

The Dairy Farm Company Ltd

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27 September 2006

Tax Reform

Financial Services and the Treasury Bureau
4/F, Main Wing, Central Government Offices
Lower Albert Road
Hong Kong

Dear Sir,

Re: GST Consultation

I am writing on behalf of The Dairy Farm Company Limited, trading as Mannings, to register our opposition to the introduction of GST in Hong Kong.

We have reviewed the Consultation Paper outlining the Government's desire to broaden the tax base, but believe the case to broaden the tax base is unproven and that, in any event, a GST is the wrong way to do this. Our reasons for opposing the GST are summarised below.

- **Effect on consumers:** consumers, the bearers of the tax, will suffer. The GST will reduce consumer consumption and will result in an increase in prices for all consumers. The GST will be largely regressive in nature resulting in relatively greater hardship for the less well-off among Hong Kong's population. Measures to provide relief via compensation payments will inevitably be unequal as well as creating additional administration costs. The effect of reduced spending will be significantly adverse for our business.
- **Erosion of competitive advantage:** the GST would erode Hong Kong's competitive advantage by increasing the costs and decreasing the ease of doing business in Hong Kong. The rest of world rightly envies Hong Kong as a simple and tax-friendly place to do business. Voluntarily giving up a significant part of Hong Kong's competitive advantage would be a mistake.
- **Not a level playing field:** the proposed GST is fundamentally unfair to larger businesses. The Consultation Paper states that the purpose of "setting a high registration threshold is to exclude most small and medium sized businesses". Only 28% of Hong Kong businesses (65,000 out of 230,000 active companies) would be obliged to register for the GST. The remaining 72% of businesses will be exempt from charging GST, in exchange for forfeiting recoupment of input tax credits. This is an unequal and unreasonable exchange, and will result in smaller businesses being able to opt in or out of the GST regime to suit their best financial outcome. Inevitably, some of our smaller competitors will be able to opt out of charging GST and will thereby gain customers at the expense of larger GST-complying companies.

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- **Implementation costs for business:** the retail industry is hugely dependent on point-of-sale scanning to capture sales data which then forms the backbone on which the accounting and merchandising systems operate. These systems will have to be re-written to comply with GST, and amended when GST rates change in the future. The systems are very complex and fundamental to the operation of our business, and any amendments to them are enormously costly in terms of programming, testing and user training. Our company would need to carry out these changes in all of our 232 store locations in Hong Kong, as well as undertaking extensive work on our central systems. We would then need to co-ordinate training sessions for our staff, again at enormous cost for which we will receive no benefit or compensation.
- **Complexity:** GST is a complex tax to introduce and administer at the company level, and will be a deterrent to business in Hong Kong generally. Further, and although not mentioned in the consultation paper, there will inevitably be exemptions and zero ratings for some categories of goods. This occurs wherever GST is implemented, and has the result of making implementation of the tax more difficult (with each item having to be "tagged" so that the point-of-sale system can apply the correct GST) and exposing retailers to constant audit penalties for honest mistakes.
- **Cost and reputation risk:** politicians inevitably promise to keep retailers from "profiteering" during implementation period. This imposes a de facto retail price freeze before and after the GST introduction date, during which time normal price increases imposed by suppliers cannot be passed on to customers, with a consequent cost to the business community. Similarly, where genuine errors are made in seeking to comply with a complex new tax, businesses are attacked by Government and the press as profiteers, with consequent and undeserved harm to these businesses' reputations.
- **Effect on tourist spending:** while the Consultation Paper proposes a tax refund scheme for tourists, this scheme has a "minimum spend per store" restriction that will substantially reduce the attractiveness of tourist spending in Hong Kong. In addition, the Government should be aware that even for a qualifying level of expenditure per store, there is considerable inconvenience to individual shoppers in complying with the administration of refund schemes. This means that in practice the additional tax is an effective price increase, with consequent negative effect on tourist spending.

In summary, we believe the proposed GST will adversely affect consumers, cause substantial economic cost to our business and to businesses throughout Hong Kong. It will reduce the ease of doing business, to the detriment of the entire Hong Kong SAR. We recommend that the Government should not proceed with this proposed new tax.

Yours sincerely,

(Signed)

Lily Chan

CEO, Mannings (HK & Macau)