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Founded in 1913

# 香港華人會計師公會 The Society of Chinese Accountants & Auditors

(在香港註冊成立之有限公司)

(Incorporated in Hong Kong as a company limited by guarantee)

12 February 2014

Mr. TSANG Chun Wah, John, GBM, JP  
The Financial Secretary  
Government of the Hong Kong Special Administrative Region  
The People's Republic of China

Dear Sir,

## **Budget Submission**

The Society of Chinese Accountants and Auditors was formed in 1913 and incorporated in 1948. We have over 1,000 members representing hundreds of Certified Public Accountants ("CPA") firms in Hong Kong. The CPA firms of which our members are partners, directors or managers, service a significant majority of businesses in Hong Kong, and also companies investing into or through Hong Kong. Our members directly and regularly communicate with clients, their directors and employees and consequentially understand their needs and concerns.

Presently Hong Kong is facing high inflation and an unstable economy. It is therefore important for the government to plan carefully for the future of Hong Kong.

It is with this in mind that we herewith submit our views for your consideration.

## **CARING FOR THE INDIVIDUALS**

### **1. WIDENING THE TAX BANDS**

Under the present Salaries Tax regime, there is a progressive rate levied on assessable income after the deduction of allowances. However, these progressive rate bands have not been reviewed since the tax year 2008/09. With the increasing cost of living and the implementation of the minimum wages scheme, the level of wages earned by taxpayers has increased and, as a result, many middle class salary earners paid tax at 17% on their marginal income.



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### RECOMMENDATIONS -

- Raising the tax band from the present level of \$40,000 to \$50,000 to relieve the tax burden of the sandwich class taxpayers and to enable them to share the benefit of our economic growth amidst the pressure of rising inflation.

## 2. INCREASING THE BASIC ALLOWANCE, MARRIED PERSON'S ALLOWANCE AND CHILD ALLOWANCE FOR SALARIES TAX AND PERSONAL ASSESSMENT

We notice that the increase in Basic/Married Allowances in the last few years fell short of the inflation:

<u>Year of</u>	<u>Inflation</u>	<u>Basic Allowance</u>		<u>Child Allowance</u>	
<u>Assessment</u>	<u>Increase</u>	<u>Amount</u>	<u>Increase</u>	<u>Amount</u>	<u>Increase</u>
2010/11	4.5%	108,000	0	50,000	0
2011/12	5.3%	108,000	0	60,000	20%
2012/13	4.1%	120,000	11%	63,000	5%
2013/14	4.3%	120,000	0	70,000	11%

We understand that there is not necessarily a correlation between tax allowances and inflation. However, we submit that taxpayers should not be asked to shoulder an unnecessary burden when there was fiscal surplus. There is therefore a need to adjust Basic/Married Allowance to cope with inflation.

We admit that you have been fairly generous on reviewing Child Allowance. Certainly you are aware of the cost of upbringing a child and we submit that there is still room for further adjustments. On the other hand, Dependent Brother/Sister Allowance used to be 60% of Child Allowance before the year of assessment 2010/11, we therefore suggest that Dependent Brother/Sister Allowance should likewise be adjusted.

### RECOMMENDATIONS -

- Increasing the Basic Allowance to \$140,000 per year and the Married Person's Allowance to HK\$280,000 per year;
- Increasing the Child Allowance to \$75,000 per year for each child;
- Increasing the Dependent Brother / Sister Allowance to \$45,000 for each dependent brother/sister.



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### 3. RELAXING THE ENTITLEMENT TO ADDITIONAL DEPENDENT PARENT AND DEPENDANT GRANDPARENT ALLOWANCES

At present, Additional Dependent Parent and Dependent Grandparent Allowances can only be claimed by taxpayers living together with their parents or grandparents. We fully appreciate that this special requirement aims at encouraging the younger generation to take care of their parents and/or grandparents. However, with the high property prices, the floor area affordable by the younger generation gets smaller and smaller. Forcing the younger and the elder generations to live together in a small apartment may create tensions between the generations and may lead to other social problems. There is a Chinese saying, “It’s fine to meet each other but difficult to live together” (“相見好, 同住難”). Many taxpayers choose to rent or purchase separate quarters for their parents/grandparents.

#### RECOMMENDATIONS -

- Extending Additional Dependent Parent and Dependent Grandparent Allowances to taxpayers who have provided living quarters for their parents and/or grandparents, either by renting or purchasing separate properties.

### 4. PROVIDING RELIEF FOR HIGH MEDICAL COSTS

With the aging population in Hong Kong, it is important that those who can afford to seek private medical help be encouraged to shoulder part of the responsibilities by going to private hospital instead of drawing on public resources by going to public hospitals.

In addition, while taxpayer is given additional allowances for maintaining **disabled dependents**, he is not given similar allowance if he is himself a disabled person. To encourage disabled persons to rejoin the work force and to enhance their self-esteem, we proposed to introduce a new “Disabled Person’s Allowance”.

#### RECOMMENDATIONS –

- Introducing a new “Disabled Person’s Allowance” for disabled taxpayers;
- Introducing a new Serious Illness Allowance;
- Providing deduction up to a maximum of \$30,000 per annum for Medical Insurance Premium or medical expenses;
- Increasing the Health Care Voucher amount to \$5,000 per annum.



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### 5. SUPPORTING YOUNG PARENTS – Increasing the New Born Baby Child Allowance and Introducing a new Child Education (Textbooks) Allowance

The Hong Kong population is expected to remain on an aging trend. From the Hong Kong Statistics Press Releases, the proportion of population aged 65 or above is projected to increase from 13% in 2011 to 30% in 2040. Hong Kong's birth rate, on the other hand, has continued to decline in the last two decades.

The aging problem will generate social and economic challenges to our society, such as low productivity level, increase in social welfare expenses, increase in infrastructure spending, etc. The Government should take measures to encourage Hong Kong residents to expand their family in order to sustain our economic competitiveness in the upcoming years.

#### RECOMMENDATIONS –

- Increasing the New Born Baby Child Allowance by HK\$80,000 if the baby is born in a Public Hospital (i.e. for taxpayers who are already benefitting from government support); HK\$150,000 if the baby is born in a Private Hospital, to encourage the mother-to-be to attend Private Hospitals instead of Public Hospitals;
- Introducing a new Child Education (Textbooks) Allowance of HK\$10,000 per child.

### 6. INCREASING THE TIME LIMIT AND THE MAXIMUM AMOUNT OF HOME LOAN INTEREST

As a result of the sky-rocketing property prices in recent years, taxpayers can hardly finance the purchase of properties with 10-year mortgage terms. Although property prices are expected to decline, the present property prices still pose difficulties for young couples. To assist them on their home purchases and to relieve the burden of middle income earners on home mortgage loan, the home loan interest deduction should be reviewed.

#### RECOMMENDATIONS –

- Extending the entitlement of home loan interest deduction to 25 years;



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### 7. PROVIDING RELIEF FOR HIGH RENTAL EXPENSES

On the other hand, there are many taxpayers who cannot afford to purchase any property and opt to rent rather than purchase their residential property. Although the Government wishes to keep property prices at an affordable level, these measures may not take effect immediately.

#### RECOMMENDATIONS -

- Introducing a Home Rental Allowance for 2 years for an amount up to HK\$100,000 per year.

### CARING FOR THE EMPLOYERS

### 8. BUSINESS REGISTRATION FEE

Under the current inflationary economy, the Government should continue to attract investors to carry on business in Hong Kong and to help reduce the burden of small and medium sized businesses.

#### RECOMMENDATIONS -

- Extending the waiver of business registration fee for three years.

### 9. CHARITABLE DONATIONS

Donations to charitable institutions may partially release the financial burden on the Government to additional demands from the education and social welfare sectors during years of economic downturns. The present tax deduction provision however discourages regular donors to continue to contribute to these social responsibilities in a loss year.

#### RECOMMENDATIONS -

- Allowing deduction of up to 50% of the income or assessable profit of the taxpayer for approved charitable donations;
- Allowing deductible donations to be added to the loss and be able to be carried forward in the year when the taxpayer incurred losses. In the circumstances, the allowable donations may be limited to the average of the donation made by the taxpayer in the past 5 years.
- Exempting the Buyer's Stamp Duty of purchasing properties by charitable organizations.



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### 10. GROUP LOSS RELIEF AND LOSS CARRY-BACK

There have been public outcries for group loss relief and loss carry-back for many years. We believe that it is time for the Government to respond to the public's requests.

Our neighboring areas, such as Singapore and Japan, have adopted group loss relief or similar system. Hong Kong has placed itself in a global tax and economic disadvantage in comparison with our competitors.

Taxpayers are obliged to pay tax on profit made during a year. However, loss results in subsequent years cannot be carried backward and will be forfeited upon cessation of business. In order to assist small and medium enterprises to survive through the current unstable economic conditions and to provide a more favourable tax environment to attract potential investors, we suggest that the Government should consider granting tax relief for carrying back losses.

#### RECOMMENDATIONS –

- Introducing new legislation allowing group loss transfer;
- Allowing current year loss to be carried back for setting off the profits of the last two years.

### 11. MAINTAINING TAX NEUTRALITY, EQUITY AND SIMPLICITY

In the past months, there were waves of discontentment, resistances and challenges in Hong Kong. It is therefore vital that an efficient and fair tax system be established to stimulate economic activities while distributing the resources on a fair and equitable basis.

Neutrality, equity and simplicity are general tax principles emphasized by Adam Smith in his well-known book: "The Wealth of Nation". It was quoted in a research paper, "Tax Policy for Developing Countries", published by the IMF in March 2001. (The original paper can be found at: <http://www.imf.org/external/pubs/ft/issues/issues27/index.htm>)

S. 16 of the Inland Revenue Ordinance provides that *"In ascertaining the profits in respect of which a person is chargeable to tax under this Part for any year of assessment **there shall be deducted all outgoings and expenses** to the extent to which they are incurred during the basis period for that year of assessment by such person in the production of profits in respect of which he is chargeable to tax under this Part for any period....."*



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However, the provisions for outgoings and expenses deductions for taxpayers that pay Property Tax and Salaries Tax are less generous. Our tax law is therefore not neutral.

### Property Tax

As stated previously, many baby boomers will be retiring from the workforce and are in the stage of planning for their retirements. Holding properties to earn income is becoming a simple and viable investment to maintain a steady income during their retirement days. In the 2009-10 Budget, you proposed to launch an “Operation Building Bright” to assist owners of old buildings to carry out repair works. Obviously, you recognize that repairing cost is a heavy burden to house owners, yet our present tax law only allows deduction equal to 20% of the rental income. The different deduction provisions have prompted taxpayers to seek reporting their rental income under Profits Tax (e.g. D122/02 IRBRD Volume 18; D14/09 IRBRD Volume 24, 2<sup>nd</sup> supplement). We submit that allowing taxpayers to choose to deduct the actual cost incurred in earning the rental income should achieve fairness and equity and to stop taxpayers seeking redress by way of appeal.

### RECOMMENDATIONS-

- Allowing Property Tax taxpayers to choose to deduct the actual expenses incurred in the production of the rental income, including repairing and interest expenses.

### Salaries Tax

*S.12(1)(a) of the Inland Revenue Ordinance stated that “(1) in ascertaining the net assessable income of a person for any year of assessment, there shall be deducted from the assessable income of that person-*

*(a) all outgoings and expenses, other than expenses of a domestic or private nature and capital expenditure, **wholly, exclusively and necessarily** incurred in the production of the assessable income;*

It is well-known that the words “wholly, exclusively and necessarily” are notoriously rigid, narrow and restricted. With these words in the present tax legislation, the chance of a salaried taxpayer claiming deductions is nearly zero (*Lomax v Newton* (1953) 34 TC 558, 561-562). In D61/06 (IRBRD Volume 21, 3<sup>rd</sup> supplement), a teacher was unfairly disallowed expenses for purchase of books; in *CIR v Franco Tong Sui Lun*, HCIA 2/2006, a securities dealer was disallowed bad debts that were deducted from his commission



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income, etc. The Court and the Board of Review agreed that the expenditure incurred by the taxpayers would have enhanced the quality of the taxpayers' work, were reasonable and deductible if the taxpayers were subject to Profits Tax. Nevertheless, the Court/Board decided that the expenditure were not "legally deductible" under Salaries Tax.

In D102/03 (IRBRD Volume 18, 3<sup>rd</sup> Supplement), the Board of Review had paid regard to the inherent unfairness in the contrasting rules governing Salaries Tax and Profits Tax deductions. In other words, the present legislation in this respect is not neutral.

### RECOMMENDATIONS –

- Establishing a **Tax Policy Steering Committee** (or, "special unit") under the Financial Services and Treasury Bureau to conduct a thorough review of our Inland Revenue Ordinance with a view to maintaining neutrality, simplicity and equity.

Our Society has been supporting Hong Kong since 1913 and it is our wish that Hong Kong will strive and prosper in the future.

We will be happy to answer any further questions that you may have. Should you require more information, please do not hesitate to contact the undersigned or Ms. Elizabeth Law, Chairman of our Taxation Committee, or Mr. Chan Cheong Tat, Advisor to our Taxation Committee.

Happy New Year of the Horse!

Yours sincerely

Stella Choy  
President

c.c. Mr. K C Chan GBS, JP, Secretary for Financial Services and the Treasury