

INLAND REVENUE BOARD OF REVIEW DECISIONS

Case No. D2/01

Salaries tax – deductions – home loan interest – premium on Hong Kong Housing Authority flat – section 26E of the Inland Revenue Ordinance (‘IRO’).

Panel: Ronny Wong Fook Hum SC (chairman), David Lee Tai Wai and Lily Yew.

Date of hearing: 8 January 2001.

Date of decision: 9 April 2001.

The taxpayer purchased a flat from the Hong Kong Housing Authority in 1992, the consideration of which was lower than the full market value. Restrictions on alienation of the flat by the taxpayer were attached. In mid-1996, the taxpayer paid a premium assessed by the Hong Kong Housing Authority thus enabling him to have the alienation removed.

The taxpayer financed payment of the premium by a loan and argued that the premium was in essence a deferred payment for part of the purchase price for the flat. The taxpayer contended that he was entitled to deduct home loan interest under section 26E of the IRO.

Held:

The crucial question is whether the loan was a loan of money which was applied wholly or partly for the acquisition of a dwelling. The sum was applied for the purpose of removing the restriction on alienation. The restriction does not in any way hinder his use of the flat as his dwelling. It was not applied for the acquisition of a dwelling.

Appeal dismissed.

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Ma Wai Fong for the Commissioner of Inland Revenue.

Taxpayer in person.

Decision:

Background

1. At all material times, the Taxpayer is a Government employee working in Department A.

2. By an assignment dated 20 October 1992 (' the Assignment') between the Hong Kong Housing Authority (' the Authority') as vendor and the Taxpayer and Madam B as purchasers, in consideration of \$227,300, the Authority assigned in favour of the Taxpayer and Madam B as joint tenants the Flat. The Assignment provides as follows:

- (a) By Recital 5 that the Assignment is subject to the terms, covenants and conditions mentioned in the Schedule to the Housing Ordinance (Chapter 283).
- (b) By clause 4 that the parties agreed ' that the full market value of the said premises as at the date of sale is \$390,900.'

Madam B is the mother of the Taxpayer.

3. Paragraph 1 of the Schedule to the Housing Ordinance provides:

' 1. Subject to paragraph 4 of this Schedule, the purchaser shall not at any time alienate ... the land sold other than to the Authority ... unless –

(a) either –

(i) a period of 5 years has elapsed from the date of the first assignment of the land –

(A) from the Authority to any purchaser; or

(B) to any purchaser nominated by the Authority,

whichever is the earlier; or

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- (ii) *before the period has elapsed, the purchaser has offered to assign the land to the Authority and the Authority or its nominee ... has declined to accept the assignment; and*
- (b) *the purchaser has first paid to the Authority the amount of the premium calculated under the following formula –*

$$\text{Premium} = \frac{\text{Prevailing market value} - (\text{Initial market value} - \text{Purchase price})}{\text{Initial market value}}$$

4. Madam B passed away on 6 February 1994. The Flat became vested in the Taxpayer as the survivor of the joint tenants.
5. In relation to the consideration of \$227,300 paid by the Taxpayer and Madam B under the Assignment, this was financed in part by a loan of \$200,000 from a finance company, Company C. This loan was completely discharged by November 1995.
6. In about mid-1996, the Taxpayer applied to the Authority for assessment of premium under paragraph 1 to the Schedule of the Housing Ordinance. By a letter dated 7 June 1996, the Authority informed the Taxpayer that premium was assessed at \$807,746. The Taxpayer duly paid the premium so assessed. By a letter dated 15 July 1996, the Authority informed the Taxpayer ‘that the alienation restrictions as specified under the Schedule to the Housing Ordinance ... are removed.’
7. The Taxpayer financed payment of the premium by a loan of \$770,000 from another finance company, Company D. This loan was repayable by 120 monthly instalments of \$9,859 each.
8. On or about 29 July 1996, approval was given to the Taxpayer to receive home purchase allowance in respect of Property 1 under the terms and conditions of the Home Purchase Scheme annexed to the Civil Service Branch Circular No 22/93 dated 30 December 1993 (‘the Circular’). The Taxpayer was asked to send a ‘record of owners’ certified by his solicitor to prove his purchase and ownership of the Flat. We have not been supplied with a copy of the Circular nor have we been furnished with the Taxpayer’s correspondence with the Director of Accounting Services proving his purchase and ownership of the Flat. It is however not disputed that as from 1 August 1996, the Taxpayer received home purchase allowance in the sum of \$7,030.
9. The issue before us is whether the Taxpayer is entitled to deduct home loan interest under section 26E of the IRO.

Relevant provisions in the IRO

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10. Section 26E(1) provides:

‘(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.’

11. Section 26E(9) provides:

‘In this section -

“dwelling” means any building or any part of a building –

(a) which is designed and constructed for use exclusively or partly for residential purposes; and

(b) ...

“home loan”, in relation to 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.’

Sworn testimony of the Taxpayer

12. The Flat had been his residence since about April 1983.

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13. He drew our attention to clause 4 of the Assignment. He argued that the premium of \$807,746 is in essence part of the purchase price for the Flat.

14. He explained that he applied for assessment of premium as he was told that the home purchase allowance would only be available to him if the restriction on alienation over the Flat is removed.

Our decision

15. The crucial question is whether the loan of \$770,000 from Company D was a loan of money which was applied wholly or partly for the acquisition of a dwelling. The Revenue contends that it was not. On the Taxpayer's admission, the Flat had been his dwelling since April 1983. The sum of \$770,000 was applied for the purpose of removing the restriction on alienation. It was not applied for the acquisition of a dwelling. The Taxpayer contends that it was. The Taxpayer submitted that the loan went towards discharge of \$807,746 which in essence is the difference between the consideration paid under the Assignment and the market value of the Flat as at the date of the Assignment. He was merely paying on a deferred basis the balance of the purchase price for the Flat.

16. We agree with the contentions of the Revenue. The Taxpayer acquired the Flat as his dwelling in 1982. He did use the Flat as his dwelling and would be able to continue such usage without taking any other step. At the price paid, his acquisition was saddled with a restriction on alienation. That restriction does not in any way hinder his use of the Flat as his dwelling. The premium paid did not acquire a new dwelling. What he did acquire via the premium was the right to alienate a flat which has always been his dwelling. We reject the Taxpayer's contention that the premium was in essence deferred consideration for the Flat. His initial purchase was at a consideration tied to restriction on alienation. The premium was not payment of deferred consideration for the acquisition of the Flat. The premium was the consideration for removal of the restriction over his subsisting dwelling.

17. For these reasons, we dismiss the Taxpayer's appeal and confirm the assessment.