Home Loan' and 'Home Loan Interest' under section 26E(9)?***

9. The Respondent made the following submissions.
  - 9.1. The Shorter Oxford Dictionary defines 'loan' as 'a thing that is lent; esp. a sum of money lent to an individual, organization, etc.' and 'the action or an act of lending; the state of being lent'.
  - 9.2. 'Home loan' and 'Home loan interest' are defined under section 26E(9) which both starts with the phrase 'in relation to a person claiming a deduction'. By looking at what is clearly said in the IRO and fairly at the language used, the only possible interpretation is that the loan of money refers to in the definition of 'home loan' must be, among other things, a loan of money to the taxpayer claiming the deduction but not any other person. If the correct construction of the definition of 'home loan' does not require a loan of money to the person claiming the deduction, it would be otiose to mention the terms 'in relation to the person claiming the deduction under this section' in the definitions of both 'home loan' and 'home loan interest'.
  - 9.3. Had the Appellant's argument that satisfaction of other conditions of section 26E without having a loan of money to her is sufficient for section 26E, it would cause absurdity as someone who did not borrow money would come within the scope of section 26E.

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10. Like the Taxpayer, this Board is unable to agree to the submission advanced by the Respondent.

11. In section 26E(9), the definition of ‘home loan (居所貸款)’ is formulated as ‘in relation to a person claiming a deduction under this section for any year of assessment, means a loan of money which is –...’ and then a number of specific requirements are set out. Those specific requirements do not require that the loan ‘is taken out by the person claiming a deduction under the section. Those specific requirements only require that the loan in question is

‘ (a) *applied wholly or partly for the acquisition of a dwelling which -*

(i) *during any period of time in that year of assessment is held by the person as a sole owner, or as a joint tenant or tenant in common; and*

(ii) *during that period of time is used by the person exclusively or partly as his place or residence; and*

(b) *secured during that period of time by a mortgage or charge over that dwelling or any other property in Hong Kong;’*

12. It can be readily seen that the words ‘in relation to a person ...’ are added to set out the context for,

12.1. ‘... a dwelling which (i) ... is held by the person’ during the period; and

12.2. ‘... a dwelling which (ii) ... is used by the person’ during the relevant period.

13. Similarly, we note that the definition of ‘home loan interest (居所貸款利息)’ in section 26E(9) is that the words ‘in relation to a person ...’ are added to set out the context for the ‘interest paid by the person ... for the purposes of a home loan to [various specified persons]’.

14. There is no requirement in section 26E(9) that the loan in question is taken out by the Taxpayer as such to qualify as a ‘home loan’ or for the interest arising therefrom to qualify as ‘home loan interest’.

**Onus**

15. Notwithstanding our conclusion in paragraph 14 herein, the Taxpayer will still have to satisfy, inter alia, the requirement

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15.1. that the ‘Home Loan Interest’ arises from the relevant Home Loan that is a loan ‘which is applied wholly or partly for the acquisition of a dwelling’; and

15.2. that the Taxpayer paid the Home Loan Interest.

16. In Shui On Credit Company Limited v Commissioner of Inland Revenue, (2009-10) IRBRD, vol 24, 589, Lord Walker NPJ said in the Court of Final Appeal judgment at paragraph 30 that the Board’s function is to consider the matter *de novo* (meaning starting from the beginning; anew)

‘ 30 ... *the Board’s function, on hearing an appeal under s.68, is to consider the matter de novo: CIR v. Board of Review ex parte Herald International Limited [1964] HKLR 224, 237. The taxpayer’s appeal is from a determination (s.64(4)) but it is against an assessment (s.68(3) and (4)) ...*’

17. There has been no concession by the Respondent whether these two points have been established by evidence. It is not for the Respondent to put forward a case and to prove that the Taxpayer’s position is wrong. It is for the Taxpayer to prove that she is so entitled.

18. The Taxpayer and the Husband are well aware of the need to prove payment of the Loan Interest and in fact that was the reason why the Husband chose to give sworn evidence at the hearing. He knew that the Respondent has not conceded this issue. He said

‘ ... 其中一個 *terms* 係到底 ... 我太太 ... 有冇畀 *interest* 呢樣嘢，而家稅局個立場似乎就係話，因為佢唔係 *home loan* 嚟嘅，咁所以呢佢就當冇畀，... 如果佢到時再 *raise* 呢個 *point* 出嚟 ... 咁我作一個證人話畀你聽，咁我--我係見證呢件事情。... 咁稅局 *so far* 就有提出過呢樣嘢，佢哋係好 *agree* 定唔 *agree* 嘅，變咗佢--佢而家話都唔一定個喎咁樣，佢哋覺得即係個個唔--而家發覺係未有足夠嘅證據，咁我又--即係會作為一個--可以作為一個證人咁樣去--去見證呢件事情啦。’

***Was the Bank G Loan wholly or partly used to pay for the dwelling?***

19. In her tax return the Taxpayer claims the deduction in respect of the Property E which is the dwelling in question.

20. In her letter to the Commissioner dated 26 February 2011, the Taxpayer contends:

20.1. ‘We bought [Property E] on March 22, 2009. The loan drawdown date [of the Bank G Loan] was April 14, 2009, i.e. when we have to pay the 10% deposit and stamp duty.’

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20.2. 'We bought [Property E] at HK\$3.5 million the loan amount of the charged property [Property D] is HK\$1.2 million, which is exactly the 30% down payment plus the stamp duty of our [Property E]. The remaining 70% loan is under the [Bank F Loan]'

21. On closer scrutiny, one notes that in the Preliminary Sale and Purchase Agreement for Property E:

21.1. the deposits of \$100,000 and \$250,000 totalling \$350,000 (and not \$1,200,000) were payable on 22 March 2009 and 15 April 2009 respectively.

21.2. the balance \$3,150,000 was payable on completion on 22 June 2009.

22. It is obvious that the Bank G Loan drawn on 14 March 2009 could not have been used to pay the initial deposit of \$100,000 on 22 March 2009.

23. The Taxpayer bears the onus of proof. Unless there is express agreement by the Revenue to any particular fact, it is upon her to prove every factual element upon which she claims her entitlement.

24. In his evidence given at the hearing on behalf of the Taxpayer, the Husband said that as a family member he knows that both loans were used for the acquisition of Property E.

‘我哋想強調嘅就係，兩個 loan...都係攤嚟 acquire 嗰個-[Property E] 嘅...，呢件事情係就我所知作為其中一個 family member，我有參與，我知道呢件事情，... 佢兩個 loans 都係咁樣攤嚟買咗嗰個 property。...’

25. When he was asked to refer us to documents to support that position, all he could point to was the Agreed Facts especially paragraph 8(d) to (f) which at most shows

‘... we pool our income together into a number of bank accounts (which could be in either's name or a joint account), which would then be spent over different types of expenses (and savings) ...’

26. Bank G entered into a loan agreement with the Husband and created a legal relationship as lender and borrower. The loan was deposited into the Husband's Account. Such money became the Husband's own funds and he is at liberty to apply them in whatever way he likes.

27. There is no direct evidence that any portion of the Bank G Loan is in fact used for acquisition of Property E. We are asked to draw inferences by the mere facts of:

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27.1. the proximity of the date and drawdown and the date of the liability to pay under the Preliminary Agreement liability of utilisation; and

27.2. the relative similarities between the amounts of the drawdown and the amounts needed to be paid for the acquisition.

28. We are not provided with the contemporaneous matching bank statements or receipts from lawyers handling Property E Conveyancing or any accounting evidence to show that any portion of the payments for acquisition of Property E came from the Bank G Loan.

29. We are not satisfied on balance of probabilities that the Bank G Loan was disbursed for the acquisition of Property E. Thus, there is no qualifying Home Loan for the purpose of which any qualifying Home Loan Interest could have been paid.

***Any payment of home loan interest?***

30. Given our findings in paragraph 29 herein, it is not necessary for us to consider whether in fact there is payment of the Home Loan Interest.

31. However, in the event that we are wrong, we deal with this question below.

***Mortgage liability equals payment?***

32. The Taxpayer argued that by virtue of the mortgage arrangement, she has undeniable liability towards the repayment of the Bank G Loan, or her interest as one of the joint owners in Property E would be severely damaged.

33. It is not disputed that the Taxpayer has assumed a secondary liability under the mortgage arrangement.

34. However, the Taxpayer merely covenants to upon demand pay make good and discharge to Bank G all sums due by the Husband. Her covenants to pay are no evidence of actual payment.

***Factual payment of home loan interests?***

35. The Taxpayer contends that she did pool majority of her monthly salaries to the Husband's Account to pay for most of the expenses including the repayment to Bank G. As such, the Taxpayer claims that she has paid the home loan interest in respect of a home loan.

36. The Taxpayer's liability under the Mortgage to pay arises upon demand made by Bank G. According to the annual statement issued by Bank G, the Bank G Loan was drawn down on 14 April 2009 and the monthly repayment commenced around one month after the date of advance in accordance with clause 2 of the loan agreement. There is no

information suggesting any default in repaying the Bank G Loan. It is apparent that no payment was ever made by the Taxpayer by virtue of the Mortgage.

37. It might be true that the Taxpayer and the Husband has pooled their incomes and shared the household expenses including the interest payment on the Bank G Loan. However, the Taxpayer's deposit of money into Husband's Account is not equivalent to paying interest to Bank G. It is too far to say that the Appellant has 'paid' the interest. Given the legal effect of the loan agreement is between the borrower and lender, it is the Husband who paid the interest to a financial institution, not the Taxpayer.

38. Again we are not provided with any accounting evidence and we are not prepared to draw the inferences contended for by the Taxpayer.

***Section 26E(2)(b) deeming***

39. Section 26E(2)(b) provides

*'For the purposes of this section, where a dwelling is held by a person otherwise than as a sole owner, the amount of the home loan interest paid referred to in paragraph (a)(i) shall be regarded as having been paid -*

- (i) where the dwelling is held by the person as a joint tenant, by the joint tenant each in proportion to the number of joint tenants; or*
- (ii) where the dwelling is held by the person as a tenant in common, by the tenants in common each in proportion to his or her share in the ownership in the dwelling.'*

40. This section could help the Taxpayer establish the fact of payment of home loan interest in the stated proportion if in fact a home loan had been established.

41. For the avoidance of doubt, we would emphasize that mere establishment of the fact of any amount of home loan interest having been paid by the Taxpayer (no matter by evidence or by virtue of the deeming effect of section 26E(2)(b)) does not amount to establishing the basis for deduction under section 26E(1). One still needs to establish the fact that the payment of the home loan interest is 'for the purposes of a home loan' as required by section 26E(1). Given our findings in paragraph 29 herein, the Taxpayer's appeal fails.

**Conclusion and disposal**

42. The appeal by the Taxpayer is dismissed. We confirm the assessment of the Respondent.