

**Replies to the questions raised by Hon. SIN Chung-Kai,
Member of the LegCo Panel on Financial Affairs on the
Introduction of a Goods and Services Tax (GST)**

1. Structural fiscal problem

In response to media enquiries in late July, the Financial Secretary (FS), Mr. Henry TANG, referred to the reports by the “Task Force on Review of Public Finances” and the “Advisory Committee on New Broad-based Taxes”. He said that the former report pointed out that Hong Kong has a structural deficit while the latter report stated that if Hong Kong has a structural deficit, GST is the only new tax which is not incompatible with Hong Kong’s competitiveness.

It is stated in the “Final Report to the Financial Secretary by Task Force on Review of Public Finances” (“the Final Report”) submitted to FS in 2002 that ‘Should the deficits not disappear with the return of the economic cycle to “normal” levels, Hong Kong would be seen to have a structural fiscal problem.’ (Paragraph 53).

- a. The Government projected in the Final Report that even with a “higher” economic growth, the deficits will continue and all the fiscal reserves will be quickly used up after 2006-07 if the Government does not implement measures to increase revenue/reduce expenditure (see Table 1). Nevertheless, the Government surplus was \$14 billion and the reserves stood at \$310.7 billion as at March 2006. In the 2006-07 Budget, the Government also forecasts a surplus for the coming year. But the projection in the Final Report is different from the actual situation.

Table 1. In the “Final Report to the Financial Secretary by Task Force on Review of Public Finances”, the 2001-02 to 2021-22 projected budgetary positions based on a higher economic growth with the application of the “current policies” are as follows:

2001/02	2006/07 (projected)	2011/12 (projected)		2016/17 (projected)	2021/22 (projected)
Revenue (\$ billion)	174	277	380	535	754

Expenditure (\$ billion)	240	337	498	771	1,196
Surplus/Deficit (\$ billion)	-66	-60	-118	-236	-442
Fiscal Reserves (\$ billion)	369	92	-359	-1,274	-3,027

Source : Annex VIII to “Final Report to the Financial Secretary by Task Force on Review of Public Finances” (<http://www.fstb.gov.hk/tb/budget/budget02-03/tfr/english/annex8.pdf>)

Q i. Could the Government clarify the meaning of “Hong Kong would be seen to have a structural fiscal problem” referred to in the Final Report? Does it mean the continuance of the deficits even after “the return of the economic cycle to “normal” levels”? If yes, does it mean that Hong Kong no longer has “a structural fiscal problem” as there will be surplus over the next five years according to the Government’s projections in the Budget? If no, could the Government define “structural fiscal problem”?

A i: The 2002 Final Report reviewed the Government’s fiscal position at that time. The Report pointed out that there were indeed some structural problems in our public finances.

Shortly after the release of the Final Report, the Government took follow-up action and made a series of concrete recommendations in the 2002-03 Budget to stringently control government expenditure, which included reducing the civil service establishment and salaries, streamlining procedures, etc. The Government also followed the recommendations of the Final Report to tighten the guideline for government expenditure growth, which states that the nominal growth of government expenditure should not outstrip the nominal growth in GDP. At the same time, the Government also proposed appropriate measures to raise new revenue with a view to resuming fiscal balance in the government accounts in 2006-07. Therefore, in the 2003-04 Budget, the Government introduced a series of measures to increase revenue and reduce expenditure, which included reverting the tax bands and marginal tax rates under Salaries Tax to their levels in 1997-98, increasing the standard rate of Salaries Tax and the Profits Tax, a further cut of the civil servant establishment and salaries and introducing various measures to better utilize resources.

Hong Kong's economy rebound strongly after mid-2003. The real growth of our economy reached 8.6% in 2004 and 7.3% in 2005. In fact, it was a period of the fastest growth of our economy in the past two decades. However, reliance only on the additional revenue brought by economic recovery still could not solve the problem of budgetary deficit of the Government. If the Government had not introduced a series of measures to increase revenue and reduce expenditure in the 2002-03 and 2003-04 Budgets, we certainly could not resume fiscal balance in the government accounts in 2005-06 and recorded a surplus of \$14 billion. Singling out the two proposals to raise tax revenue and reduce the establishment and salaries of civil servants in the two Budgets had already brought some additional revenue and reduction in expenditure totalling \$23 billion for the Government in 2005-06.

According to the medium range forecast (MRF) in the Budget delivered in February this year, the financial position of the Government will remain sound. This is based on the growth of the economy over the past two years, and the expectation that the economy will remain robust and on an upward trend in the coming few years. Nevertheless, the fiscal reserve had reduced by \$190 billion between the seven-year period from 1998-99 to 2004-05.

It is pointed out in the Conclusions of the Final Report that "even when the economy returns to 'normal' growth, the budget deficits will remain and indeed worsen". This is based on a major assumption that the Government would follow the previous approach in managing its finances without introducing any reform measure. Obviously, the measures taken by the Government to increase revenue and reduce expenditure in the 2002-03 and 2003-04 Budgets are some of the major factors in achieving the surplus in 2005-06. However, in the long run, Hong Kong still faces the problems of volatile public revenue and serious ageing of population. As a responsible government, we must be vigilant in peacetime. We must continue to address the flaws and weaknesses of the existing tax system to make it more viable. This will ensure that the Government will be able to respond to the challenges posed to public finances arising from the rapid ageing of the population.

Overall, there are still some fundamental flaws in our public finances. In terms of revenue, they include the following: (1) Hong Kong's tax base is very narrow and we have limited range of tax types. We are particularly reliant on revenues from land sales and property-related taxes, which are highly sensitive to economic conditions and are unstable; (2) Investment earnings from accumulated reserves is also easily susceptible to external conditions; (3) With the ageing of population, the workforce will be on the decrease. This means if the Government continues to rely on income taxes as the main source of revenue, it will be exposed to an increased risk of financial instability. In

terms of expenditure, they include the following: (1) We have implemented vigorous measures to contain expenditure in recent years and there is very limited scope for further cuts; (2) An ageing population will add burden to the medical and welfare expenditure. Particularly in respect of medical expenditure, medical costs will increase substantially with the advance in technologies. These fundamental problems are not closely related to overall economic cycles; they mainly demonstrate the problems that have arisen from the incompatibility of the structure of government revenue with economic and social structural changes.

Q ii. Further to the above question, how do you define the “normal” growth trend in the expression “when the economy returns to a ‘normal’ growth trend”?

A ii: The expression “when the economy returns to a ‘normal’ growth trend” in general means that the economy has bottomed out and expands continuously at a rate in line with the growth trend.

Q iii. In the Budget delivered in February 2006, Mr. Henry TANG, FS, forecast that the Government would have a surplus in the coming five years up to 2010/2011 (See Table 2), and that the surplus would build up. This is contradictory to the worsening deficit as projected in the Final Report. Could the Government tell us which better reflects the present situation of Hong Kong, the projection in the Final Report, i.e. the deficit will worsen, or the MRF in the Budget, i.e. the government surplus will increase?

A iii: As pointed out in “A i”, had the Government not strictly taken measures to increase revenue and reduce expenditure over the past few years, the financial position in the medium term projected in the Final Report would probably occur.

The MRF in the Budget delivered by the Financial Secretary in February this year has already taken into account the results achieved by the cost-saving measures taken in the past few years, the economic growth in the past two years and the expected solid economic growth in the coming few years. The figures projected in the Budget announced in February this year reflect the present situation in Hong Kong.

The forecast in the 2006-07 Budget is not comparable to the references and assumptions used for the projection in the 2002 Final Report. During the period, we have introduced quite a few new government policies that have affected the public finances. Thus, we should not compare the two projections.

Table 2. The medium range forecast in the 2006–07 Budget

2006/07	2007/08 (forecast)	2008/09 (forecast)		2009/10 (forecast)	2010/11 (forecast)
Revenue (\$ billion)	257.3	268.7	289.6	291.8	309.2
Expenditure (\$ billion)	251.7	258.4	266.4	272.7	276.6
Surplus/Deficit (\$ billion)	5.6	10.3	23.2	19.1	32.6
Fiscal reserves (\$ billion)	306.4	316.7	339.9	359.0	391.6

Source: Paragraph 82 of the 2006-07 Budget Speech

(<http://www.budget.gov.hk/2006/eng/budget27.htm>)

Q iv. Further to the above question, if the Government considers that the projection in the Final Report is more applicable, is the MRF in the Budget too optimistic? Will the Government have deficits in the coming five years?

A iv: Please refer to “A i” and “A iii”.

Q v. Further to Qii, if the Government thinks that the MRF of the 2006-07 Budget can provide a more accurate picture of the current situation of Hong Kong, is the forecast in the Final Report too pessimistic? Is it still applicable? If the forecast is considered to be too pessimistic, will the conclusion that Hong Kong would be seen to have a structural fiscal problem derived from it become untenable?

A v: Please refer to “A i” and “A iii”. Please also note that the fundamental problems mentioned in the Final Report, including the pressure brought about by the ageing population on public finances, are still problems that need to be addressed by the Government. Even if the impact of ageing population does not emerge in the coming five years (i.e. the time frame of the MRF), ageing population, narrow tax base and unstable source of revenue will have serious impacts on the fiscal health of the Government in the long run. As such, the directional projections of the Government’s

long-term fiscal position in the Final Report can still serve as a useful reference. Therefore, the Government should face up to these long-term problems and plan ahead. Otherwise, there may be a risk of budgetary imbalance again in our public finances when there is another economic downturn and in the stage of serious ageing of population, which will lower our ability to provide various public services, including education, medical and social welfare services.

Q vi. If the Government thinks that there is still a structural financial problem in Hong Kong, what are the reasons for that?

A vi: As pointed out in “A i”, the Government must face up to and address the weaknesses of the existing financial system, particularly the narrow tax base of Hong Kong, limited tax types and the Government’s heavy reliance on unstable property and investment related revenue. On the other hand, the public expenditure is rigid and the problem of ageing population is approaching. With fewer people in the workforce, the tax base of Salaries Tax will shrink gradually (For details, please see “A i”). Ageing population will increase the demand for healthcare services. The number of elderly receiving CSSA has nearly doubled in the past 10 years and the related expenditure increased more than 200%. At present, the Hospital Authority’s expenditure on elderly healthcare has reached 46% of its total expenditure. It is estimated that the number of elderly will increase by 1.5 times in the coming 25 years. One can imagine the financial pressure to be borne by the Government. Therefore, the Government must seize the opportunity to study the long-term arrangement for our public finances. In this connection, we consider that reform on tax system and broadening of tax base are feasible options in addressing the fundamental weaknesses of the existing tax system.

b. The Final Report pointed out that, “a fundamental change” had occurred in the property market and it was one of the factors giving rise to structural problem in the government revenue. Could the Government provide the following data for the period from 2001-02 to 2005-06?

Q i. Revenue from land premium (data of Table 8 in the Final Report)

A i:

Revenue from Land Premium					
Financial Year	2001-02 \$billion	2002-03 \$billion	2003-04 \$billion	2004-05 \$billion	2005-06 \$billion
Revenue from Land Premium	10.3	11.5	5.4	32.0	29.5

Q ii. Revenue from stamp duty on transfer of immovable property (data of Table 9 in the Final Report)

A ii:

Revenue from Stamp Duty on Property Transactions					
Fiscal Year	2001-02 \$billion	2002-03 \$billion	2003-04 \$billion	2004-05 \$billion	2005-06 \$billion
Stamp Duty	4.4	4.2	5.0	9.2	9.5

Q iii. Contribution to Profits Tax revenue from the property and banking sectors

A iii:

Contribution to Profits Tax Revenue from the Property and Banking Sectors					
Financial Year	2001-02 \$billion	2002-03 \$billion	2003-04 \$billion	2004-05 \$billion	2005-06 \$billion
Property Sector	5.7	6.0	6.6	9.6	Not Available
Banking Sector	7.0	6.6	9.8	12.6	Not Available
All Corporations	35.0	38.1	46.5	58.1	Not Available

Remarks: The Profits Tax returns for the 2005/06 assessment year were sent out in April 2006 and the assessments have not been completed. The Inland Revenue Department can provide the figures only until April 2007.

2. Consumption Tax

The “Broadening the Tax Base, Ensuring our Future Prosperity – What’s the Best Option for Hong Kong” Consultation Document (the Consultation Document) points out that “Hong Kong’s tax base stands out as clearly lacking in its low reliance on taxes from goods and services. Hong Kong’s reliance on consumption taxes was 17.8%. This is in contrast to the OECD economies, where consumption taxes accounted for over 31% of total tax revenue.” However, the Consultation Document shows that (see Table 3) consumption tax is the third largest source of revenue in Hong Kong and has even overtaken the “property-related taxes”. “Consumption tax” accounts for 17.8% of government revenue, close to the 31.8% of the OECD. On the contrary, the “social security tax”, which is an important tax of the OECD, is not implemented in Hong Kong.

Table 3. HK vs OECD – percentage of various taxes in the total revenue

	HK	OECD
Profits Tax	35.9%	9.3%
Personal Income Tax	27.2%	25.6%
Social Security Tax	0.0%	25.7%
Payroll Tax	0.0%	0.9%
Property-related Taxes	17.7%	5.5%
Consumption Tax	17.8%	31.8%
Other taxes	1.4%	0.9%

Source: Chart 1 in paragraph 19 of the “Broadening the Tax Base, Ensuring our Future Prosperity – What’s the Best Option for Hong Kong” Consultation Document.

Qa. Will the Government consider the tax base as broad only when Hong Kong’s tax composition and distribution are consistent with those of the OECD or other countries? If yes, will the Government follow the OECD and introduce the Social Security Tax, or substantially reduce the Profits Tax and “property-related taxes”?

Aa: Whether the tax base of a jurisdiction is narrow can be evaluated in two aspects. One is the number of tax items on which the government revenue relies on and the other is the number of the taxpayers. The Government does not intend to (and should not) fully apply the tax composition of other countries to Hong Kong. We are trying to develop a tax system suitable for Hong Kong and our future development. The specific design of the tax system should consider many factors, including the needs of the community (e.g. distribution of population), the pattern of public expenditure, the tax regime (e.g. types of tax, population of taxpayers) etc. By comparing the percentage of various taxes in the total revenue between Hong Kong and the OECD in the Consultation Document, the Government hopes to illustrate Hong Kong's tax base in a simple manner. Since the OECD consists of developed countries, we believe that it is appropriate to make such a comparison.

Qb. Further to the above question, if the answer is no, in view of the fact that the consumption tax already accounts for nearly 20% of Hong Kong's total tax revenue, what is the share of the consumption tax in the total tax revenue that the Government considers to be broad-based?

Ab: The Government does not think that the amount of tax revenue can represent the broadness of the tax base. The broadness of the tax base is measured by the scope of tax items covered and the number of taxpayers. At present, we only impose taxes on a limited range of commodities, such as excise duties, betting duty, hotel accommodation tax, air passenger departure tax and motor vehicle first registration tax. Therefore, though the consumption tax accounts for nearly 20% of the total tax revenue, the actual consumption tax base remains narrow.

3. Tax systems of OECD economies

Please list when in the past decade the OECD economies revised the tax rates of the following taxes: profits tax, personal income tax, social security tax, payroll tax, property-related tax and consumption tax.

A: We have no such information. Members may contact the relevant organisations direct for the information.

4. Income tax

It is stated in the Consultation Document that “many economies have cut income tax rates” and that the increase of our Salaries Tax in 2003 “has undermined our attractiveness to international talent”.

Qa. Please list the allowances for income tax, the tax bands and the marginal tax rates of OECD economies, Singapore, Taiwan and the Mainland China.

Aa: We have no such information. Members may contact the relevant organisations direct for the information.

Qb. The Government increased the Salaries Tax and other taxes in 2003 because of the deficit at the time. However, the Government has now returned to a fiscal surplus, and our fiscal reserves stand at \$310 billion. Besides, it is pointed out in the Consultation Document that a tax increase will “undermine our attractiveness to international talent”. If the Salaries Tax rate is reverted to the 2002-03 level, government revenue will be reduced by about \$5 billion. With a surplus of \$14 billion last year, the Government can certainly meet the expenditure needs. If cutting the Salaries Tax is considered so important for retaining talent, then why doesn't the Government revert the Salaries Tax rate to the 2002-03 level?

Ab: The Government is aware of the importance of Salaries Tax system and rate in attracting and retaining talent in Hong Kong. However, in reviewing the tax rate, we must take into account our fiscal position and other important factors. For example, whether there is room to cut Salaries Tax rates without affecting the fiscal balance, the long-term provision of public services and the necessary administrative expenditure. For this reason, in considering whether to revert the Salaries Tax rates to the 2002-03 level, we must also ensure that the stability of public finances will not be undermined. According to our study, if the problem of the narrowness of our tax base can be solved, there will be wider room for the Government to reduce Salaries Tax rate.

5. Tourist Refunds

The Consultation Document proposes that the threshold for tourist refunds be set at “\$1,500 for purchases in a shop”. According to the figures provided by the Tourism Board, the consumption of most tourists in Hong Kong concentrates on “shopping” and “expenditure on hotel” (see Table 4).

Table 4 Consumption of tourists in Hong Kong

Regions	Per capita spending of an overnight tourist in 2005 (HK\$(a))	Shopping		Hotel bills	
		As percentage of the total tourists' consumption (%) (b)	Average expenditure (HK\$) (= a x b)	As percentage of the total tourists' consumption (%) (b)	Average expenditure (HK\$) (= a x b)
America	5477	28.4	1555.5	45.5	2492
Europe, Africa and Middle East	5331	31.8	1695.3	40.4	2153.7
Australia, New Zealand and other South Pacific countries	5068	41.0	2077.9	33.4	1692.7
North Asia	4300	40.3	1732.9	31.7	1363.1
South Asia and South East Asia	4377	44.7	1956.5	28.5	1247.4
Taiwan	4916	53.4	2625.1	22.4	1101.2
Mainland China	4554	65.4	2978.3	11.4	519.16

Source: Hong Kong Tourism Board

Qa. According to the projections in Table 4, tourists cannot obtain any refunds unless they make all purchases in the same shop. What impacts does the EDLB think such an arrangement will have on tourists' consumption in Hong Kong?

Ab: Because of the proposed low GST rate, the Government expects that the impact of GST on price of commodities would be moderate and one-off. Hence, we expect at this

stage that GST and its refund arrangements would have limited impact on tourists' consumption in Hong Kong. However, we welcome views and comments from the public on the proposed tourist refunds threshold of \$1,500 for purchases in each shop.

Qb. Please provide the information for 2005 in the following table:

Overnight Visitors

Regions	Number of overnight visitors in 2005	Median expenditure of overnight visitors on shopping (HK\$)	Number of overnight visitors with spending less than \$1,500 on shopping	Median expenditure of overnight visitors on hotel bills (HK\$)	Number of overnight visitors with spending less than \$1,500 on hotel bills
America	1,196,735	300	908,442	1,321	653,537
Europe, Africa and Middle East	1,271,423	425	915,806	1,203	730,051
Australia, New Zealand and South Pacific countries	494,554	700	323,735	1,020	312,311
North Asia	1,190,211	550	839,099	823	870,520
South Asia and South East Asia	1,777,379	667	1,214,128	587	1,361,828
Taiwan	619,886	810	386,065	705	505,827
Mainland China	8,029,705	1,021	4,533,571	0 ¹	7,351,998

Remarks 1 : More than half of the overnight visitors from the Mainland China stayed at homes of their relatives and hence their median expenditure on hotel bills was zero.

6. GST to be paid by the Government

Paragraph 138 of the Consultation Document points out that the Government would have to account for input and output tax.

Qa. According to the Government's estimates, how much gross and net GST would the Government have to pay if the tax is introduced?

Aa: As the proposals are now only at the consultation stage, we are still awaiting public views before we can proceed to the next stage and to determine the implementation details of the proposed GST framework. Thus, we cannot predict at this moment the amount of gross and net GST to be paid by the Government.

Qb. What is the definition of "those supplies that were commercial in nature or in competition with the private sector" in paragraph 139 of the Consultation Document?

Ab: Based on the principle of fair competition, both public and private sectors are regarded as "taxable persons" under the proposed GST regime. The Government would have to tax those supplies that were commercial in nature or in competition with the private sector. In simple terms, "those supplies that were commercial in nature or in competition with the private sector" refer to those government services that same or similar services can be provided by the private sector, e.g. postal services and carparks, and not those services that are mandatory and/or regulatory in nature, e.g. vehicle licensing and business registration.

The Government currently levies around 5 000 fees and charges, which would be classified according to the basis of whether they were commercial or mandatory and/or regulatory in nature, so as to determine whether GST should apply. For the avoidance of doubt, all taxable government fees and charges would be explicitly stated and regulated under any future GST law.

Qc. What is the estimated administration cost to be incurred in the payment of GST by the Government itself?

Ac: International experience indicates that the ongoing administrative cost for the Government to collect GST would be approximately 1% to 2% of the net GST revenue. Given Hong Kong's lack of the necessary infrastructure to collect GST, the administrative cost would be closer to 2% in the initial years due to the need to set up

and operate the new systems. Such expense would include the administrative cost for handling of payment of GST by the Government itself. Since the proposed GST framework would be finalised only after collection and study of public views, we cannot calculate at present the administration cost to be incurred in the payment of GST by the Government.

7. GST credit for water and sewage charges

With regard to the \$500 GST credit for water and sewage charges proposed for households, please provide the following information:

Qa. The number of households paying annual water and sewage charges of over \$500 in the past five years;

Aa: Due to the existing independent operation of the water and sewage charges accounts, we can only provide the numbers of households paying each charge of more than \$500 per year at below for reference. However, it is proposed that households paying annual water and sewage charges of more than \$500 would be entitled to the full credit of \$500.

Financial year	No. of households paying annual water charge of more than \$503 [i.e. with water consumption of 50 units or above] (1 000 households)
2001-02	831
2002-03	865
2003-04	915
2004-05	918
2005-06	897

Financial year	No. of households paying annual sewage charge of more than \$500 [i.e. with water consumption of 152 units or above] (1 000 households)
2001-02	22
2002-03	22
2003-04	23
2004-05	24
2005-06	22

Qb. Please provide a breakdown by every \$100 increment of the number of households paying annual water and sewage charges of less than \$500 in the past five years.

Ab: Due to the existing independent operation of the water and sewage charges accounts, we can only provide the numbers of households paying each charge of less than \$500 per year at below for reference. However, it is proposed that households paying

annual water and sewage charges of more than \$500 would be entitled to the full credit of \$500.

No. of households paying annual water charge of equal to or below \$503 (1 000 households)						
Financial year	\$0 (0-12 units)	\$1-100 (13-20 units)	\$101-200 (21-28 units)	\$201-300 (29-36 units)	\$301-406 (37-44 units)	\$407-503 (45-49 units)
2001-02	367	194	212	210	213	128
2002-03	374	197	213	219	218	130
2003-04	375	196	208	220	216	130
2004-05	374	199	218	226	223	135
2005-06	372	212	231	236	233	134

No. of households paying annual sewage charge of equal to or below \$500 (1 000 households)						
Financial year	\$0 (0-12 units)	\$1-100 (13-40 units)	\$101-200 (41-68 units)	\$201-300 (69-95 units)	\$301-400 (96-123 units)	\$401-500 (124-151 units)
2001-02	322	683	585	260	88	28
2002-03	338	697	608	273	92	29
2003-04	340	699	617	289	101	33
2004-05	331	709	635	296	103	33
2005-06	329	753	635	285	78	51

Qc. Does the Government think that the “GST credit” of \$500 would cause an unnecessary increase in the public’s water consumption, resulting in water wastage?

Ac: The proposed “GST credit” of \$500 for water and sewage charges is to relieve most families of the financial burden arising from the imposition of GST. The Government believes that Hong Kong people are rational, and they are fully aware of the need to save water. Therefore, we are not worried that the public would waste water in order to take full advantage of the credit for water and sewage charges.

Qd. Has the Government planned to increase the water and sewage charges with a view to raising the cost recovery rates? If yes, would the provision of the credit of water and sewage charges for households as a result of the introduction of GST affect the plan of raising the cost recovery rates?

Ad: The Government has frozen most fees and charges, including water and sewage charges, during the period between 1998 and 2003 as an exceptional measure to alleviate the financial burden on the public in times of economic difficulty. In view of the economic recovery, FS announced in the 2004-05 Budget that the Government fees and charges would be reviewed by phases. The exercise is an on-going one. The relevant Bureaux will examine the best option to revise the fees that are related to the livelihood of the public, including water and sewage charges. In reviewing the fees, we will fully consider public acceptability and affordability.

It is envisaged that the proposed GST credit will not have any effect on the cost recovery rates which will be calculated as if the credit does not exist.

8. Cash allowance provided for low-income households not drawing CSSA

The Government proposes to provide an annual cash allowance of \$2,000 for low-income households not drawing CSSA and employ a self-identification system.

Qa. Paragraph 168 of the Consultation Document indicates that a set of objective criteria would be adopted to assess whether self-identified households are eligible for the allowance. What “objective criteria” would be used for assessing which households are low-income?

Aa: In the Consultation Document, we assume that the low-income households are those households not drawing CSSA, but with income within the lowest 20% income households in Hong Kong. According to the data obtained from the Household Expenditure Survey, they include approximately 400 000 households with monthly income of less than \$11,000. Since the Government does not have a database to identify this group, we intend to adopt a self-identification system whereby households belonging to this group would have to apply to the Government. Applications would then be assessed against a set of objective criteria. At the present stage, we have not yet decided on how to define this group of low-income households that need additional assistance. Hence, we also have not yet set any criteria for assessing applicants’ income. Anyhow, the criteria would ensure assistance be provided to all those in genuine need. We will listen to the views of the public in this respect during the consultation period, and then develop a set of objective criteria for assessing the eligibility for cash allowance.

Qb. According to the Government’s estimates, how many households would be eligible for this allowance? What is the percentage of low-income households who would apply for this allowance? And how many applications would the Government need to process?

Ab: For the purpose of this consultation exercise, we estimate that approximately 400 000 households with household income within the lowest 20% but not drawing CSSA would be relieved by the proposed cash allowance. The percentage of low-income households who would apply for this allowance and the number of applications that the Government would need to process depend on the assessment criteria to be developed and the response of the eligible households to the allowance. It is difficult to make an assessment at this stage.

Qc. Which department would be responsible for making the assessment, the Social Welfare Department, the Inland Revenue Department or other government departments?

- Ac: Which department will be responsible for making the assessment is an administrative arrangement. We will make a decision on it only when we have decided to implement the above measures.
- Qd. If the assessment is to be made by the Social Welfare Department, will the Government worry that there would be a labelling effect on low-income households, thus deterring them from applying for the cash allowance?
- Ad: The purpose of the cash allowance is to offset the impact on purchasing power of eligible households as a result of the GST introduction. It is not a welfare measure. We therefore do not think that applicants would be deterred from making applications for fear of being labelled.
- Qe. In granting the allowance, does the Government need to re-assess the eligibility of an applicant every year?
- Ae: Whether the Government needs to re-assess the eligibility of an applicant annually is a detailed implementation arrangement. We will make a decision on it only when we have decided to implement the above measures.
- Qf. According to the Government's estimates, what additional administrative expenses will be incurred every year for making the assessment alone?
- Af: Since we have not yet determined the specific administrative arrangements of the assessment, it is impossible for us to estimate at this stage the additional administrative expenses that will be incurred in this particular task every year.
- Qg. According to the Government's plan, would making a false declaration in order to obtain the allowance be a criminal offence?
- Ag: In principle, the Government thinks that making a false declaration in order to obtain the cash allowance, like making a false declaration to obtain other allowances, would be a criminal offence. The details will be examined after we have decided to implement the above measures.

9. Administrative cost

The Government estimates that the administrative cost for collecting GST will be approximately \$0.5 billion. What are the areas covered by the cost and what is the estimated cost involved in each area?

A: International experience indicates that the ongoing administrative cost for the Government to collect GST would be approximately 1% to 2% of the net GST revenue. Hence, we estimate that the administrative cost for the Government to collect GST will be approximately \$0.5 billion. According to our understanding, the administrative cost of 1% to 2% of the net GST revenue in other jurisdictions has already taken into account of expenses incurred in all respects of work for the implementation of the tax.

10. Tax burden on the public

According to the Government's estimates, if all revenue from GST were used to reduce Salaries Tax after the introduction of GST (i.e. Option 1), would the tax burden on the following groups/families be increased or reduced, and what would be the increase or decrease?

A: Even if the income is the same, families with different combination of family members (e.g. number of children and number of dependents, etc.) will enjoy different tax relief. Thus, the adjustment of tax burden for each income group after the Salaries Tax reduction cannot be calculated without such information.

11. Experience of Singapore

Singapore introduced GST in 1994. Please provide the following information for reference of Panel on Financial Affairs:

Qa. What were the reasons for Singapore to introduce GST?

Aa: We have no such information. Members may contact the relevant organisations direct for the information.

Qb. Please provide information about Singapore with respect to the following items for the period between 1990 and 2005:

- i. Income Tax
- ii. Property Tax
- iii. Stamp Duties
- iv. Estate Duty
- v. Betting Duty
- vi. Private Lotteries Duty
- vii. Goods and Services Tax
- viii. Total tax revenue (including tax revenue collected by the Inland Revenue Authority and the Customs and Excise Department)
- ix. Total revenue of the government
- x. GDP and gross domestic product deflator
- xi. Consumer Price Index

Ab: We have no such information. Members may contact the relevant organisations direct for the information.

October 2006