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( 庫 務 科 )  
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**FINANCIAL SERVICES AND  
THE TREASURY BUREAU  
(The Treasury Branch)**

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本函檔號 Our Ref. : FIN CR 1/2161/97  
來函檔號 Your Ref. : CB1/PL/FA

6 January 2005

Miss Salumi Chan  
Clerk to Panel  
LegCo Panel on Financial Affairs  
Legislative Council Building  
8 Jackson Road  
Central  
Hong Kong

Dear Miss Chan,

**Panel on Financial Affairs  
Item proposed by Hon Tam Heung-man  
And item referred by AJLS Panel**

I refer to your letter of 18 November 2004.

(a) Review of the Inland Revenue Ordinance

Regarding the review of the Inland Revenue Ordinance as proposed by the Hon TAM Heung-man in her letter to the Chairman of the Panel on Financial Affairs dated 28 October 2004 and in Mr Lloyd DEVERALL's letter to her, please note that the Administration held a meeting with Miss Tam and her tax advisors (including Mr Deverall) on 12 November 2004.

At the meeting on 12 November 2004, we explained to Miss Tam that while we saw no need for an overall review of the Inland Revenue Ordinance at this juncture, the Ordinance has been amended from time to time to meet changing needs. All these amendments were effected after detailed deliberation by the Legislative Council. As regards the interpretation of the existing law, we explained that guidance on many of such issues has been given by the Courts and the Board of Review, the decisions of which are binding.

The Administration welcomes views from the public on taxation-related matters. There are well-established consultation channels between the Administration and taxation professionals. One of such channels is the Joint Liaison Committee on Taxation (JLCT), which is formed by members from various chambers of commerce, legal, taxation and accountancy professions and academics. It holds regular meetings with representatives of the Financial Services and the Treasury Bureau, the Inland Revenue Department and the Department of Justice with a view to advising the Government on taxation matters. Invariably, we have consulted JLCT on major amendments to the Inland Revenue Ordinance before submitting a bill to the Legislative Council. JLCT has recently invited Miss Tam to join the Committee, and we note that Miss Tam has nominated a representative to attend the JLCT meetings.

----- In this connection, a copy of our reply to the relevant LegCo question raised by the Hon Tam Heung-man on 5 January is attached for reference.

The Administration would continue to listen to views of the industry and the public on taxation-related issues and keep our tax laws under constant review. We will maintain dialogue with the industry and interested parties. As regards the specific technical issues raised in Miss Tam's paper, we will refer them to the JLCT for comments/study and report to the Panel where appropriate.

(b) Proposal of granting tax relief to divorced persons paying maintenance to ex-spouses

As regards the proposal of granting tax relief to divorced persons paying maintenance to ex-spouses which arose from a LegCo Question dated 10 July 2002, we are preparing an information paper for the Panel and will send it to you in due course.

Yours sincerely,

(Miss Erica Ng)  
for Secretary for Financial Services and the Treasury

Encl.

### **LEGCO QUESTION NO. 3**

**(Oral Reply)**

**Asked by Hon TAM Heung-man**

**Date of Meeting : 5 January 2005**

**Replied by : Secretary for Financial Services and the Treasury**

#### **Question**

Regarding Hong Kong's tax system and tax assessment, will the Government inform this Council:

- (a) of the time when the last comprehensive review of the Inland Revenue Ordinance was conducted, and whether it has assessed if the current Inland Revenue Ordinance confers excessive discretionary powers on the Commissioner of Inland Revenue; if it has, of the assessment results; and whether it will consider conducting a comprehensive review of the Ordinance; if not, the reasons for that;
- (b) of the measures to enhance the fairness and transparency in tax assessment, and whether it will follow the practice of publishing the Assessors' Manual, which has been adopted in countries such as the United Kingdom and the United States of America, to inform taxpayers of the assessment criteria of the Inland Revenue Department; if not, the reasons for that; and
- (c) whether it has assessed if Hong Kong lags behind other developed economies in its tax system; if the assessment results show that Hong Kong's tax system so lags behind, of the authorities' strategies to eliminate such situation?

**Reply :**

Madam President,

(a) The last comprehensive review of the Inland Revenue Ordinance was carried out in 1976. Since then, the Administration has kept the various tax items under constant review in the context of the annual budget exercises and other policy review exercises. On a more technical level, the various provisions of the Inland Revenue Ordinance are also reviewed regularly to make sure that our taxation system is competitive in the global context. Enhancements are introduced to meet the ever-changing social and economic environment. All these amendments are effected after detailed deliberations by the Legislative Council. The Administration welcomes views from the public on taxation matters. Every year, the Financial Secretary organises budget consultations with legislators, political parties, professional bodies and organizations in related industries as well as members of the public.

In this connection, in 1987, in order to better and more systematically gauge the views of the practitioners and chambers on tax legislation, which could be very complex and highly technical, the Administration initiated and encouraged the establishment of the Joint Liaison Committee on Taxation (JLCT), the main liaison body between the Administration and the industry on taxation matters. The JLCT is an umbrella organisation comprising private sector representatives nominated by chambers of commerce, the Hong Kong Institute of Certified Public Accountants, the Taxation Institute of Hong Kong, the Law Society of Hong Kong, and the International Fiscal Association. It also invites members from the academic, legal as well as tax-related fields to attend its meetings from time to time. Representatives from the Legislative Council, the Financial Services and the Treasury Bureau, the Inland Revenue Department and the Department of Justice also attend JLCT meetings on a regular basis.

Invariably, the Administration consults the JLCT on all major amendments to the Inland Revenue Ordinance and other taxation legislation before submitting the relevant bills to the Legislative Council in order to make sure that the views of the industry and business

community are duly reflected in our legislative proposals. The JLCT is functioning well in providing a constructive forum for liaison between the Administration and representatives of the private sector, to formulate advice to the Government, and to conduct or sponsor researches and educational activities in connection with taxation matters. Various sub-committees are formed from time to time under the JLCT to study different taxation topics of interest, contribute to the drafting of the IRD's Departmental Interpretation and Practice Notes and provide advice on the drafting of tax legislation.

JLCT has recently invited Hon Tam Heung-man to join, and we note that Ms Tam nominated a representative to attend JLCT meetings. Ms Tam is welcome to make use of this channel to provide advice on taxation matters.

Other well-established consultation channels between the Administration and taxation professionals include the annual meeting between the Inland Revenue Department and the Hong Kong Institute of Certified Public Accountants.

As a result of the regular reviews and after consultation with the industry and tax professionals, legislative changes were made and implemented from time to time. For example, a total of 34 bills have been introduced into the Legislative Council since 1991 proposing various amendments to the Inland Revenue Ordinance. These amendments seek to introduce both policy and technical changes to keep our taxation regime competitive and up-to-date.

The Administration would also establish ad hoc committees and working parties to undertake in-depth study on specific issues, whenever there is such a need.

We consider that the present approach of keeping various tax items under constant review in annual budget exercises and other policy review exercises and reviewing various provisions of the IRO regularly with inputs from the industry, the profession and the business community through the various consultative channels including the JLCT is effective and efficient. At present, we do not see any genuine need for

conducting an overall review of the Inland Revenue Ordinance.

On the question of whether or not the existing Inland Revenue Ordinance gives excessive discretion to the Commissioner of Inland Revenue, the Administration is of the view that all the powers vested in the Commissioner under the Inland Revenue Ordinance are necessary for her to discharge the tax assessment and collection duties effectively in order to protect public revenue. Such powers were carefully deliberated by the legislature in the course of enactment. Besides, our tax and legal system has a well defined system of objection and appeal, which enables taxpayers to contest the judgements or assessments made by the Commissioner. For instance, the disagreements will be adjudged by the Board of Review, which is an independent statutory body established to determine tax appeals, as well as the independent courts. This mechanism provides very effective checks and balances on the discretionary power exercised by the Commissioner or other tax officials and has been operating effectively.

(b) Ensuring integrity and transparency in the exercise of tax-assessing duties are important objectives. Towards this end, the IRD has published a series of Departmental Interpretation and Practice Notes (DIPNs) setting out the Department's view on applications of the tax law and the usual practices in conducting the tax assessment functions. To facilitate taxpayers' access to such information, these notes are also published on the website of the IRD. The Department also has a statutory scheme of providing advance ruling on taxation matters. Rulings that may be of interest to the tax-paying public are published on the website. Other more important policies that may affect taxpayers, such as the policy of imposing penalty by way of Additional Tax on tax evasion offences, are also published on the IRD website for easy reference.

The Assessor's Manual serves as a training tool for newcomers to the Department and a procedural manual detailing the operation procedures for day-to-day assessing duties for individual officers. It should not be of much reference value to taxpayers or their representatives. The Administration does not think that publishing the Assessor's Manual will help enhance the transparency of the tax system. We will continue to

work with the JLCT to expand and update the DIPNs with a view to improving their usefulness and reference value to taxpayers.

(c) In terms of competitiveness, Hong Kong's tax system compares favourably with other tax jurisdictions. Hong Kong is well-known for its simple and low taxes. We adopt the territorial source concept in taxation. Only income arising in or derived from Hong Kong is chargeable to tax. These tax rates are very low compared to European, North American and some Asian countries. They are also lower than almost all of our neighbours in the Asian region. Besides, we do not have world-wide tax. Nor do we have any capital gains tax, dividends tax or interest tax. These other taxes are usually present in other tax regimes.

Apart from having low tax rates, our tax system is also very simple and fair. Certainty and simplicity in the taxation system are very important to foreign investors. We rank the first in 2005 (for the 11<sup>th</sup> consecutive year since the index's inception in 1995) amongst 161 places as the freest economy in the world by the Index of Economic Freedom published jointly by the Heritage Foundation and the Wall Street Journal. One of the criteria adopted in determining the ranking is taxation.

We are mindful that these advantages of Hong Kong's taxation regime should be maintained, and that we have to stay ahead of the global competition for investments. We have assessed and kept under constant review our tax system and our competitiveness with other tax jurisdictions.

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