



香港稅務學會

THE TAXATION INSTITUTE OF HONG KONG

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

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2006/07 BUDGET COMMENTARIES

The Financial Secretary, Henry Tang, delivered his third budget speech yesterday at the Legislative Council. Although the economy has bounced back, the Institute has suggested (see our budget submission dated 11 January 2006) to the Financial Secretary to adhere to the principle of prudent financial management, while giving more tax incentives and relieves to the middle class taxpayers and businesses which face difficulties. His budget proposal has been prepared amid great expectations from legislators and political parties for tax cuts and increase in public spending. The main changes on taxation and our comments thereon are summarized below.

Overview

The budget does not contain any surprise. It is a prudent proposal with moderate concessions / incentives to appeal the middle class taxpayers.

Profits Tax

Although we have repeatedly suggested that the Government should introduce group loss relief and the carry back of current year loss to prior years, it seems to us that it is the Government's stated policy that it will not pursue these two suggestions for the sake of preserving the simple tax system in Hong Kong. The Financial Secretary explained in paragraph 79 of his budget speech that the reason for not considering the group loss relief and the loss carry-back is that it can easily be abused as a means to evade tax and if the proposed change is adopted, the Government will face enormous pressure on tax revenue during periods of economic downturn. We are still of the view that the proposal should be adopted and would urge the Government to reconsider this proposal (which we believe should not be difficult to administer and in fact would reduce dispute on management fees sharing among group companies operating in Hong Kong) when the economy has fully recovered and the Government has built up a healthy reserve as a buffer against any such potential revenue losses. We believe that unless the profits tax rate in Hong Kong can be reduced further and the Administration will adhere strictly to a territorial base of taxation, our competitive edge may be lost to our competitors in the region in future.

Salaries Tax

We welcome the Government's proposal to reduce the second, third and top tax bands for individual taxpayers to 7%, 13% and 19% respectively and the extension of mortgage loan interest deduction to ten years. These measures will, to a certain extent, relieve the financial burdens of middle class taxpayers.

However, we believe too little has been proposed to help alleviate the potential demographic crisis – an aging population in Hong Kong. The Government has not accepted our proposal to increase child allowance nor has the Government been decisive enough to consider implementing tax deductions for premiums paid on medical insurance policies in the next financial year. We believe that the government's deferment of decision to consider whether to allow tax deduction for medical insurance premium, pending the consultation on healthcare arrangement, is unnecessary.

Goods and Services Tax (GST)

We are pleased that the Government has accepted our proposal to conduct a comprehensive consultation on the implementation of GST in Hong Kong in 2006 and reduction of direct taxes at the same time. We agree with the Government's stated principle that even if GST is implemented a low and simple tax regime should be maintained. These principles accord with the spirit of our budget submission.

Environmental Tax

We believe the Government should speed up the study, consultation and implementation of the taxation on tyres and plastic bags, otherwise, our environment will suffer irreversible damage.

In addition to tax policies, we believe that administrative measures and concessions (otherwise than in form of direct favourable tax treatment) should be devised to encourage the establishment of industries involved in the recycling of waste products or production of environmentally friendly goods, and create a favourable environment for their continued operation.

Other Fiscal Measures

We would urge the Government to speed up the negotiation and conclusion of Double Taxation Agreements with Hong Kong's trading partners so that our competitive edge in the region can be maintained, the budget proposal has not dealt with this point.

In addition the proposal lacks specific incentives to improve business operating environment (for example, incentives to companies setting up headquarters in Hong Kong and additional deductions for investment costs in human resources) and a roadmap for the sustainable economic development of Hong Kong in the longer term.

Conclusion

Apart from the aforementioned reservations, we believe the overall tax measures proposed in the budget are appropriate for a recovering but apparently unstable economy and the adoption of a prudent financial management policy will put Hong Kong's public finance on solid ground.

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