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Your Ref.

Our Ref. SC

The Honourable Henry Tang Ying-yen,  
Financial Secretary,  
Hong Kong S.A.R.  
12th Floor, West Wing,  
Central Government Offices,  
Lower Albert Road,  
Hong Kong.

28th September, 2006

Dear Sir.

Re: Introduction of GST in Hong Kong

In January, 2000, as the Vice President of the Taxation Institute of Hong Kong, I have prepared a draft position paper to initiate a discussion on the introduction of "Sales Tax" in Hong Kong (similar in concept as GST) amongst Council Members. I am enclosing herewith copies of these papers and also a copy of my interview with the press on this subject. You may, perhaps, find some of the points raised of use in your publicity on GST.

For the public to accept the idea of GST, it is suggested that Government should present a projection of the fiscal position of Government for 5 to 10 years showing (A) the expenditure required in the provision of public services taking into account the increase and aging of the population and (B) the collection of Revenue having regards to ups and downs of the economic cycle. It is to be expected that there will be years when budget deficits will occur and the Government is forced to tighten its belt which will mean the public, particularly the poor, will suffer because social welfare and medical services may have to be curtailed. If depression should occur, the increase in tax rate would not help to increase Government revenue, owing to great reduction of profits and income in the business and employment sectors.

It has been argued that the poor will suffer most by GST. However, in your proposals, some reliefs will be provided to the poor if GST is to be implemented. I suggest this point be emphasized in your publicity campaign demonstrated with examples.

Yours faithfully,

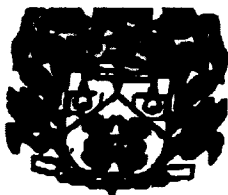
(Signed)

(Samuel S. K. CHIU)

(Editor's note: The newspaper cuttings, publications or website materials, etc. contained in this submission are not published in the compendium.)

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**香港稅務學會**  
**THE TAXATION INSTITUTE OF HONG KONG**  
(Incorporated in Hong Kong as a company limited by guarantee)

**To: All Council Members**

**From: Samuel Chin**

**Date: 18th January, 2000**

**Subject: Introduction of Sales Tax in Hong Kong**

Enclosed please find minutes of the meeting of the ad hoc committee on Sales Tax held on 7th January, 2000 for your information.

As proposed in the meeting, I have prepared the first draft of our position paper and should be grateful for your comments / feedback / additions.

Please respond by 23rd January, 2000 so that a further meeting be held by end of the month to finalize the details.

**Regards**

(Signed)

**Samuel Chin**  
**Exec.**

Should "Sales Tax" be introduced in Hong Kong?

(1) What is "Sales Tax" ?

"Sales Tax" is a taxation on expenditure. This means that tax is imposed when one expends money. This is in contrast with "Income Tax" which imposes tax when income is earned. As practically every person has to expend money "Sales Tax" would give a much broader base of taxation than "Income Tax". Nowadays, "Sales Tax" adopted in the world generally falls into three groups. Viz: (a) value-added tax, (b) wholesale tax and (c) retail tax.

- (a) Value-added tax is (definition) and is adopted in countries such as
- (b) Wholesale tax is (definition) and is adopted in countries such as
- (c) Retail tax is (definition) and is adopted in countries such as

(2) Arguments against "Sales Tax"

Introduction of "Sales Tax" is often opposed on the following grounds:-

- (a) "Sales Tax" is regressive in nature because ordinary people would spend proportionally more of their income than the rich and is against the principle of vertical equity.
- (b) "Sales Tax" would cause inflation and makes life more difficult for the poor.
- (c) "Sales Tax" would deter tourists from visiting Hong Kong and would not help to promote tourism.

(3) Arguments For "Sales Tax"

The arguments put forward for the introduction of "Sales Tax" are:-

- (a) "Sales Tax" provides a broad base of taxation and should produce a relatively stable source of revenue for Government as it is less vulnerable to economic cycles.
- (b) Because of the broad base of taxation, it is possible to maintain a low tax rate and yet producing the required revenue for the budgeted expenditure..
- (c) Apart from basic needs (which can be provided for by special measures), Sales Tax is optional because people can elect to spend less and thus avoid the payment of Sales Tax. Generally speaking, the people who are paying more "Sales Tax" are the affluent persons who have much greater spending ability.
- (d) "Sales Tax" can be used as a fiscal policy to discourage undesirable social behavior such as smoking and drinking and to deter activities which cause environmental pollution e.g. use of leaded petrol.

(4) General Principle of Taxation

Taxation has been described as "a price of civilisation". In a civilised world the Government is committed to provide a safe, comfortable and peaceful environment of living for people. For the provision of such an environment it is necessary to have the required funds so that public services can be provided. Taxation is a system which determines as to how such funds for public services are to be contributed by the citizens. It follows that if one person pays less tax another person will have to pay more to compensate for the deficit. There can be little argument that a good taxation system should have the following features:-

- (a) It produces the required revenue for Government to provide the desired public services.
- (b) The tax rate is as low as possible so that it gives the least impact on the economy as a whole.
- (c) It is equitable and generally acceptable to the public.

(5) The taxation System of Hong Kong and why Sales Tax is proposed

Hong Kong adopts a Taxation System which taxes earning and income on a territorial source concept. However, not all income and earnings are subject to taxation in Hong Kong. For example, there is no tax on dividend and bank interest received. There is no tax on capital gains so that profits on disposal of capital assets are excluded from the tax net. Because of the territorial source concept income and profit received by residents of Hong Kong from ex-Hong Kong sources are not taxed. It is possible that there are Hong Kong residents with great wealth and large income need pay no tax in Hong Kong. From Government statistics, it is noted that taxes from profits and earnings contribute 48% to 51% of the total Government Revenue. Of the Profits Tax collected, over 50% were paid by property and banking corporations. Of the Salaries Tax collected 49.8% was contributed by some 94,000 taxpayers. This represents 7% of the total salary tax payers and 1.38% of the total population of 6.8m. It will be seen that the tax base in Hong Kong is extremely narrow. Although during the boom years, there have been no problem in collecting the required revenue for the Government Expenditure, at the time of economic recession, when earnings and profits dropped (such as in the years 1998/99 and 1999/2000) Government would not be able to collect sufficient money for its budgeted expenditure. An idea that may seem worth consideration is to broaden the tax base so that each Hong Kong resident contributes some (depends on his ability) towards the public coffer. This is the idea behind the proposal of introduction of Sales Tax. It is to be expected that the amount of sales tax paid will be in proportion to ability to spend of the people which is also in proportion to their wealth and income. It is not denied that Sales Tax may cause hardship to the poor but this can be remedied by special measures as adopted by other countries practising Sales Tax.

(6) Impact on Economic Development by Sales Tax

It is certain that introduction of Sales Tax will cause inflation but how great is this impact on the economy will depend on the tax rate. If the tax rate of Sale Tax is only 3% (compared to Canada of 15% and New Zealand of <sup>10 7/8</sup>~~12 1/2~~%), it is believed that the impact is not so great as some have suggested. Furthermore, it is not believed that tourists will refrain from visiting to Hong Kong because of the 3% Sales Tax. (Suggest to produce statistic of Canada, New Zealand which have Sales Tax to support this)

(7) Conclusion

If Hong Kong is to maintain its low tax rate on a long term basis, it is obvious that its tax base must be broaden. Only with a broad base of taxation that a low tax rate is possible to generate the required revenue. It is said that a good tax structure is one that has as little economic effect as possible and this can only be achieved by low rate of taxation. How Hong Kong can produce the required revenue for its public expenditure and yet to maintain a low tax rate, it is suggested that this subject be considered by a special Committee consists of members from the public.