

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D10/89

Appeals – accounts of taxpayer – description of payment as ‘deposit’ and receipt as ‘interest’ – whether taxpayer bound to these descriptions – s 28(1)(a) of the Inland Revenue Ordinance.

Interest tax – interest paid on security amount placed by stockbroker with governmental authorities – whether this amount was a ‘deposit, loan, advance or other indebtedness’ whether interest was subject to interest tax – s 28(1)(a) of the Inland Revenue Ordinance.

Interpretation – meaning of ‘deposit’ – whether the same word can be construed to have different meanings in different statutes.

Panel: T J Gregory (chairman), Glen C Docherty and Hwang King Hung.

Dates of hearing: 4 and 5 January 1989.

Date of decision: 29 April 1989.

The taxpayer company did not carry on business in Hong Kong. However, it was a registered dealer under the Securities Ordinance and the Commodities Trading Ordinance. Under these ordinances, it was required to place deposits with relevant governmental authorities, and these deposits could be forfeited in certain cases. The ordinances provided that the deposits would be released to the taxpayer when it ceased to be registered.

Pursuant to these ordinances, the government paid interest to the taxpayer with respect to these deposits.

The IRD assessed these receipts to interest tax. The taxpayer appealed. It argued that the interest did not arise from a ‘deposit’ within the meaning of section 28(1)(a).

Held:

The interest was not subject to interest tax.

- (a) Not all interest is subject to interest tax. To be subject to interest tax, the interest must arise from those types of indebtedness set out in section 28(1)(a).
- (b) The interest did not arise from a ‘deposit’ as that word is defined in section 2(1), namely, a loan of money.

INLAND REVENUE BOARD OF REVIEW DECISIONS

Prior to that definition being introduced into the Inland Revenue Ordinance, the meaning of 'deposit' had to be construed in the context of the surrounding words, namely, 'loan', 'advance' and 'other indebtedness'. Under this approach, 'deposit' bore a meaning associated with a financial transaction. These words did not describe the payments made by the taxpayer to the governmental authorities, which were in the nature of performance bonds which were subject to forfeiture in certain cases. The payments were not made with a view to earning interest or securing any directly associated financial benefit.

- (c) The fact that the payments made by the taxpayer to the governmental authorities were described as 'deposits' under the Securities Ordinance and Commodities Trading Ordinance did not mean that they were 'deposits' for the purpose of the Inland Revenue Ordinance. A word may have different meanings in different legislation so as to reflect the intent of each legislation.
- (d) The fact that the taxpayer described the payments in its accounts as 'deposits', and called its receipts 'interest', does not oblige the customer to pay interest tax on such receipts.

Appeal allowed.

Cases referred to:

D62/87, IRBRD, vol 3, 43
Bennett v Ogston (1930) 15 TC 374
Darcy v Carragher (1887) 18 IR 317
R v Chief Registrar of Friendly Societies ex p New Cross Building Society [1984] 1 QB 227
Webb v Stenton (1883) 11 QBD 518
Westminster Bank Ltd v Riches (1947) 28 TC 159

Lee Yun Hung for the Commissioner of Inland Revenue.
Peter R Griffiths of Touche Ross and Co for the taxpayer.

Decision:

1. THE NATURE OF THE APPEAL

The Taxpayer Company ('the company') objected to interest tax assessments for the years of assessment 1980/81 to 1986/87, both inclusive, the interest in question being

INLAND REVENUE BOARD OF REVIEW DECISIONS

interest paid under the provisions of the Securities Ordinance (Cap 333) and the Commodities Trading Ordinance (Cap 250).

2. THE FACTS

The following facts are not in dispute:

- 2.1 The company was incorporated as a private company in Hong Kong in March 1979 and has never commenced business in Hong Kong. At all relevant times, it operated as an information centre for its New York affiliate, providing information regarding foreign securities, stocks and commodities to local customers.
- 2.3 The company was registered as:
- 2.2.1 A dealer with the Commissioner for Securities and, pursuant to section 51(1) of the Securities Ordinance, had placed two deposits each of \$50,000 with the Commissioner for Securities; and
- 2.2.2 a dealer with the Commissioner for Commodities Trading and, pursuant to section 31(1) of the Commodities Trading Ordinance, had placed a deposit of \$100,000 with the Commissioner for Commodities Trading.
- 2.3 The deposits are to be released to the company when it ceases to be registered as a dealer as provided under section 52(11) and section 33(11) of the Securities Ordinance and Commodities Trading Ordinance respectively.
- 2.4 Sections 52(7) and (8) of Securities Ordinance and sections 33(6) and (7) of the Commodities Trading Ordinance require such deposits either to be deposited with a licensed bank or invested in such manner as directed by the Financial Secretary. Section 52(9) of the Securities Ordinance and Section 33(8) of the Commodities Trading Ordinance further provide that the Financial Secretary shall, after the end of each financial year, declare a rate of interest to be paid for that financial year in respect of each sum deposited.
- 2.5 The company received in each year of assessment interest as follows:

<u>Year of assessment</u>	<u>Securities dealers' deposit</u>	<u>Commodities dealers' deposit</u>	<u>Total</u>
	\$	\$	\$
1980/81	5,388.66	6,560.11	11,948.77
1981/82	19,705.48	21,000.00	40,705.48
1982/83	16,000.00	15,000.00	31,500.00

INLAND REVENUE BOARD OF REVIEW DECISIONS

1983/84	15,000.00	15,000.00	30,000.00
1984/85	11,500.00	11,000.00	22,500.00
1985/86	13,000.00	11,500.00	24,500.00
1986/87	6,500.00	5,500.00	12,000.00

On various dates, the assessor raised on the company the following interest tax assessments for the years of assessment 1980/81 to 1986/87 inclusive:

<u>Year of assessment</u>	<u>Gross interest</u> \$	<u>Tax payable Thereon</u> \$
1980/81	11,948.77	<u>1,792.32</u>
1981/82	40,705.48	<u>6,105.82</u>
1982/83	31,500.00	<u>4,725.00</u>
1983/84	32,000.00	<u>4,800.00</u>
1984/85	22,500.00	<u>3,825.00</u>
1985/86	24,500.00	<u>4,165.00</u>
1986/87	12,000.00	<u>2,040.00</u>

As a result of representations by the representative of the company, the gross interest for the year 1983/84 is agreed to have been overstated at \$32,000 with tax of \$4,080 payable thereon instead of \$30,000 with tax of \$4,050 payable thereon.

3. DOCUMENTATION

The Board had before it:

- 3.1 A copy of a receipt dated 24 April 1979 for a deposit of \$100,000 paid pursuant to section 31(1) of the Commodities Trading Ordinance.
- 3.2 Copies of two receipts, each for a deposit of \$50,000 paid pursuant to section 51(1) of the Securities Ordinance, dated 24 April 1979 and 16 May 1980.
- 3.3 Copies of letters for the years ended 31 March 1980 to 31 March 1987, both inclusive, from each of the Office of the Commissioner for Securities and the Office of the Commissioner for Commodities Trading enclosing the cheques for the interest itemized in paragraph 2.5 above together with copies taken from

INLAND REVENUE BOARD OF REVIEW DECISIONS

the Government Gazette of the relevant notices as to the rates of interest together with the audited balance sheet, revenue and expenditure account of the deposits received by the said Commissioner.

3.4 Copies of the company's profits tax return with its balance sheet as follows:

<u>Year of assessment</u>	<u>Date of return</u>	<u>Date of balance sheet and audited accounts</u>
1982/83	21 June 1983	31 December 1982
1983/84	14 November 1984	31 December 1983
1984/85	undated	31 December 1984
1985/86	17 April 1986	31 December 1985

3.5 A copy of the determination of the Commissioner dated 23 December 1987.

3.6 The notice and grounds of appeal of the company dated 15 January 1988.

3.7 Extracts from the digest of statistics for October 1984 to May 1987.

4. THE CASE FOR AND SUBMISSION ON BEHALF OF THE COMPANY

4.1 In his opening, the representative of the company:

4.1.1 Stated that the dispute revolved around a question of law, namely, the meaning of 'interest' in section 28(1)(a) of the Inland Revenue Ordinance.

4.1.2 Referred to the reasons of the Commissioner, particularly paragraph 3.3, and submitted that not all interest is taxable under the Ordinance: it is only interest caught by section 28(1)(a) of the Ordinance upon which tax is payable.

4.1.3 Stated that the question for the Board to consider was whether the sums received by the company were interest within section 28(1)(a) of the Ordinance.

4.2 Evidence:

The company called one witness:

4.2.1 He stated that he was the accounting and operations manager of the company by whom he had been employed for about one year. He was in charge of the company's accounting records.

4.2.2 He stated that the bundle of documents produced had been extracted from the company's records, namely, the documents referred to in sub-paragraphs 3.1 to 3.4 above.

INLAND REVENUE BOARD OF REVIEW DECISIONS

- 4.2.3 He produced the company's assessments for the years of assessment 1982/83 to 1985/86, both inclusive, which were admitted as exhibits.
- 4.2.4 Under cross-examination, the witness stated that he was not responsible for the accounts prepared during the relevant period. He had been employed by the company from 1 November 1987. He said that the deposits were described in the balance sheet accompanying the profits tax returns as 'deposits' and the interest paid on the deposits was described in note 1(b) as 'interest received from the Offices of the Commissioner for Commodities Trading and Commissioner for Securities'.
- 4.2.5 There was no re-examination of the witness.
- 4.3 The submission on behalf of the company may be summarised as follows:
- 4.3.1 There had been no mistakes made in the accounts prepared for the company or the returns.
- 4.3.2 The word 'interest' in each of the Securities Ordinance and the Commodities Trading Ordinance has a special meaning. If interest is not 'interest' within section 28(1)(a) of the Inland Revenue Ordinance, it is not taxable even though it may be interest for other purposes.
- 4.3.3 Ground 1 of the grounds of appeal:
- 4.3.3.1 The representative took the Board through section 28(1)(a) and then through section 52 of the Securities Ordinance (Cap 333) and thereafter sections 31 and 33 of the Commodities Trading Ordinance (Cap 250).
- 4.3.3.2 The representative then analysed section 28(1) of the Inland Revenue Ordinance and its various sub-sections. He stated that this case was concerned only with section 28(1)(a), and that the word 'deposit' where used in that sub-section had to be construed ejusdem generis with the remaining words used.
- 4.3.3.3 The expression 'deposit' is defined in 'Words and Phrases Judicially Defined' at page 594. The first paragraph of this definition could have applied until 1982 when the word 'deposit' was first defined in the Inland Revenue Ordinance.
- 4.3.3.4 From 1982 until 1986, 'deposit' can only mean a deposit as defined in the Deposit-taking Companies Ordinance (then Cap 328), and from 1986 it can only mean a deposit as defined in the Banking Ordinance (Cap 155). He submitted that the 'deposits' in question cannot be 'deposits' within the meaning of either Ordinance.

INLAND REVENUE BOARD OF REVIEW DECISIONS

- 4.3.4 The company's representative then proceeded to review the position prior to the inclusion of the definition.
- 4.3.4.1 The word 'deposit' where it appears in section 28(1)(a), when read in context, must refer to a deposit in the nature of a bank deposit, that is, an indebtedness. It has to be read in context with the other words used, namely, 'loan', 'advance' and 'other indebtedness'.
- 4.3.4.2 The Board was then referred to the Shorter Oxford English Dictionary for the interpretation of these words.
- 4.3.5 The representative then referred the Board to:
- 4.3.5.1 Webb v Stenton (1883) 11 QBD 518 and, having cited part of the headnote, proceeded to address various passages in the report.
- 4.3.5.2 R v Chief Registrar of Friendly Societies ex p New Cross Building Society [1984] 1 QB 227: a passage putting forward a similar proposition was cited.
- 4.3.5.3 Darcy v Carragher (1887) 18 IR 317: it was submitted that this was an analogous case: an amount payable at some time but even that was not a debt but could be attached.
- 4.3.6 The representative then referred to the description of the interest as 'turnover' and the note to the accounts referring to 'interest from deposits'. He stated that these 'names' had no significance: the terminology merely repeated what the two Ordinances say. He submitted that the use of the wording of one particular Ordinance does not confer upon that terminology the same meaning when used in section 28(1)(a) of the Inland Revenue Ordinance. Accordingly, the accounts are irrelevant to the appeal and such is supported by Board of Review case D62/87, IRBRD, vol 3, 43.
- 4.3.7 Counsel concluded his comments on ground 1 by stating that the two interest amounts are not chargeable to tax.
- 4.3.8 The representative then proceeded to address ground 2 of the grounds of appeal.
- With due respect to the representative, first, the Board did not regard this ground of appeal as good and, secondly, it is not relevant to the determination of the appeal.

5. THE SUBMISSION FOR THE REVENUE

INLAND REVENUE BOARD OF REVIEW DECISIONS

The Representative of the Revenue handed in a submission which had been revised to reflect the submissions made by the company's representative.

- 5.1 Before going to his submission, the representative of the Revenue referred to the three receipts (the documents referred to in sub-paragraphs 3.1 and 3.2 above) and focused attention on the word 'deposit' used in the receipts. The expression 'deposit' was used prior to that word being defined in the Ordinance, so that the word should be given its ordinary meaning.
- 5.2 The Commissioner's representative then went to his written submission in which, having focused on the disagreement between the parties and stating that the onus of proof was on the company to establish that the sums concerned were not correctly brought to charge, the history of the events leading to the payment of interest was addressed.
- 5.3 The Board was then taken through the charging section, section 28(1)(a) of the Ordinance, whereafter the word 'interest' was reviewed. Various cases were cited during the course of this address as follows:
 - 5.3.1 Westminster Bank Ltd v Riches (1947) 28 TC 159 and
 - 5.3.2 Bennett v Ogston (1930) 15 TC 374.
 - 5.3.3 The Commissioner's representative then proceeded to submit that the amounts received were to be treated as interest. He proceeded to examine the definitions of the words 'loan', 'deposit' and 'other indebtedness' by reference to the Shorter Oxford English Dictionary.
- 5.4 He then proceeded to analyse the cases cited by the company's representative.
 - 5.4.1 The representative of the Revenue submitted that, as soon as the 'deposits' had been paid by the company to the relevant Commissioner, the relevant Commissioner was indebted to the company in the sense that the deposits concerned would have to be repaid to the company (see section 52(11) of the Securities Ordinance and section 33(11) of the Commodities Trading Ordinance). The fact that the company was entitled to apply for the release of the deposits without any financial risk when it ceased to be registered as a dealer demonstrated that the interest received by the company was interest on indebtedness.
- 5.5 The representative also referred the Board to section 52(2) of the Securities Ordinance and section 33(1) of the Commodities Trading Ordinance in order to substantiate the statement that deposits were a debt or a form of indebtedness in that there was a payment due to a liquidator unless forfeited.

INLAND REVENUE BOARD OF REVIEW DECISIONS

- 5.6 The representative then proceeded to submit that, if the Board did not regard the interest as interest on an indebtedness, it should be treated as interest on a loan or a deposit. The dictionary was again referred to for the meaning of the word 'loan' and the word 'lend'.

6. REPLY OF THE COMPANY'S REPRESENTATIVE

In his reply to the Commissioner, the company's representative restricted his comments to his main arguments, the charging part of section 28, and proceeded to comment on the Revenue's authorities and the definitions cited by the Revenue. He concluded by commenting that the crux of the case was the question as to whether there was a present obligation of the Commissioner to pay this money at any time. The company said that there was no such obligation, in which case the deposits cannot be any form of 'debt' and no interest arose with respect to them.

7. REASONS FOR THE DECISION

- 7.1 The part of section 28 of the Ordinance relevant to this appeal is the preamble set out in sub-section (1) and the specific provisions of sub-section (a). They read:

'Interest tax shall, subject to the provisions of this Ordinance, be charged for each year of assessment on the recipient of any sum paid or credited to him in that year being –

- (a) interest arising in or derived from Hong Kong on any debenture, mortgage, bill or sale, deposit, loan, advance or other indebtedness whether evidenced in writing or not'

- 7.2 As the interest paid to the company was received in a period prior to the word 'deposit' being defined and a period subsequent to it being defined, the Board has to consider both positions.

- 7.3 Prior to inclusion of the definition:

- 7.3.1 The Board agrees with the submission made on behalf of the company: the word 'deposit' should be construed ejusdem generis with the other words in the sub-section.

- 7.3.2 It is perfectly clear that the 'deposits' paid by the company to the Commissioner of Securities and the Commissioner of Commodities Trading cannot fall within the meaning of 'debenture', 'mortgage' or 'bill of sale'. In the opinion of this Board, these expressions and the following expressions, 'loan' 'advance' and 'other indebtedness', confer on the word 'deposit' a meaning associated with a financial transaction.

INLAND REVENUE BOARD OF REVIEW DECISIONS

7.3.3 Although the Securities Ordinance and the Commodities Trading Ordinance use the word 'deposit', the Board cannot accept that the payments made by the company to the Commissioner of Securities and the Commissioner of Commodities Trading were in the nature of loans or advances to the respective Commissioners or indebtedness of the respective Commissioners to the company. The 'deposits' are in the nature of a performance bond, namely, sums of money which are subject to forfeiture in given events. The 'deposits' were not made by the company with a view to earning interest or to secure any directly associated financial benefit. The 'deposits' were made as a precondition to the carrying on of the company's business. Being in the nature of a performance bond, they are not 'deposits' as that word is used in section 28(1)(a).

7.4 After inclusion of the definition:

The Board finds that the situation was not altered by the inclusion of the definition of the word 'deposit'. The 'deposits' continued as deposits in the nature of a performance bond and, quite clearly, were not the types of 'deposit' contemplated by those two Ordinances.

7.5 The Board also agrees with the submission on behalf of the company that the fact that the word 'deposit' is used in the receipts does not mean that either the Securities Ordinance or the Deposit-taking Companies Ordinance intended to bring the deposits paid within section 28(1)(a) of the Inland Revenue Ordinance. The fact that, in the company's audited accounts, the words 'deposit' and 'interest' are used does not commit the company to the payment of tax on the interest received.

7.6 The Board agrees with the submission for the company: a particular word may have several interpretations and, when such a word is used in legislation, it has to be interpreted in the way which reflects the intent of the legislation. The Board is satisfied that the type of deposit made under the Securities Ordinance and the Commodities Trading Ordinance was not intended to be treated as a 'deposit' as that word is used in section 28(1)(a) of the Inland Revenue Ordinance.

8. DECISION

For the reasons given, the Board allows this appeal and discharges the assessments, to interest tax of the interest received by the company on the deposits made by the company with each of the Commissioner of Securities (pursuant to the Securities Ordinance) and the Commissioner of Commodities Trading (pursuant to the Commodities Trading Ordinance).