



To: <taxreform@fstb.gov.hk>  
 cc:  
 Subject: Tax Reform Comments (To Financial Secretary, Mr. Henry Tang)

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Urgent  
 Return Receipt

Dear Mr. Henry Tang,

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After reading your tax reform consultation document, I have several comments.

First of all, I would like to point out that the underlying problem with our revenue is not solely due to our tax system but a distorted economy. <?xml:namespace prefix = st1 ns = "urn:schemas-microsoft-com:office:smarttags" />Hong Kong has relied on high land price and high property price to sustain economic growth and stable revenue in the past. After 8 years of economic slowdown, the government is still promoting this type of economy. It is true that the tax base (direct tax) is narrow because the majority of tax revenue comes from a small number of big corporations and high-income individuals. However, it only shows how distorted and imbalanced our economy is. While some big corporations can earn billions of dollars in profits and their top CEOs pay millions of dollars in income tax, low-income to middle-income families, small and medium-sized business are struggling for survival.

Hong Kong is still a low income tax, low profit tax region by international standards. The tax rate is still lower than most developed countries in the world or Asia Pacific region. There is no urgency to reduce the income tax or profit tax rate drastically. Competitiveness is also not relied on tax rate alone but you seem to deliberately ignore other factors.

No tax system can ensure a steady income. During economic recession, there would be less consumption spending, the revenue collected through GST would also decrease. Worse still, the new tax can further hamper the economy. You will then need to increase income tax and profit tax again.

GST is not a fair tax. Everyone knows it is regressive. It affects low-income families more as their consumption takes up the majority of their earnings. It is a twist of fact to claim that GST is a fair tax. Even though high-income families may pay more GST compared to low-income families, the tax takes up a much smaller percentage of their income.

You claim that other countries also have GST for years. But what are their top income tax and profit tax rates? These rates are 2-3 times higher than those in Hong Kong! These countries also have good social welfare, pension plans, employment insurance and health care. They have implemented minimum hourly wages and antimonopoly laws for many years. How can you selectively pick one single tax for comparison and ignore the whole picture?

Your rationale to charge necessities such as groceries, public transport fees, medical expenses for GST but yet giving the exemption to financial services and residential property is puzzling. In many countries where GST is implemented, necessities such as groceries and public transport fees are exempted (health care is free in many countries). You claim that exemptions can add to complexity but only a lazy government would only care about the simplicity of collecting tax and not about fairness or the burden the new tax imposes on the

people.

According to your report, top 800 companies pay 60% of total profit tax. It only shows that these big corporations grab the largest piece of the pie. It is fair that the more you get from the society, the more you give back. To broaden this tax base, the government should introduce plans to let small and medium-sized businesses flourish so they can contribute more to tax revenue. GST is doing the opposite. Large corporations can save billions of tax dollars and yet small and medium-sized businesses pay extra cost to collect tax for the government.

You said that GST can reduce income tax and profit tax and make Hong Kong more competitive. If tax rate is the only factor for competitiveness, no one will work in EU countries as their top income tax rate is 44% compared to 16% standard rate in Hong Kong. Everybody in EU should flee and come to work in Hong Kong, right? There are other factors affecting how a country or region can attract talents, such as living environment, a democratic society, social stability and health care, etc.

You point out that Hong Kong population is aging and we need stable income (other than income tax) to compensate for increasing expenditure. But when I look at chart 8 (government revenue & expenditure), I notice that something is seriously wrong. From 1996-97 to 2003-04, our expenditure has increased 36% from 180 billions to 245 billions (roughly). Were these money spent effectively? No tax reform can compensate for such a huge increase in expenditure. There is no surprise that Hong Kong people worry that GST would turn on the green light for huge government spending.

Your consultation document has a lot of emotional blackmailing. You keep saying that without GST, we have no choice but to increase income tax and profit tax in case of economic recession or increased government spending. A responsible government would take steps to cut government expenditure and facilitate sustainable economic growth (not relying on speculation in stock market / property market). Instead of taking these steps, you seem to suggest that GST is our only solution.

There are many suggestions to broaden the tax base, such as capital gain tax, departure tax and progressive profit tax. And yet, you rule out all of these, claiming that they will make Hong Kong less competitive. Using capital gain tax as an example, this tax is practiced in many developed countries. I have never heard that no one will invest in the NYSE because of the capital gain tax. A higher capital gain tax for short term investment can also discourage speculation and curb market volatility.

According to your proposal, only businesses which have 5 millions dollars in revenue need to register. It seems like many small or medium-sized businesses will not be affected by GST. But in reality, if the small or medium-sized businesses buy any goods or services from a registered business, they are obliged to pay the input tax. So either they eat up the extra cost themselves or they have to pass the tax to the consumers. In the former case, their profit is reduced or else, they are forced to spend additional resources on accounting and add the tax to their products or services.

The impact of GST on tourism is hard to predict. Hong Kong is a shopping paradise but with an additional 5% GST (which would only increase not decrease), are we still so competitive?

Many tourists may not benefit from GST refund as there is a threshold or they may find filing for refund too troublesome. Why is competitiveness not your concern here?

It is proposed that GST allowances will be provided across the board for all families in Hong Kong. But some of these allowances are subject to review after 5 years. In other words, they may be discontinued after 5 years and at the same time, the GST rate may increase. If the HK government is really concerned about providing relief to those affected by GST, shouldn't these allowances be permanent and adjusted as GST rate increases in the future. In contrast, your proposal sounds like a trick to buy the support from the public. The fact that you use extreme examples where all extra income would be used in income tax reduction or profit tax reduction further illustrates this point.

In addition, you have not outlined how low-income families can file for GST allowances (actually, it is better called GST credit). Many low-income families live in harsh conditions but they refuse to apply for social security assistance right now. They do not want to receive government support. If GST allowances are considered as some kind of government subsidies and subject to income and family assessment, many families will be reluctant to file for the allowances. Not to mention that some elderly or less educated people may have difficulties applying for the allowances themselves.

Your document outlines a rosy picture after GST. CSSA families will not be affected as their assistance will be adjusted accordingly. Low-income families will not be affected because there will be GST allowances and may even benefit from this according to the calculation in the document. Middle-income families can also benefit because of the Rate and Water fee reduction and income tax relief (but whether the Rate reduction will be passed to the tenants is hard to monitor). Though you did not mention, everyone knows that the top earning households gain the most benefits from an income tax reduction. But this does not make sense at all. If everyone is not affected or benefits from GST, where will the extra revenue come from?

As someone else points out, Hong Kong people across the board are already paying indirect "tax" because of high land price, high property price and high rental fees. This indirect "tax" is very broad based. Without taking this into consideration, it gives a false picture that income tax and profit tax contribute to a much higher percentage of government income compared to other countries (in reality, they contribute to a high percentage of tax revenue, not total revenue).

Therefore, I do not believe that the government has a strong case to push forward GST at this time. At least, you should consider other options first: other new taxes, such as capital gain tax, departure tax, progressive profit tax, increase the bandwidth and spectrum of income tax with a higher tax rate for the top earning individuals; take steps to cut government expenditure and encourage the growth of local small and medium-sized businesses (how about antimonopoly laws); and find a direction for sustainable economic growth. Steady revenue can only be achieved by a stable and balanced economy not a simple "solution" such as GST!

Yours Sincerely,  
Miss Kwan Hung LO  
(A low-income household with middle-income expenditure)