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- Urgent  
 Return Receipt

To: taxreform@fstb.gov.hk  
 cc:  
 Subject: vat

Greetings,

I am only a canadian, therefore my input into the internal affairs of your wonderful Hong Kong are irrelevant. I do however have a very good idea of what happens when a state takes the disastrous step of introducing vat.

First, such a tax is extremely regressive. It hammers the poorest in society, generating terrible hardships for the lowest rungs of society. Even in my house, with a comfortable income we suffer. Only the very rich are immune to financial setbacks from vat. In canada, when a 7% vat was introduced, none of the wealthy really had a problem. If your income is so high that you are enjoying a level of disposable income approaching 30%, it is no hardship to absorb an automatic 7% rise in the cost of living, not to mention the inflationary pressures built in to such a system. As a personal example, at the mid-income level, my family is forced to take fewer vacations, and we now only replace our automobiles every ten years or so, instead of the five year cycle we followed pre-vat. That money is permanently gone from productive use in canada's economy. The working poor are devastated. The rich, and the mids like myself can adjust downward our standard of living, but the working poor have no such buffer given low income levels to begin with. These economic impacts stifle growth, not to mention confidence that your personal economy will sustain you in the long run.

Secondly, there is the enormous growth in economic lawlessness. Many of the old folks I reference here are now deceased, but of the ones who regularly spent money on non-essential expenses at the time that canada was foolish enough to go vat, most stopped spending. I watched an entire segment of the population go from being the most honest group in the society to becoming travellers across the border to the U.S., and smuggling their purchases home. Buying off-shore in the U.S. to avoid vat, then becoming criminals via cross-border smuggling, again to avoid vat. Pretty fantastic trick. Turning your most law-abiding citizens into criminals overnight, because of vat! And it is not just the older segment of society using such methods. Vat makes tax evasion a national sport, instead of the preserve of the genuinely criminal!

Thirdly, the underground economy. People in canada now will not sign on to any financial transaction, from home renovations, to any imaginable purchases, large or small, without first inquiring if there might not be a financial advantage to doing the transaction in cash to evade vat. I can attest that fully half of my small business friends will simply divert as much of their trade as they can to cash-only, to satisfy customer demand, and avoid vat. I can also verify that this tax evasion technique is practised at ALL income levels, not just the lower end of the spectrum.

Fourth, vat has a large negative effect on charitable operations, since even though they are charities, all of the society must be saddled by the inconvenience and expense of vat on their operations. Of course, if you take money from a charitable organization's front end in vat, they can help fewer people, causing those no longer helped to enter onto the welfare rolls. It is quite simply more sensible to stay home waiting for a welfare cheque,

than to work hard at a lower-end income, and watch taxation in the form of vat eat what little income you have.

Fifth is the added expense forced onto business. Particularly in the small business sector, where limited personnel resources are diverted into a more complicated, time-consuming role of being unpaid remittance people.

Everyone understands that business pays no tax, but merely passes on costs to the end consumer of a service or product. Hence the built-in inflationary aspect to vat previously mentioned.

Lastly, I don't know how eager the government in Canada is to admit to the HK government that their taxation policies are a failure, but the revenue growth that was to be generated by vat in Canada has not, even now. After three plus decades, reached the original estimates. On top of the unfulfilled promises offered by the World Bank when they tricked Canada into going vat, tax revenues fell far short of estimates. The promised drop in costs for collection of taxes never materialized, and in fact now Canada spends 15% more in per-dollar tax collected costs, than pre-vat. But you may rest assured that moving to vat will result in job growth. In government. You too, like Canada, will have to create an entirely new bureaucracy to shadow-box with the newly established high-growth area in your economy. The one referred to as underground.

In closing, if your taxation system needs to be fine tuned, there are ways to do it in the framework of your current successful model. It seems to me that if you have a taxation system that is the envy of people world-wide, particularly to a place like Canada, it might be unwise to go vat, rather than tweaking an already workable, respected model. My wise old grandmother told me that such a move would be like throwing the baby out with the bathwater!

Please forgive my audacity in presuming to advise wise legislators such as yourselves, but I feel your citizens may be betrayed if you only hear the point of view of the World Bank and ilk. The World Bank is a valuable group, but it is generally unable to offer concrete assistance to already successful economies such as the one you have, and Canada used to enjoy.

Thank you.

k smart, Canada