Case No. D49/12

Property tax – tenancy agreement terminated by agreement within first month – whether tenancy agreement void *ab initio* – whether property tax chargeable to the whole month – whether Commissioner could change its position on assessment after lodging of grounds of appeal – whether authorities in the United Kingdom regarding apportionment applicable to the Board – sections 3 and 4 of Apportionment Ordinance (Cap 18) – sections 5, 5B and 68 of the Inland Revenue Ordinance (Cap 112) ('the IRO').

Panel: Chow Wai Shun (chairman), Ho Chi Wai and Liu Man Kin.

Date of hearing: 26 November 2012.
Date of decision: 7 February 2013.

The Appellants were spouses and owners of a property ('the Property'). By a tenancy agreement ('Tenancy Agreement'), they let the Property to a tenant for a term of two years. Under the Tenancy Agreement, (a) after the first year, both the Appellants and tenant could terminate by giving two months' written notice; (b) rent had to be paid in advance on the first and second day each month. Twenty-six days after the entering into of the Tenancy Agreement, the tenant entered into another agreement with the first Appellant for early termination of the Tenancy Agreement ('Termination Agreement'), under which the tenant would deliver vacant possession to the Appellants on the same day and rental deposit and rent paid for the first month would be forfeited as compensation.

The Commissioner assessed property tax on the Appellants by apportioning the monthly rent under the Tenancy Agreement by 26 days out of 31 days. The first Appellant objected to the assessment, and the Commissioner proposed to revise the assessment which the first Appellant did not accept. The first Appellant appealed against the determination, contending that: (i) the Tenancy Agreement was made on a monthly basis and so there was no daily rent; (ii) as reflected in the Termination Agreement, the amount forfeited represented compensation for the tenant's breach of the Tenancy Agreement; (iii) as soon as the breach occurred, the Tenancy Agreement was revoked as if it were not in existence from the beginning. Hence, no part of the amount forfeited was assessable for property tax.

Subsequent to the Grounds of Appeal being lodged, the Commissioner revised the assessment and the entire amount of rent paid in advance (instead of the rent of 26 days) was assessed for property tax.

Held:

Substantive appeal

1. Where a contract was terminated by agreement or for breach, the contract was not rescinded *ab initio* as if it had never been made. The Tenancy Agreement had been effective at all relevant times until it was breached. The Appellants received the deposit and the rent in advance, and the tenant was given the keys to the Property, which represented possession of the same, on the basis of the Tenancy Agreement. The Termination Agreement could not be construed to have altered the nature of those receipts. (Johnson v Agnew [1980] AC 367 considered)

2. The rent paid in advance for the first month was paid in consideration for the right of use of the Property for the first month. Hence, it was assessable to property tax.

3. The Commissioner, even in argument before the Board, was not bound by the reasons set out in the determination and could introduce new reasons to justify the assessment. The Board's function in an appeal was to consider the matter *de novo* and was obliged to make a general review of the correctness of the assessment. (D27/91, IRBRD, vol 6, 65 and Shui On Credit Co Ltd v CIR [2009] 12 HKCFAR 392 considered)

4. Sections 3 and 4 of the Apportionment Ordinance were relevant. If the provision did not apply, the one-month rent paid to the Appellants would not be apportioned. Since the Hong Kong provision was identical to the UK, the UK authorities equally applied to Hong Kong and the present case. Thus, where rent was payable, the whole amount of rent for that period was still recoverable from the tenant. The Tenancy Agreement did not provide the otherwise. Therefore, the whole amount of rent paid in advance should be assessed in full. (Ellis v Rowbotham [1900] 1 QB 740 and William Hill (Football) Ltd v Willen Key & Hardware Ltd 108 Sol Jo 482 considered)

Costs order

5. The present case was a simple one involving a small amount of money. No arguable case had been put forward by the Appellants. The case could have been resolved earlier on without going to the Board. The appeal was unmeritorious and frivolous. It was a complete waste of time and resources of the Board.

Appeal dismissed and costs order in the amount of $5,000 imposed.

Cases referred to:

Ellis v Rowbotham [1900] 1 QB 740
William Hill (Football) Ltd v Willen Key & Hardware Ltd 108 Sol Jo 482
Johnson v Agnew [1980] AC 367
D27/91, IRBRD, vol 6, 65
Shui On Credit Co Ltd v CIR [2009] 12 HKCFAR 392

Taxpayer in person.
Ng Sui Ling and Fung Ka Leung for the Commissioner of Inland Revenue.

Decision:

1. This is an appeal against the determination of the Deputy Commissioner of Inland Revenue dated 23 March 2012 ('the Determination').

2. Only Appellant 1 signed the notice and statement of the grounds of appeal. He appeared in person and for and on behalf of Appellant 2 at the hearing. This Board, as a preliminary matter, asked Appellant 1 if any written authorization had been received from Appellant 2. Appellant 1 said no but also said that the authority was given orally. The Respondent raised no concern over this matter. Given the relationship between the Appellants (as disclosed below in paragraph 3(a) and their previous conduct relating to this matter, we considered that Appellant 1 at least had the ostensible authority to act for and on behalf of Appellant 2. In case we were wrong, Appellant 2 had not lodged any appeal against the Determination. In any event, it would not affect the outcome of this appeal.

3. The Appellants raised no dispute to the facts upon which the Determination was arrived at and gave no further oral evidence. On such basis, and having considered all documentary evidence sent to the Board before the hearing, we find the following facts as facts relevant to these appeals:

(a) The Appellants are husband and wife. At all relevant times they were the owners of the property at Address A ('the Property').

(b) By a tenancy agreement dated 29 December 2008 ('the Tenancy Agreement'), the Appellants let the Property to a tenant at a monthly rent of $36,000 for a term of two years from 16 January 2009 to 15 January 2011. The Tenancy Agreement provided, inter alia, that from 16 January 2010, both the Appellants and the tenant could terminate the lease by giving to the other party two months' written notice.

(c) Upon signing the Tenancy Agreement, the Appellants acknowledged receipt of the rental deposit of $72,000 and the rent of $36,000 for the

first month of the lease from the tenant.

(d) On perusal of the Tenancy Agreement, this Board also found that under Clause 10, the parties agreed that rent had to be paid in advance. The original wordings in Chinese are:

'在租約期內，該物業之租金必須在每月起租時之第壹日或第貳日繳納．．．．．．'

(e) On 10 February 2009, the tenant entered into an agreement ('the Termination Agreement') with Appellant 1 for the early termination of the Tenancy Agreement. Pursuant to the Termination Agreement, the tenant would deliver vacant possession of the Property to the Appellants on 10 February 2009 and the rental deposit and the rent paid for the first month of the lease would be forfeited as compensation to the Appellants.

(f) A Property Tax Return was issued to the Appellants for the year of assessment 2008/09 but was returned to the Inland Revenue Department uncompleted. In the absence of a completed Property Tax Return, the Assessor raised on the Appellants the following estimated Property Tax assessment for the year of assessment 2008/09:

	$
Assessable value	90,580
Less: 20% statutory allowance for repairs and outgoings	(18,116)
Net assessable value	72,464
Tax payable thereon	10,869

(g) Appellant 1 objected and furnished the Property Tax Return in order to validate the objection. The Assessor accepted that the rental deposit and the amount originally paid for the period from 11 February 2009 to 15 February 2009 forfeited were not taxable and proposed to revise the assessment as follows:

	$
Rental income ($36,000 [Paragraph 3(c)] x 26/31)	30,193
Less: 20% statutory allowance for repairs and outgoings	(6,039)
Net assessable value	24,154
Tax payable thereon	3,623

(h) Appellant 1 refused to accept the proposal and continued the objection.

4. As stated in the Grounds of Appeal, it is the Appellants' case that the Tenancy Agreement was made on a monthly basis and so there was no daily rent as such. A tenancy

period of 26 days only (from 16 January 2009 to 10 February 2009), therefore, did not exist under the Tenancy Agreement. It is also the Appellants' main argument that as reflected in the Termination Agreement, the amount forfeited represented compensation for the tenant's breach of the Tenancy Agreement. The Appellants also contended that as soon as the breach occurred, the Tenancy Agreement was revoked as if it were not in existence from the very beginning. As a result, the Appellants argued, no part of the amount forfeited was assessable for property tax.

5. By a letter dated 15 November 2012, the Respondent informed the Appellants that on further legal advice (see paragraph 7 below), it was then considered that the entire amount of rent paid in advance (that is $36,000) should be assessed and hence the revised assessment as follows:

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Rental income	36,000
Less: 20% statutory allowance for repairs and outgoings	(7,200)
Net assessable value	28,800

The statutory provisions

6. We find the following sections of the Inland Revenue Ordinance relevant to the this appeal:

(a) Section 5

'*(1) Property tax shall, ……, be charged for each year of assessment on every person being the owner of any land or buildings…… wherever situate in Hong Kong and shall be computed at the standard rate on the net assessable value of such land or buildings……*'

(1A) …… net assessable value means the assessable value of land or buildings…… ascertained in accordance with section 5B –

……

(b) less –

i. where the owner agrees to pay the rates in respect of the land or buildings…… those rates paid by him; and

ii. an allowance for repairs and outgoings of 20% of that assessable value after deduction of any rates under subparagraph (i).'

(b) Section 5B

'…..

(2) The assessable value of land or buildings…… for each year of assessment shall be the consideration, in money or money's worth, payable in that year to, to the order of, or for the benefit of, the owner in respect of the right of use of that land or buildings……'

…..

(6) In this section, consideration includes any consideration payable in respect of the provision of any services or benefits connected with or related to the right of use.'

(c) Section 68

' ……

(4) The onus of proving that the assessment appealed against is excessive or incorrect shall be on the appellant.'

7. Regarding the latest change of position by the Respondent as set out in paragraph 5 above, this Board accepts the Respondent's submission that section 3 of the Apportionment Ordinance is relevant to this case. Indeed, this Board finds section 4 of the said Ordinance also relevant. The two provisions read:

'3. All rents…… shall…… be considered as accruing from day to day, and shall be apportionable in respect of time accordingly.

4. The apportioned part of any such rent…… shall be payable or recoverable, …... when the next entire portion of the same would have been payable…… and not before.'

On this point, the Respondent also referred this Board to section 2 of the UK Apportionment Act and decisions of the UK courts which held that the UK provision applies only where rent is payable in arrears, not in advance.[1]

The Appellant's submission

8. In his submission at the hearing, Appellant 1 reiterated his main argument. He did confirm that the keys to the Property were delivered to the tenant on 16 January 2009 and not returned to him until 10 February 2009. However, the Appellants were not aware of

[1] Ellis v Rowbotham [1900] 1 QB 740 and William Hill (Football) Ltd v Willen Key & Hardware Ltd 108 Sol Jo 482.

when the tenant moved in. From what he knew and told this Board, the tenant did move in but moved out just a few days afterwards.

9. In his reply, Appellant 1 put forward a number of hypotheticals. In each of those hypotheticals, he asked what would happen if the innocent landlord refunded part of the rent already paid for the month during which the tenant defaulted. Certainly the Respondent needed not provide an answer on the spot. None of those hypotheticals, however, resembled the facts of the case before this Board since the Appellants forfeited ***all*** the money already paid (emphasis added).

Our analysis

10. The Appellants' contention that the Tenancy Agreement was breached and revoked as if it were not in existence from the very beginning is conceptually unconceivable and wrong. When there is no contract, there cannot be a breach of contract; when there is no breach, there cannot be a right for damages (or compensation) for breach. If the Tenancy Agreement were considered as if it had never been entered into, the parties' respective positions should have been put back to square one, no more no less.

11. Therefore, this Board accepts the Respondent's submission that where a contract is terminated by agreement or for breach, the contract is not rescinded *ab initio* as if the contract had never been made.[2] As such, the Tenancy Agreement had been effective at all relevant times until it was breached. The Appellants received the deposit and the rent in advance, and the tenant was given the keys to the Property which represented possession of the same, on the basis of the Tenancy Agreement. The subsequent Termination Agreement cannot be construed to have altered the nature of those receipts.

12. The Respondent has dropped his pursuit over the deposit in the Determination, which this Board agrees. He did not pick this up again in his latest position set out in paragraph 5 above, which this Board also agrees. The remaining issue therefore is whether the rent in advance, and if so, how much of it, is assessable to property tax.

13. Regarding the latest change of position by the Respondent, this Board cannot find any statutory prohibition against it. Indeed pursuant to D27/91, IRBRD, vol 6, 65, the Commissioner, even in argument before the Board, is not bound by the reasons set out in the determination and can introduce new reasons to justify the assessment. In this regard, this Board also accepts the Respondent's submission that the Board's function, on hearing an appeal, is to consider the matter *de novo*,[3] and that is to say that this Board is obliged to make a general review of the correctness of the assessment.

14. Under the Tenancy Agreement, rent is payable in advance. The rent paid in advance for the first month of the lease was paid in consideration for the right of use of the Property for the first month from 16 January 2009. As such, this Board holds that it is

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2 Johnson v Agnew [1980] AC 367.

3 Shui On Credit Co Ltd v CIR [2009] 12 HKCFAR 392.

assessable to property tax.

15. The tenant gave up possession before the end of the first month of the lease. This Board accepts the Respondent's submission that section 3 of the Apportionment Ordinance is relevant to be considered. If the provision does not apply, the one-month rent paid to the Appellants will not be apportioned. Since the Hong Kong provision is identical to the UK one, this Board accepts the Respondent's submission that the UK case law authorities equally apply to Hong Kong and, specifically, to this case. This means that where rent is payable in advance but the lease ends before the end of the period for which rent is payable, the whole amount of rent for that period is still recoverable from the tenant. The Tenancy Agreement did not provide anything to the otherwise. Therefore, the whole amount of rent paid in advance should be assessed in full.

Conclusion

16. On the basis of the above, we dismiss the appeal and agree with the Respondent on his latest position taken as set out in paragraph 5 above.

Cost order

17. We asked Appellant 1 for submission on why a cost order under section 68(9) of the Inland Revenue Ordinance should not be made against him. The section empowers the Board to order an appellant to pay as costs of the Board a sum not exceeding the amount specified in Part 1 of Schedule 5[4] which shall be added to the tax charged and recovered therewith where the Board does not reduce or annul the assessment being appealed.

18. Appellant 1 contended that it would be unfair to the Appellants since the statutory provisions as well as the legal principles were too difficult for lay people like them to apprehend and understand but the amount involved was so small that it would be unreasonable to retain professional help. He protested that even the Respondent had got it wrong until shortly before the hearing. He also complained that the case had been dragged on for unreasonably long.

19. Even though there might have been some truth in the points raised, this Board finds no sympathy on the Appellants. This is a simple case involving a small amount of money. No arguable case has ever been put forward by the Appellants, both in writing and in oral submission at the hearing. The case can, and should, have been resolved earlier on, without going to the Board. The appeal is unmeritorious and frivolous. It is a complete waste of the time and resources of the Board. Accordingly, this Board decides to make a cost order under section 68(9) of the Ordinance against the Appellants and the sum is $5,000.

[4] Currently $5,000.