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)
創於1913年
Founded in 1913

11 February 2019

The Honourable Mr. Chan Mo-po, Paul, GBM, GBS, MH, 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. 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.

In the coming year, the Hong Kong business community has to face the uncertain consequence of the Trade War and International Disputes. In addition, over 90% of the businesses in Hong Kong are in the service industry. The sharp increase in labour costs, namely the close to 9% increase in minimum pay which will indirectly affect the salaries of all employees and the upcoming adjustments in Mandatory Provident Funds) would significantly increase the costs of most businesses in Hong Kong. As the HKSAR Government ("the Government") has been accumulating a huge reserve throughout the years, it is important that the Government issues timely and effective measures to help businesses and protect the employment while providing the right stimulus at the right time.

It is with these factors in mind that our Society submits the following suggestions:

PROVISION FOR AN EQUITABLE & EFFICIENT TAX ENVIRONMENT

A. REVIEW OF HONG KONG TAX SYSTEM

Our Inland Revenue Ordinance ("IRO") was last reviewed in 1976. Since then, there have been tremendous changes all over the world. Although the Joint Liaison Committee on Taxation ("JLCT") is functioning well in providing a constructive forum for liaison between the Administration and representative of the private sector, it can by no means replace the function of a comprehensive tax review committee. There are several areas which we consider requiring a comprehensive review, for example:

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(i) The "territorial source" principle under the Base Erosion and Profit Shifting (BEPS) environment.

(ii) The tax deduction provisions under profits tax and salaries tax/property tax.

On implementing the BEPS measure, the Government emphasized that our territorial source principle should remain unchanged. For example, in a press release dated 13 July 2018 the Government spokesman said, "Our long-established territorial source principle of taxation will continue to apply to determine the chargeability of income or profits to Hong Kong tax." However, the Inland Revenue Department ("IRD") has taken the view that there is in practice no case for allowing "offshore" profits following the legislative changes. Offshore claim cases invariably have to end up in appeals to the Board of Review or Courts. Given IRD's present position, we consider that it is necessary to review and clarify the application of our existing territorial source concept in order to save the resources of the Government, the Judiciary and the taxpayers in handling these claims.

In respect of (ii), the Board of Review commented in D102/03 (IRBRD Volume 18, 3rd Supplement) that the rules for salaries tax deduction, derived from ancient United Kingdom precedent, were enacted in a very different time to that existing in modern Hong Kong. The Board paid regard to the inherent unfairness in the contrasting rules governing salaries tax and profits tax deductions.

For property tax, many taxpayers are concerned that with the introduction of the Mandatory Building Inspection Scheme, Mandatory Window Inspection Scheme, etc., an allowance of 20% for repairs and outgoings may no longer be sufficient to cover the expenses incurred in producing the rental income. We also consider that it is against the equity and neutrality principle to disallow deduction for interest expenses incurred in the production of rental income in computing the liability to property tax. At present, an individual property owner may claim deduction for interest expenses only if he is eligible and elects for personal assessment.

RECOMMENDATIONS –

- Establishing a Tax Review Committee to conduct a comprehensive review of the taxation policies in Hong Kong.

- Relaxing the deduction provision for salaries tax by deleting the words "wholly, exclusively and necessarily" from section 12 of the IRO.

- Elevating the 20% deduction rate for property tax and allowing deduction for interest expense incurred in the production of rental income in addition to the rate specified for repairs and outgoings (similar to the present treatment for "Rates").

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B. PROVIDING A MORE FAVOURABLE BUSINESS ENVIRONMENT – STREAMLINING TAX ADMINISTRATION

The principle goal of taxpayers is to have tax matters resolved fairly with finality. If they have made taxes that are not agreed by the tax administration, one would expect the tax administration to inform the taxpayers as soon as possible. Under the IRD's "Assess First, Audit Later" system, taxpayers are often informed of the disagreements several years later and are liable to penalty even if there is no intention to evade or avoid tax.

There are always areas of uncertainty in the interpretation of tax law and practice. It is important for the tax administration to appreciate the value of certainty and to help taxpayers to achieve them by providing increased transparency and timely certainty. It is detrimental to taxpayers' relationship if tax administration seeks to raise estimated assessments without first raising enquiries and leaves to the taxpayer to discharge the onus of proof.

RECOMMENDATIONS –

- Commissioning the Commissioner of Inland Revenue ("CIR") to review the "Assess First, Audit Later" system with a view to improving certainty of taxpayers' tax matters.
- Defining loss statement as an assessment in order to provide finality for loss cases.
- Reversing the onus of proof in certain circumstances.
- Reviewing the penalty provisions to restrict penalty to interest in cases where there is no intention to evade tax.

RELIEF FOR SMALL AND MEDIUM ENTERPRISES ("SMEs")

C. PROVIDING A MORE FAVOURABLE TAX ENVIRONMENT – 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.

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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 SMEs 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.

D. TAX RELIEF FOR SMEs OVERSEAS DEVELOPMENT

We support the Government's policy to create favorable conditions for diversifying Hong Kong's industries, so as to actively participate in the development of "Guangdong-Hong Kong-Macao Greater Bay Area ("the Greater Bay Area"). However, we understand that there are 4 key stages for companies entering into a new market, i.e. market penetration, market exploration, positioning and market promotion. To encourage Hong Kong companies ("companies") carry out more activities in this growth journey and to support more companies to expand overseas, especially the Greater Bay Area, we recommend that the Government allows approved companies have 150-200 per cent tax deduction for the qualifying expenses incurred for qualifying activities, for instances, expenses in participating a business deployment trips and/or overseas trade fairs, etc...

RECOMMENDATIONS –

- Introducing a tax relief (e.g. 150-200 per cent tax deduction for the first HK$100,000 of qualifying expenses incurred for qualifying activities) for those Companies having a permanent establishment in Hong Kong, with a primary purpose in developing overseas business, such as promoting the provision of services or trading of goods in new markets outside of Hong Kong.

E. REVIEW OF SECTION 39E OF THE INLAND REVENUE ORDINANCE

When section 39E was enacted in 1986, the Administration stated that the amendments were intended to counteract tax avoidance through "sale and lease back" and "leverage leasing" financing arrangements. In response to Legco members enquiries, the then Financial Secretary undertook on behalf of the CIR that he did not intend to interfere with genuine commercial transactions and would apply section 39E to tackle anti-avoidance arrangements only. The CIR's

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present interpretation of section 39E has gone back on his words before the Legco and is detrimental to any intended investment plans in the Greater Bay Area.

RECOMMENDATIONS –

- Reviewing section 39E with reference to the legislative intent.

F. OPENING BANK ACCOUNTS

We support the Government's initiatives to attract more businesses to invest in Hong Kong. However, businesses are experiencing significant difficulties in opening bank accounts in Hong Kong. This is usually the case for countries from the Belt and Road areas.

RECOMMENDATIONS –

We recommend that special treatments should be given to investors from new markets, particularly those from the Belt and Road countries, Russia or USA so that more businesses can open startups or regional offices in Hong Kong.

RELIEF FOR INDIVIDUALS

G. INCENTIVES FOR HIGHLY SKILLED INDIVIDUALS

We welcome the implementation of two-tiered profits tax rate regime, which aimed to foster a favorable business environment and enhance Hong Kong's competitiveness. In order to strengthen Hong Kong's competitiveness and to build a successful and productive economy, we will need skilled people. To attract and encourage more expertise or skilled professionals work and contribute in Hong Kong, it is important to provide a favorable environment for individual and, we suggest that a similar tax incentive should be introduced for an individual. Besides, with effect from 1 April 2018, the profits tax rate for individual's profits up to $2,000,000 is reduced to 7.5%, thus creating unfairness to salaries earners.

RECOMMENDATIONS –

- The standard rate of calculation of salaries tax will be aligned with new regime of calculation of profits tax.

- Tax rate for the first HK$2 million of net assessable income before deducting personal allowance to be lowered to 7.5% (half of the standard rate).

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H. PROMOTE VOLUNTARY DISCLOSURE

The publication of a recent tax evasion case in the Mainland is very alarming and creates effective deterrent for tax evasion. On releasing the news, the State Administration of Taxation of the Mainland ("SAT") announced that taxpayers who volunteer to make self correction (自查自繳) would not be penalized.

Although IRD's Departmental Interpretation and Practice Note 11 states that it is the practice of the CIR to be influenced where a person has made a full confession in respect of any offence to which he has been a party, very few taxpayers receive the message. After all, CIR's undertaking on penalty is very vague. In this respect, SAT's pronouncement of no penalty (免予行政處罰) is more appealing to taxpayers. In order to convince delinquent taxpayers to put their house in order, the Administration may consider launching a special exercise to promote voluntary disclosure. Penalties in these cases should be clearly defined, e.g. restricted to interest on tax undercharged.

RECOMMENDATIONS –

- Considering to launch a special exercise to promote voluntary disclosure and to restrict penalty to interest on the tax undercharged for taxpayers who volunteer full confession.

PROMOTING CORPORATE SOCIAL RESPONSIBILITIES

I. 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 or when profit for the year decreased drastically in any year.

RECOMMENDATIONS –

- Hiking the percentage threshold of the donation to 50% of the assessable profit of the taxpayer for approved charitable donations.

- Allowing deductible donations to be carried forward during the year when the taxpayer incurred losses. In the circumstances, the allowable donations may be limited to donations made by the taxpayer in the past 5 years.

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J. SPECIAL TAX DEDUCTIONS FOR EQUIPMENT FOR THE ELDERLIES

As the population in Hong Kong is aging at a very fast pace, it is important that the whole community in Hong Kong be equipped to embrace this change.

RECOMMENDATIONS –

- Special deductions should be available for companies and individuals to develop equipments (including innovations in wheelchairs, beds and other eldercare equipments) or renovations made specially for the use of elderlies and the disabled.

- Exemptions for special fittings for elderlies or disabled persons in Motor Vehicles First Registration Tax.

K. ALLOWING THE ELDERLIES TO ENJOY THE CONVENIENCE OF THE GREATER BAY AREA

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 encourages 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. Apartments in Hong Kong are getting tinier and tinier. Forcing the younger and the elder generations to live together in small apartments may create tensions between the generations and therefore lead to other social problems. There is a Chinese saying, "its fine to meet each other but difficult to be living together" ("相見好，同住難"). Many taxpayers choose to rent or purchase separate quarters for their parents/grandparents.

With the opening of the High Speed Rail and the Hong Kong-Zhuhai-Macao Bridge, the retirees and elderlies can take advantage of the lower costs for elderly / residential care homes and care workers by having the additional choice of retiring in the Greater Bay Area while maintaining good connectivity with the younger generations.

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.

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- Taking reference from "Portable Comprehensive Social Security Assistance (PCSSA) Scheme (綜援長者廣東及福建省養老計劃)" launched by Social Service Department, we recommend that parents and grandparents residing outside of Hong Kong to be also eligible for the Allowances.

- Expenses paid for residential care homes situated outside Hong Kong should be an eligible expense for tax deduction. This will help to alleviate the demand for welfare support from the Government.

L. EMPOWERING & EQUALITY FOR WORKING MOTHERS

To mitigate the consequences of an ageing population and shrinking labour force, the Government is seeking methods to increase working population. We propose to introduce the following measures to encourage women to remain in or rejoin the workforce.

Many female homemakers who gave up their career to devote to their families possess high education level and precious working experience that can provide valuable manpower resources. Some grassroots female homemakers who shoulder family burdens lack the incentive to work and/or seek subsidies from the Government. With the support from the Government, employers can attract talents and alleviate manpower shortages and Government's financial burden on public expenditure such as Comprehensive Social Security Assistance (CSSA) can be lightened.

RECOMMENDATIONS –

- Providing infrastructure support for families with both parents working, such as childcare service and flexible workplace arrangements.

- Additional Childcare Allowances for extra help needed by a working mother.

- Allow 150% tax deduction for expenditure of employers spent on renovations (e.g. breast feeding areas, etc.) made to work environment to support young working mothers.

- Setting up a special Parental Program Fund so that, similar to other countries like Canada, UK or Singapore, etc., maternity payments can be paid by the special Fund instead of it being shouldered solely by individual employers. This will help to alleviate the inequality and discrimination against female employees and also help to encourage more women to rejoin the work force.

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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.

Yours sincerely,

Tanny

Yu Kwong Man, Tanny
President

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