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TAI HING COTTON MILL, LTD.
 (INCORPORATED IN HONGKONG)

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5 September 2006

The Honourable Henry Tang Ying-yen, GBS, JP
 Financial Secretary
 Government Secretariat
 Government of the Hong Kong Special Administrative Region
 12/F Central Government Offices
 West Wing, Lower Albert Road
 Hong Kong

By Registered Post

Dear Mr Tang,

Broadening the Tax Base. Ensuring our Future Prosperity

We welcome the opportunity to comment on the "Consultation Paper on Proposed Reforms to Broaden Hong Kong's Tax Base", and would like to set out our views as follows.

We are concerned that the main purpose of this proposed tax reform is to establish a dependable and growing revenue base so that the government could meet the future challenges. We feel that this dependable and growing revenue base is built at the expenses of every member of the community. Both the government and the public have to face with economic uncertainties. During the economic downturn, the public will suffer the same difficulty as the government. Under the proposed GST scheme, the government revenue will be protected by that time. The public, on the opposite side, will not only receive less income but also bear an additional burden, which is GST, on their already reduced income. This is the most unfair solution to shift over the further burden and liability to the public when the public is already in the most difficult time under economical downturn or under disastrous crisis, such as the past "SARS" case.

Although tax refunds are provided to tourists but we doubt how many tourists would bother to waste their time filling in unfamiliar claim documents to ask for it. This may discourage them to spend in Hong Kong and the retailers will suffer. It would also tarnish Hong Kong's image as "a shopping paradise".

Hong Kong is one of the well-known free ports in the world. People and goods travel freely and efficiently without complicate procedures. GST will force travellers to



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in line for luggage check. We cannot imagine how the airport could handle such a large amount of travellers and goods. If we want to be one of the leading logistic centres, an efficient status of free port must be maintained.

In paragraph 3 of the Consultation Document, the government admits that "the rapid recovery of our economy in the last two years is attributable to many factors, one of which is our simple, predictable and low-rate taxation system, which encourages investment and rewards people for their hard work." A simple taxation system is very important to encourage investments and to attract foreign investors because it helps to keep down the costs of doing businesses. However, a GST will completely destroy the simple taxation system enjoyed and praised by everyone. It would impose heavy administration costs on businesses because they will be forced to serve as tax collectors for the government.

We understand that GST is, in theory, not a tax borne by business. However, from our experience in other country, it is difficult to pass the cost to our direct customers. The selling price of our cotton yarns and piece goods are indirectly controlled by downstream manufacturers who have more bargaining power. We would have to absorb the cost (GST) ourselves, if our selling price plus GST will be higher than our competitors' prices, such as products coming from Pakistan and mainland China. As we have already suffered from high production costs in Hong Kong and faced keen competition from the factories in the mainland China, the absorption of this 5% GST for the introduction would become the last straw that breaks the camel's back. The spinning industry is already in very bad shape and all mill top management are exhaustedly struggling for survival. The new proposed GST will be the fatal weapon to kill the Hong Kong spinning industry without doubt.

The Government commits that, at least for the first five years after GST introduction, "all revenue so generated, after government administrative costs relating to its collection had been met, would be returned to the community as tax relief or compensation or other measures". We wonder how and how long the government could honour this commitment, especially if during such period, we encounter another sudden economic downturn. Moreover, it is obvious that extra manpower is needed to handle the tax relief. Furthermore, if no one is affected by GST, then why the government needs to provide tax relief?

According to Article 107 of the Basic Law, "The Hong Kong Special Administrative



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Region shall follow the principle of keeping the expenditure within the limits of revenues in drawing up its budget, and strive to achieve a fiscal balance, avoid deficits and keep the budget commensurate with the growth rate of its gross domestic product." Therefore, the government should share the good commercial practice that when it has surplus income, it should save it as reserve for the economic downturn. When it suffers from budget deficits during the economic downturn, it should cut its expenditure and use its reserve to help the public and to stimulate economic growth. This is a common strategy practiced by all financial, commercial, and industrial companies worldwide. The government should not operate like a protected monopoly and put the public to guarantee its income.

In conclusion, GST is definitely not the right solution to broaden the tax base and to ensure future prosperity.

We hope that the government will consider our comments carefully and seriously.

Yours sincerely,
Tai Hing Cotton Mill Ltd

(Signed)

Y. C. Chen
Managing Director