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The Society of Chinese Accountants & Auditors
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26 January 2021

The Honourable Mr. Chan Mo-po, Paul, GBM, GBS, MH, JP
The Financial Secretary
Government of the Hong Kong Special Administrative Region
The People's Republic of China

Dear Sir,

2021 Budget Submission

2020 has been an exceptional year for everybody as the COVID-19 pandemic has caused unprecedented disruptions to the global economy and, similar to other parts of the world, Hong Kong's economy recorded serious contraction due to the COVID-19 outbreak. In addition to the pandemic, US-China trade tensions, social unrest and other challenges together have all taken their toll in our economy, and as a result unemployment is rising rapidly.

It is important that the HKSAR Government implement timely and effective relief measures to provide the right stimulus to support the various sectors of Hong Kong and to protect employments, especially those employed by the SMEs.

It is with these factors in mind that the Society of Chinese Accountants and Auditors ("SCAA") submits the following suggestions and recommendations:

RELIEF MEASURES IN RESPONSE TO THE OUTBREAK OF COVID-19

A. Relief Measures for Corporations and Enterprises

We understand that until an effective vaccine is developed; travel restrictions, social distancing and other preventive measures constitute the main options for containing the pandemic; however, because of the pervasiveness of the effects of the above factors, businesses can only turn to the Government for financial support and financial assistances at the right moment. Otherwise, a wave of closures would ensue creating a major domino effect that could seriously damage the economy. Rescuing the economy from a full-on collapse would be more costly compared to prolonging existing and assistances and support for the industry.

RECOMMENDATIONS –

- **Tax Loss Carry Backwards & Group Tax Loss Relief**
  Many businesses are faced with severe shortages of cash. However, presently taxpayers are only allowed to carry forward their losses to offset profits of future years. If the taxpayer incurred a loss in 2020/21, the first possibility of utilizing the tax losses to enhance their cash flows can only be materialized after the filing of their 2021/22 Profits Tax Returns and only during their payment of taxes at the end of 2022 (i.e. more than 23 months from now). This will not be of any help to businesses that urgently need cash flows NOW for survival.

  It is vital that Government supports be precisely given to entities that have previous contributions to the Hong Kong Treasury and we believe that those entities usually have a higher chance of turnaround in the future as they have proven records of profitable operations. These are usually entities that hire more employees. We therefore suggest that amendments be made immediately so that businesses can carry back their 2020/21 taxation losses to offset their assessable profits for the two years of assessment 2018/19 and 2019/20, so that the Government can refund the taxes to the businesses as soon as they file their tax returns. is the present Inland Revenue Ordinance already allow the offsetting of tax losses with future tax profits; advancing this payment to an earlier date can really help businesses in need.

  We also recommend that tax losses be allowed to be utilized amongst group companies, therefore increasing tax efficiency as well as the cash flows for groups during this difficult period.

- **Special Tax Deductions to encourage rent reductions by landlords**
  Recently we noticed that many landlords did not reduce their rent and some even increased the rental for the tenants. During these difficult days, it is important that all sectors of the economy work together to keep businesses afloat to maintain stability in Hong Kong. In order to give enough incentive to landlords, we recommend that a special Covid 19 Additional 100% Deduction be given to landlords that reduce rent for their tenants during the coming year.

  This reduction will directly help businesses to weather through the storm. The incentive will be basically shared by the landlords because in reality, the Government only pays 8.25% or 16.5% of the reduction but the landlords will be shouldering their actual reduction 67% or 83.5% (depending on the tax rate). The additional deduction can also give positive encouragements to landlords who are helping their tenants through these difficult times.

- **Zero tax rate on the first 20% of the assessable profits of companies**
  In addition to the existing two-tier concession tax-rate, we recommend that additional tax concession is given to SMEs to overcome difficulties. We suggest a one-off deduction this year so that the first 20% of the assessable profits, up to a maximum of $1,000,000, of the company should be tax free. Businesses can still be charged at the reduced rate on the next HK$1,000,000 of assessable profits.

- **Super Deductions for Sanitary or Covid 19 related Items**
  During the breakout of the COVID-19, businesses need to provide special expenditures on sanitary or anti-virus equipments or supplies in order to protect their staffs or customers, these items may only be qualified as a deduction over an extended period of time. We therefore recommend that super deductions of 200% be given to both capital and revenue items of for all Sanitary items, Conferencing systems, home office equipment, online meeting system, etc., which are commonly required during this critical moment of battling against the coronavirus epidemic.

- **Waiving Business Registration fee**
  As Business Registration Fee Revenue only accounted for 0.8% of the Tax Revenue, we recommend that the Waiver of Business Registration fee for Y/A 2020/2021 be continued as an additional measure to support businesses.

B. Relief Measures for Individuals

When the Government ceases the Employment Support Scheme, one will find that many employees will be laid off due to closure of businesses or reduction of staffs by employers. Many employees, especially those who may be the sole financial earners of their families and/or burdened with mortgages on their properties, will be confronted with this sudden blow to the sources of income for their entire families.

It is important to care for the mental and physical stability of citizens of Hong Kong.

RECOMMENDATIONS –

- Suspension for collection of provisional salaries tax for Year of Assessment 2022/23.
- One off tax rebate of 100% of taxes paid in the previous years up to a maximum of HK$50,000.
- Increasing the child allowance from HK$120,000 to HK$160,000.
- Increasing the dependent parent/grandparent allowance and additional dependent parent/grandparent allowance from HK$50,000 to HK$70,000. For parent aged 55 or above but below 60, from HK$25,000 to HK$35,000.
- To continue for one more year the special measure on allowing payment of salaries tax by installments without imposing additional charges and interests.

RELIEF FOR SMALL AND MEDIUM ENTERPRISES ("SMEs")

C. Tax Relief For SMEs Overseas Development

We support the Government's policy to create favorable conditions for diversifying Hong Kong's industries so as to actively participate in the development of "Guangdong-Hong Kong-Macao Greater Bay Area ("the Greater Bay Area"). However, we understand that there are 4 key stages for companies entering into a new market, i.e. market penetration, market exploration, positioning and market promotion. To encourage Hong Kong companies to carry out more activities in this growth journey and to support more companies to expand outside of Hong Kong, especially the Greater Bay Area, we recommend that the Government allows approved companies to have 150-200 per cent tax deduction for the qualifying expenses incurred for qualifying activities. Afterall, the Inland Revenue Department's previous interpretation of section 39E of the Inland Revenue Ordinance did successfully attracted SMEs moving outside Hong Kong and led to the prosperity of today's Shenzhen and other parts of the Guangdong Province, a win-win situation.

RECOMMENDATIONS –

- Introducing a tax relief (e.g. 150-200 per cent tax deduction for the first HK$300,000 of qualifying expenses incurred for qualifying activities) for those Companies having a permanent establishment in Hong Kong, with a primary purpose in developing overseas business, such as promoting the provision of services or trading of goods and services in new markets outside of Hong Kong.

- Reviewing section 39E of the Inland Revenue Ordinance to allow depreciation allowance for plant and machinery used outside Hong Kong, particularly in the Greater Bay Area.

CARING FOR INDIVIDUALS

D. Development of Human Resources

As a result of the economic downturn and pressure faced by enterprises, we understand that some individuals might require totally different skills set and knowledge to cater to new employment or working environments in the coming year. Some individuals may also consider making use of their unpaid leaves in the outbreak period or business downturn to equip themselves with the new skills and knowledge.

RECOMMENDATIONS –

- Increasing Self-Education Allowance to $120,000 to encourage individuals to better equip themselves in the complex changing environment thereby reducing pressure to social security as well.
- Expanding the scope of Self Education Allowance from work-related education courses only to include new and different fields of educational courses.

PROMOTING CORPORATE SOCIAL RESPONSIBILITIES

E. Charitable Donations

During the outbreak of COVID-19 many enterprises and individuals initiated donation campaigns to donate to charitable organizations for procurements of surgical masks for distribution to under-privileged groups. However, presently only cash donations up to 35% of assessable profits for the year will be allowed as a deduction. This year, one can expect huge losses to be incurred or significant drop in income by many businesses and individuals. This may mean that NO or only very little deductions would be allowed for these kindhearted and socially responsible companies or individuals.

Donations to charitable institutions will surely relief part of the financial burden on the Government to demands and needs of the under-privileged groups and the educational and social welfare sectors during economic downturns.

RECOMMENDATIONS –

- Allowing 100% deduction for donations made by taxpayer to approved charitable organizations in the years of assessment 2020/2021 and 2021/22 even when the taxpayer did not have any assessable profits for the year; and

- Allowing deductible donations made in the Years of Assessment 2020/2021 and 2021/22 to be carried forward to future periods, PLUS allowing donations made in the years of assessment 2020/2021 and 2021/22 to be carried back one year which promotes corporate social responsibilities and improve community harmony.

F. Special Tax Deductions for Equipment, Medicines and Doctor’s Consultation Fees for The Elderlies

As the population in Hong Kong is aging at a very fast pace, it is vital that the whole Community in Hong Kong be equipped to embrace this change.

RECOMMENDATIONS –

- Special deductions should be made available for companies and individuals to develop equipment (including innovations in gerontechnology, e.g. wheelchairs, beds and other eldercare equipment) or renovations made especially for the use of elderly and the disabled.
- Exemptions for special fittings for elderly or disabled persons in Motor Vehicles First Registration Tax.

G. Empowering & Equality for Working Mothers

In this difficult period, we propose to introduce the following measures to encourage women to remain in or rejoin the workforce to help as a wage earner for families.

Many female homemakers who gave up their career to devote to their families possess high education level and precious working experience that can provide valuable manpower resources and keeps in the finances of the family. Some grassroots female homemakers who shoulder family burdens lack the incentive to work and/or seek subsidies from the Government. With the support from the Government, employers can attract talents, and Government's financial burden on public expenditure such as Comprehensive Social Security Assistance (CSSA) can be lightened.

RECOMMENDATIONS –

- Setting up a special Parental Program Fund so that, similar to other countries like Canada, UK or Singapore, etc., all maternity payments can be paid by the special Fund instead of having most of it being shouldered by individual employers. This will help to alleviate the inequality and discrimination against female employees and also help to encourage more women to rejoin the work force.

- Providing infrastructure support such as childcare service and flexible workplace arrangements for families with both parents working.

- Additional Childcare Allowances for extra help needed by a working mother.

REFORMING HONG KONG'S TAX SYSTEM

H. Reform Hong Kong's Tax System

2019/20 and 2020/21 are challenging years. The budgeted deficit of HK$139 billion for the current financial year (2020/21) is expected to increase to over $300 billion Our fiscal reserves will be reduced to around $800 billion, equivalent to around 12-13 months of government expenditure, close to the level after the SARS epidemic in 2003.

The unfortunate events in 2003, 2019 and 2020 clearly show that there are flaws and weaknesses in our tax system. Our revenue relies heavily on direct income tax, mainly Profits Tax and Salaries Tax. While government expenditure is stable and rigid, our revenue is relatively volatile depending on the economic conditions. In the circumstance, we are likely to face fiscal deficits during economic downturns.

We are well aware that a consultation was conducted in 2006/07 to reform Hong Kong's tax system for broadening our tax base. The consultation appeared to focus on 'Goods and Services Tax ("GST")'. While labeling the consultation as "Broadening the Tax Base", it appeared to us that the exercise aimed at increasing our government revenue since no deduction on direct income tax was proposed to set off any increased revenue arising from the study. The consultation recognized that our narrow tax base would limit our ability to allocate resources to invest for the future and to respond to challenges in the long run. Yet there was no consensus on any solution to the problem.

The consultation report in 2007 recommended that the Government should continue to study options for broadening the tax base and address the fundamental issue at a suitable time in the future. The matter was however held in abeyance probably because we managed to recover within a short spell of time in 2003. The situations nowadays are very different. It is estimated that the economic downturn we are now facing may take several years to recover.

RECOMMENDATIONS –

- We recommend reopening the study on the reform of our tax system. The study should:
  - (i) Aim at 'broadening our tax base' instead of 'increasing our revenue'.
  - (ii) Cover all options instead of limiting to a specific tax type.

REVIEWING THE INLAND REVENUE ORDINANCE ("IRO")

I. Review the Inland Revenue Ordinance ("IRO")

Our IRO was last reviewed in 1976. Since then, there have been tremendous changes all over the world. We are of view that changes are required in the following two areas:

(a) Achieve Neutrality and Equity Principles.
(b) Increase transparency and certainty.

(a) Achieve Neutrality and Equity Principles

The IRO provides different deduction requirements and tax rates for Profits Tax, Salaries Tax and Property Tax.

Deductions under Profits Tax, Salaries Tax and Property Tax are governed by section 16, section 12 and section 5(1A) respectively. Section 16 allows deduction for all outgoings and expenses incurred in the production of the assessable profits. Section 12 restricts deduction to outgoings and expenses wholly, exclusively and necessarily incurred in the production of the assessable income. Section 5(1A) limits deduction to 20% of the assessable value of the rental property.

In D102/03 (18 IRBRD 952), the Board of Review commented that the rules for Salaries Tax deduction, derived from ancient United Kingdom precedent, were enacted in a very different time to that existing in modern Hong Kong and that regard had to be paid to the inherent unfairness in the contrasting rules governing Salaries Tax and Profits Tax deductions. Likewise, we submit that it is unfair to refuse deduction claims exceeding 20% of the rental income if the excess is allowable under the general tax deduction rule.

In respect of tax rates, we appreciate Government's initiative to implement the two-tiered profits tax rate regime. The policy is however contrary to the neutrality principle since it does not extend to Salaries Tax and Property Tax. We submit that by extending the regime to Salaries Tax and Property Tax, more expertise or skilled professionals will be encouraged to work, and more property owners will be attracted to offer their vacant properties for rent.

(b) Increase Transparency and Certainty

The principal goat of taxpayers is to have their tax matters resolved fairly with finality. If they have made taxes that are not agreed by the tax administration, they would expect the tax administration to inform them as soon as possible. Finality is a basic right of taxpayers.

Taxpayers' right to finality is at present impacted by the definition for assessment and the objection provisions.

Section 60 limits an assessor's right to raise assessment or additional assessment to 6 years after the end of the year of assessment. Loss statement is not an assessment in terms of the IRO. There is no time limit for the Inland Revenue Department ("IRD") to challenge losses beyond 6 years.

Section 64(2) requires the Commissioner of Inland Revenue ("CIR") to adjudicate upon a taxpayer's objections within a reasonable time. The IRO does not define "reasonable time". The IRO also gives an absolute right to the CIR to make unconditional or conditional order in respect of the tax in dispute. If the CIR grants an unconditional stand over order, the taxpayer will have to suffer large interest on the tax stood over upon determination of the objections. If the CIR makes a conditional hold over order by purchasing a Tax Reserve Certificate ("TRC"), the taxpayer will be deprived of the use of the sums tied up in the TRC. In any event, taxpayers will suffer heavy financial loss by the IRD's delay. Yue Yuen Marketing Co., Ltd. v. CIR, HKAL 49/2009 and Dairy Farm Establishment v. CIR, HCAL 234/2018 are typical complaints in this respect.

The delay in determining objections is particularly obvious in field audit and investigation cases. By issuing repeated protective assessments, demanding purchases of TRCs and delaying determination of the objections, taxpayers under investigation or field audit are often forced to give in. In the USA, the right of finality under the Taxpayer Bill of Rights states, "Taxpayers have the right to know the maximum amount of time they have to challenge the IRS's position as well as the maximum amount of time the IRS has to audit a particular tax year or collect a tax debt. Taxpayers have the right to know when the IRS has finished an audit."

RECOMMENDATIONS –

- We recommend establishing a Task Force to review the IRO and to consider:

  (i) Extending the two-tiered tax rate regime to Salaries Tax and Property Tax;

  (ii) Allowing property owners an option to claim actual expenses incurred or the standard allowance of 20%;

  (iii) Relaxing the deduction provision for Salaries Tax by deleting the words "Wholly, exclusively and necessarily" from section 12;

  (iv) Defining loss statement as an assessment in order to provide finality for loss cases;

  (v) Defining "reasonable time" for the purpose of section 64(2) of the IRO regarding taxpayers' objections.

We will be happy to answer any further questions that you may have. Should you require more information, please do not hesitate to contact the undersigned or Ms. Elizabeth Law, Chairman of our Taxation Committee, or Mr. Chan Cheong Tat, Advisor to our Taxation Committee.

Yours sincerely,

LAU Kwok Hung, Kenneth
President

LAW, Elizabeth
Taxation Committee Chairman

Budget Submission Task Force of Taxation Committee

1. Law, Elizabeth (Chairman)
2. Chan Cheong Tat (Advisor)
3. Wong Lung Tak, Patrick (Deputy Chairman)
4. Chen Chi Hing, Andrew
5. Cheng Chung Man, Alan
6. Hui, Jane
7. Wong Chun Sek, Edmund
8. Lau Kwok Hung, Kenneth
9. Wu Chun Sing, Parco
10. Leung Pak Kee, Jason
11. Lok Kit Ying, Virginia
12. Yeung Chi Wai, Edwin

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The Society of Chinese Accountants and Auditors was formed in 1913 and incorporated in 1948. The CPA firms of which our members are partners, directors or managers, service a significant majority of businesses in Hong Kong, and also companies investing into or through Hong Kong. Our members directly and regularly communicate with clients, their directors and employees and consequentially understand their needs and concerns.