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8 November 2001

Clerk to the Legislative Council
(Attn: Ms Doris Chan)
Legislative Council
8 Jackson Road
Central
Hong Kong
(Fax: 2509 9055)

Dear Ms Chan,

**Bills Committee on Inland Revenue (Amendment) Bill 2001
Meeting on 8 November 2001**

Thank you for your letter of 6 November 2001. You asked for the Administration's views on the two proposals to amend the Inland Revenue (Amendment) Bill 2001 raised by Members at the Bills Committee meeting held on 5 November and for our assessment of whether the two proposals have charging effect as defined in Rule 57(6) of the Rules of Procedures of the Legislative Council. You would also like to know whether the Administration would take over the two proposals.

The Chief Executive announced in his 2001 Policy Address that the Government would propose to the Legislative Council an increase in the maximum amount of home loan interest deduction by 50%, from the existing level of \$100,000 to \$150,000, for the two years of assessment 2000/01 and 2002/03. The proposal seeks to ease the burden of home owners, during a period of economic difficulty. This proposal, in alleviating home owners' financial burden in respect of tax payment, will benefit over 110,000 taxpayers who are paying or will be paying an

amount of home loan interest in excess of the current tax-deduction ceiling for home loan interest. The maximum tax saving for a taxpayer will be \$8,500 per year, or \$17,000 for two years. Upon implementation of this concession proposal, the Government's revenue from Salaries Tax will decrease by \$1 billion.

The Administration has formulated the present proposal after taking into account various factors. We consider that a 50% increase in the tax-deduction ceiling lasting for a period of two years is appropriate. Our proposal will, on the one hand, provide timely and the most needed relief for home owners during a period of economic difficulty, and on the other, will not add undue pressure to our already very tight budget position. We believe our proposal has struck a good balance between providing relief and prudent fiscal considerations.

Proposal to extend the proposed increase in home loan interest deduction to beyond 2001/02 and 2002/03

At the Bills Committee meeting on 5 November, a Member asked the Administration to explain the rationale for limiting the proposed enhanced ceiling for home loan interest deduction to the two years of assessment 2001/02 and 2002/03 and not extend it to thereafter. She also requested the Administration to consider reviewing whether the enhanced level of deduction should be continued before the two year period had expired.

As explained above, we consider a 50% increase in the maximum tax-deduction ceiling for two years is appropriate in the present economic circumstances. Therefore, the Administration will not take over the proposed amendment to extend the two-year period. That said, we note Members' concern about the need to review the concession in future in the light of prevailing economic circumstances. Therefore, we will carry out a review on possible continuation of the enhanced tax-deduction ceiling in preparing for the 2003/04 Budget.

Proposal to raise the maximum home loan interest deduction from \$150,000 to \$180,000

Two other Members have proposed to further increase the tax-deduction ceiling for home loan interest to \$180,000 for the two years of assessment 2001/02 and 2002/03.

As explained above and as pointed out by the Secretary for the Treasury during the Second Reading of the Inland Revenue (Amendment) Bill 2001, the Administration considers that the present proposal to increase the tax-deduction ceiling for home loan interest from \$100,000 to \$150,000 per year for the current and the next year of assessment should provide immediate relief for home owners. Under our proposal, some 76,000 taxpayers with an annual income below \$600,000 will enjoy additional home loan interest deduction and reduction in Salaries Tax payable with a cost to Government revenue in the amount of \$280 million per annum. Another 37,000 taxpayers with an annual income over \$600,000 will enjoy reduction in Salaries Tax payable costing a reduction or revenue in the amount of \$240 million per annum. Under the proposal by Members, the further enhanced deduction will cost the Government revenue an additional \$90 million per annum for the 76,000 taxpayers in the first category, and another additional \$120 million per annum for the 37,000 taxpayers in the second category. The Members' proposal is therefore skewed towards the higher-income taxpayers in society. The Administration is therefore not in favour of the further increase proposal and will not take over the proposed amendment.

Charging effect of Members' proposals

The Administration considers both proposals have charging effect as defined in Rule 57(6) of the Rules of Procedure of the Legislative Council since, if implemented, each proposal would result in a reduction of revenue from a lawfully established source at a future date. Our view, illustrated with an analysis of the application of the Rule 57(6) of the Rules of Procedure to the second proposal, is attached at the Appendix.

In conclusion, without prejudice to our position on the application of certain Basic Law provisions relating to the operation of the Legislative Council, the Administration is of the view that both proposals raised by Members have charging effect as defined in Rule 57(6) of the Rules of Procedure of the Legislative Council, and they cannot be moved

by Members without the Chief Executive's consent in writing.

Yours sincerely,

(Miss Erica Ng)
for Secretary for the Treasury

c.c. D of Admin (Attn: Mr David Leung)

An Analysis on a proposal by Members to amend the Inland Revenue (Amendment) Bill 2001 to increase the tax-deduction ceiling for home loan interest to \$180,000

Based on legal advice, the Administration's considered view is that a proposal by Members to amend the Inland Revenue (Amendment) Bill 2001 to increase the tax-deduction ceiling for home loan interest from \$150,000 to \$180,000 has charging effect as defined in Rule 57(6) of the Rules of Procedure of the Legislative Council.

2. Rule 57(6) of the Rules of Procedure of the Legislative Council provides that -

“An amendment, the object or effect of which may, in the opinion of the President or Chairman, be to dispose of or charge any part of the revenue or other public moneys of Hong Kong shall be proposed only by -

(a) the Chief Executive; or

(b) a designated public officer; or

(c) a Member, if the Chief Executive consents in writing to the proposal.”

3. The key words in the rule are “**to dispose of or charge any part of the revenue or other public moneys of Hong Kong**”. In this context, “revenue” means the income of Hong Kong from which public expenses are met, and it is not restricted to income that has already been received or accrued due.

4. In other words, the concept of “revenue” has within it a clear meaning of prospective income in addition to that which has been received or accrued in the past. So, the revenue anticipated to be collected from the general public may properly be regarded as “revenue of Hong Kong” even though it may not as yet have accrued due. If the intention had been

to limit the powers of Members of the Legislative Council only in relation to revenue already collected, the phrase would have been “revenue collected” or “revenue received or accrued” and not “revenue of”. It follows from this that “to dispose of” with reference to “revenue of” must include any action which results in the reduction of revenue from a lawfully established source at a future date.

5. It is worth noting that, in May 1994, two Members of the then Legislative Council proposed to move amendments to a resolution proposed by the Administration. The then President of the Legislative Council made a ruling that the two amendments, which would reduce Government revenue, had charging effect. Those amendments sought to introduce a lower cap on rates increases and a lesser increase in rates than was proposed by the Administration. In that case, the President ruled that “revenue” meant the annual income of Hong Kong from which public expenses were met, and was not restricted to income that had already been received or accrued due. Therefore, it followed that to “dispose of” revenue must include any action which results in a lawfully established source of revenue no longer being receivable at a future date.

6. This also appears to be the position which Counsel to the Legislature had in mind as noted in paragraph 13 of the President’s ruling of 27 March 2001 on Hon Lau Chin-shek’s proposed resolution under Section 34(2) of the Interpretation and General Clauses Ordinance (Cap.1) in connection with the Public Revenue Protection (Revenue) Order 2001 -

“13. Counsel to the Legislature advises that as a matter of general principle, the “charging effect” restriction provided in Rule 31(1) of the Rules of Procedure applies to revenue which may be collected under statutory authority.”

7. In the present case, since the Inland Revenue Ordinance (Cap. 112) authorises the Government to collect Salaries Tax after permitting a maximum deduction of home loan interest of \$100,000 in a tax assessment year, the proposal by Members to permit a higher maximum deduction will reduce Government revenue from Salaries Tax because it will directly cause the taxpayers concerned to pay less Salaries Tax. It is very clear that the proposal has the effect of reducing “revenue” since the

Administration is presently authorised to collect the revenue which the proposal by Members is seeking to reduce.

8. Therefore, without prejudice to our position on the application of certain Basic Law provisions relating to the operation of the Legislative Council, the Administration considers that under Rule 57(6) of the Rules of Procedure of the Legislative Council, the proposal cannot be moved by a Member without the Chief Executive's consent in writing.