

**Case No. D11/06**

**Salaries tax** – home loan interest – a distinction between legal ownership and beneficial ownership – amount of deduction of mortgage interest paid in respect of a property held by the spouse of a joint-tenant – section 26E(1) of the Inland Revenue Ordinance ('the IRO').

Panel: Benjamin Yu SC (chairman), Ho Hin and Winnie Lun Pong Hing.

Date of hearing: 22 September 2005.

Date of decision: 25 April 2006.

Mr A (the appellant), the sole breadwinner of the family, is currently living with his wife ('Madam B'), their son and daughter and his mother-in-law ('Madam C') in a unit in a private development ('the Property'). The Property is and has since about January 1999 been registered in the names of Madam B and Madam C as joint tenants.

Prior to the acquisition of the Property, Madam C was a registered tenant in a public housing estate. She was able to obtain an interest free loan of \$800,000 from the Government for the purchase of a flat upon her surrender of her tenancy in the public housing estate. The purchase of the Property was funded by an interest free loan of \$800,000 borrowed by Madam C from the Government, a mortgage and the appellant's savings. Although all the mortgage instalments were all paid by the appellant, the appellant agreed to put his wife's name (Madam B) as a joint owner of the Property in order to give her a sense of security.

For the year of assessment 1999/2000, the appellant claimed in his return that his spouse was the 100% owner of the Property and claimed a deduction of \$153,000 by way of home loan interest. For the year of assessment 2000/01, the appellant claimed in his return that he was the 100% owner of the Property while his spouse was a 50% owner; and he claimed a deduction of \$100,000. Despite the apparent inconsistencies, the assessor did not raise any query at that time; but noted in the assessment that any deduction(s) allowed were subject to review and that home loan interest was restricted to taxpayer's ownership ratio or prescribed limit.

For the year of assessment 2003/04, the appellant claimed that 50% of the Property was held by him, and he claimed a deduction of \$50,000 for home loan interest. As the bank statement produced by the appellant to the revenue showed that a total sum of \$36,368.26 (including a small amount of overdue interest in the sum of \$31.94) was deducted from the joint account of Madam B and Madam C in respect of mortgage interest, the assessor only allowed 50% or the interest paid (less overdue interest) that is, \$18,168 by way of home loan interest.

(2006-07) VOLUME 21 INLAND REVENUE BOARD OF REVIEW DECISIONS

Upon further review, the assessor issued additional tax assessments in respect of the years of assessment 1999/2000 and 2000/01, the effect of which was to allow only 50% of the interest paid on the mortgage during those years of assessment. The Deputy Commissioner relied the previous decision of D22/04 and ruled that since 50% of the Property was held in the name of Madam B, the appellant was only entitled to deduct 50% of the interest referable to the payment of interest in respect of the 50% of the Property held in the name of his spouse, during the years of assessment 1999/2000, 2000/01 and 2003/04 ('the relevant years of assessment').

The issue in this appeal was therefore whether the appellant was entitled to deduct 100% of the interest he paid on a home mortgage, as he contended; or where he was only entitled to a deduction of 50% of the interest paid, as the Respondent contended.

**Held:**

1. The issue turned on the proper construction of section 26E of the IRO which draws a distinction between legal ownership and beneficial ownership of properties. In the Board's view, section 26E was concerned with legal, as opposed to beneficial, ownership in properties. This was evident from the use of the expression 'held by' in section 26E(2)(b)(i) and (ii), (2)(c)(i) and (ii) and (9)(i). Furthermore, legal ownership was a matter of title which could easily be ascertained. Beneficial ownership, on the other hand, could involve difficult questions of fact and law (D20/01 applied).
2. As the appellant and Madam B are not the legal owner of the whole of the Property (Madam B is one of the two joint tenants holding the Property), the Board came to a view that irrespective of where the beneficial ownership of the Property may lie (a matter on which the Board expressed no view), the Deputy Commissioner's Determination on the assessments and additional assessments for the relevant years of assessment was correct.

**Appeal dismissed.**

Cases referred to:

D22/04, IRBRD, vol 19, 163  
D20/01, IRBRD, vol 16, 187

Taxpayer in person.

Chan Siu Ying and Chan Wai Yee for the Commissioner of Inland Revenue.

**Decision:**

1. Mr A ('the taxpayer') appeals against the determination made by the Deputy Commissioner dated 30 May 2005 which overruled the taxpayer's claim of deduction in respect of home loan interest for the years of assessment 1999/2000, 2000/01 and 2003/04 ('the relevant years of assessment').

2. The issue in this appeal is whether the taxpayer is entitled to deduct 100% of the interest he paid on a home mortgage, as he contends; or whether he is only entitled to a deduction of 50% of the interest paid, as the Respondent contends. The issue turns on the proper construction of section 26E of the **Inland Revenue Ordinance**.

3. The relevant facts are not in dispute. The taxpayer himself gave evidence before us. There is no challenge to his evidence. We find the following facts proved.

4. The taxpayer is married to a Madam B. He is currently living with his wife, their son and daughter and his mother-in-law ('Madam C') in a unit in a private development called the Private Estate D, in District E ('the Property').

5. The Property is and has since about January 1999 been registered in the names of Madam B and Madam C as joint tenants.

6. Prior to the acquisition of the Property, Madam C was a registered tenant in a public housing estate. She was able to obtain an interest free loan of \$800,000 from the Government for the purchase of a flat upon her surrender of her tenancy in the public housing estate.

7. The \$800,000 thus borrowed from Government was used as part of the consideration for the purchase of the Property. The rest of the consideration money was funded by a mortgage and from the taxpayer's savings.

8. The taxpayer is the sole breadwinner of the family. The mortgage instalments were all paid for by the taxpayer. He agreed to put his wife's name as a joint owner of the Property in order to give her a sense of security.

9. For the year of assessment 1999/2000, the taxpayer claimed in his return that his spouse was the 100% owner of the Property and claimed a deduction of \$153,000 by way of home loan interest. For the year of assessment 2000/01, the taxpayer claimed in his return that he was the 100% owner of the Property while his spouse was a 50% owner. He claimed a deduction of \$100,000. Despite the apparent inconsistencies, the assessor did not raise any query with the

(2006-07) VOLUME 21 INLAND REVENUE BOARD OF REVIEW DECISIONS

taxpayer at the time. It is, however, fair to observe that the assessor noted in the assessment that any deduction(s) allowed are subject to review and that home loan interest is restricted to taxpayer's ownership ratio or prescribed limit.

10. In December 2004, the taxpayer filed his return for the year of assessment 2003/04. He claimed in that return that 50% of the Property was held by him, and he claimed a deduction of \$50,000 for home loan interest. The bank statement produced by the taxpayer to the revenue shows that during that year of assessment, a total sum of \$36,368.26 was deducted from a joint account of Madam B and Madam C in respect of mortgage interest, which sum included a small amount of overdue interest (\$31.94). The assessor only allowed 50% of the interest paid (less overdue interest) that is, \$18,168 by way of home loan interest.

11. Upon further review, the assessor issued additional tax assessments in respect of the years of assessment 1999/2000 and 2000/01, the effect of which was to allow only 50% of the interest paid on the mortgage during those years of assessment.

12. The Deputy Commissioner relied on a previous decision of this Board, viz D22/04, IRBRD, vol 19, 163 and ruled that since 50% of the Property was held in the name of Madam B, the taxpayer is only entitled to deduct 50% of the interest referable to the payment of interest in respect of the 50% of the Property held in the name of his spouse, Madam B, during the relevant years of assessment.

13. Section 26E provides as follows:

*'(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 purpose 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 home loan interest shall be allowable to that person for that year of assessment.*

*(2) (a) Subject to paragraphs (b) and (c) and subsection (3), a deduction allowable to a person under subsection (1) in respect of any home loan interest paid by the person during any year of assessment shall be –*

*(i) (A) where the dwelling is used by the person exclusively as his place of residence during the whole of that year of assessment, the amount of the home loan interest paid; or...*

*(b) For the purpose of this section, where a dwelling is held by a person otherwise than as a sole owner, the amount of the home*

(2006-07) VOLUME 21 INLAND REVENUE BOARD OF REVIEW DECISIONS

*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 tenants each in proportion to the number of the 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.*
- (c) For the purposes of paragraph (a), where a dwelling is held by a person otherwise than as a sole owner, the relevant amount specified in Schedule 3D referred to in paragraph a(ii) shall be regarded as having been reduced –*
- (i) where the dwelling is held by the person as a joint tenant, in proportion to the number of the joint tenants; or*
  - (ii) where the dwelling is held by the person as a tenant in common, between the tenants in common each in proportion to his or her share in the ownership in the dwelling.’...*

(9) ‘home loan’ 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.*

14. The law draws a distinction between legal ownership and beneficial ownership of properties. Sometimes, a person is both the legal and beneficial owner of a property. Sometimes, the legal ownership is vested in one person whilst the beneficial interest belongs to another. In our view, section 26E is concerned with legal, as opposed to beneficial, ownership in properties. This

(2006-07) VOLUME 21 INLAND REVENUE BOARD OF REVIEW DECISIONS

is evident from the use of the expression 'held by' in section 26E(2)(b)(i) and (ii), (2)(c)(i) and (ii) and (9)(i). Furthermore, legal ownership is a matter of title which can easily be ascertained. Beneficial ownership, on the other hand, could involve difficult questions of fact and law. It is rather unlikely that these provisions could have been intended to require the ascertainment of beneficial ownership in every case. In D20/01, IRBRD, vol 16, 187 the Board came to the same conclusion. The Board observed:

*'The Taxpayer's position is governed by section 26E(2)(c)(i). The Flat is held by her and Mr B as joint tenants. Her entitlement is to claim the amount specified in Schedule 3D (that is \$100,000) reduced 'in proportion to the number of the joint tenants'. The section does not provide for reduction in any other manner. In particular, the section does not contemplate reduction in proportion to the beneficial interests of the joint tenants. The contrast in wordings between section 26E(2)(b)(i) and 26E(2)(c)(i) on the one hand and section 26E(2)(b)(ii) and 26E(2)(c)(ii) makes the position very clear.'*

15. In the present case, the taxpayer and his spouse, Madam B, are not the legal owner of the whole of the Property, Madam B is one of the two joint tenants holding the Property. That being the case, we are of the view that irrespective of where the beneficial ownership of the Property may lie (a matter on which we express no view), the Determination on the assessments and additional assessments for the relevant years of assessment is correct. In the circumstances, we would dismiss the appeal and confirm the assessments determined by the Deputy Commissioner.