

March 11, 2005

The Hon. Tam Heung Man
Legislative Councillor
Room 421, West Wing, Central Government Offices
11 Ice House Street
Central
Hong Kong

Dear Ms. Tam,

Further to our meeting at The Chinese General Chamber of Commerce on March 8, 2005, I wish to echo your view that the current Inland Revenue Ordinance (IRO) which was enacted years ago is due for review. I wish to emphasize that the followings are purely my personal view and do not reflect the view of the Chamber.

A simple and efficient tax system based on the territorial concept has often been cited as one of the key success factors of the Hong Kong economy. However, as ways of doing business changes overtime the tax law has not been amended to cope with these changes. There are two points I wish to bring to your attention.

1. Sources of Profits Tax (“manufacturing”)

In the 1960’s and 70’s, Hong Kong had quite a number of manufacturing companies as cheap labour were easy to find. However, since 1980’s, a number of companies moved their manufacturing base to China to take advantage of the relative cheaper cost of production, initially as a processing factory, then in the form of joint venture company and finally in the form of wholly-owned foreign enterprises (“WOFE”). However, the Hong Kong Tax Ordinances were drafted in such a way either the profit is arising in or derived from Hong Kong offering no room for apportionment. The 50:50 apportionment of manufacturing profits is purely offered in the form of concession based on the Inland Revenue Departmental Practice and Interpretation Notes which do not have the force of law. In recent cases, the IRD has withdrawn the concessions they offered to the taxpayers six years ago requiring them to pay back taxes tax payers do not anticipate because the manufacturing arrangement with China has turned into a contractual joint venture or WOFE. This results in sudden cashflow problem for the taxpayers. Law requires certainty. It is a fundamental principal of

laws that no laws or practices should be retrospective. The current scenario is that virtually all Hong Kong manufacturing have been migrated to China and the customers are either in United States or Europe. There is no need to use Hong Kong Companies to do business anymore. Control of communications can be anywhere in the world. With the advent of the Macau Offshore Companies to exempt offshore income, if the IRD continues its current practice we can see most Hong Kong manufacturing companies will fled to other offshore jurisdiction thus causing ultimate loss of Hong Kong tax revenue.

Another point is that the concept of “onshore” and “offshore” is now quite obscure. Recent case decisions seem to import the concept of “central management and control” in its taxing ambit often used by OECD countries to tax Hong Kong Companies which has never been the intent of legislation. If such concept is applied and extended then Hong Kong Companies will be taxed on ‘worldwide’ income. Who then will come to Hong Kong to invest ?

2 Estate Duty

Estate Duty should be abolished because with the use of tax advisor it can be easily avoided. The burden is levied on the middle class families and the revenue it generates is negligible. With the abolishment of this tax, it is hoped that Hong Kong will attract wealthy people from other high tax jurisdiction to come to Hong Kong.

The above is just some of my shallow thought and I hope it will provoke further discussions and remedial actions to place Hong Kong in the high list of worldwide financial centers without loss of tax revenue in mind.

Yours sincerely,

(Original signed)

Dickson Wong

cc. The Honourable Bernard Chan J.P.