

STATEMENT ON THE REVENUE BILL 2003
From the
MOTOR TRADERS ASSOCIATION OF HONG KONG
15 MAY 2003

Introduction

The Motor Traders Association of Hong Kong (MTA) is grateful to be called before this Committee today to share MTA's views on the 2003 Revenue Bill as it relates to the proposed changes to the motor vehicles first registration tax (FRT).

MTA members represent by far the largest group of auto distributors/retailers in the Territory. Our members sold 90% of all new cars in Hong Kong last year. The MTA is pleased that the Government has suggested the waiving of all tax-exempt items in their proposed new FRT, and has proposed the introduction of a simple progressive structure for the new FRT system.

As members of this Committee may already know from our advocacy on the Public Revenue Protection (Revenue) Order for 2003, the MTA has consistently worked to find a balance between the Government's proposed budget changes and the realities of the current automotive market. We are committed to a fair and just result for all parties – the Government, consumers and the motor trade (who are employers of some 12,000 staff in Hong Kong). We firmly believe a win-win solution is possible on this issue.

Government's Rates and MTA's Proposal

The MTA sees the proposed high tax rates as severely damaging in their effect on the automotive trade in Hong Kong. This in turn would not generate the increase in revenue that the Government is seeking.

In response, MTA members have developed a proposal that revises downwards the Government's proposed FRT rates, to a level that still provides significant additional revenue to the Government without severely penalising the motor trade or consumers. It should be emphasized at the outset that the MTA believes these recommended levels are maximum rates tolerable to the market. Lower rates would clearly be welcome, though we acknowledge the Government's tax-raising imperative, and the need for the motor trade to play its part in ensuring the Government meets its revenue targets.

Our proposal is outlined in the following chart:

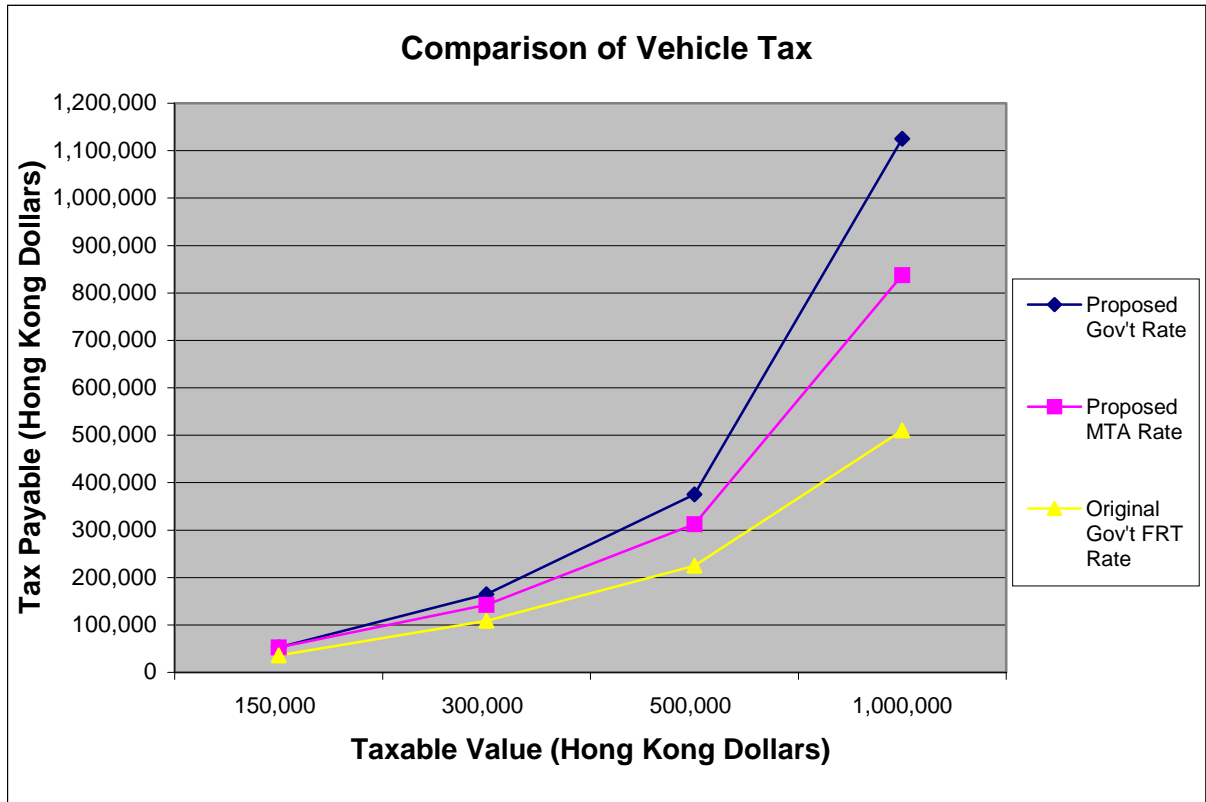
Comparisons of FRT Proposals

Taxable Value	Government's Previous FRT Rates*	Government's Proposed New FRT Rates	MTA's Proposed FRT Rates
<HK\$150,000	40%	35%	35%
HK\$150,000 to HK\$300,000	45-50%	75%	60%
HK\$300,001 to HK\$500,000	50%	105%	85%
HK\$500,001 and beyond	60%	150%	105%

*These figures do not include a number of exemptions not allowed in the new tax structure

The above chart clearly shows that the MTA's proposed rates are a compromise between the old FRT scheme and Government's new figures. MTA, with its calculations, has sought to create a smooth and progressive tax structure that compares favorably with the Government's proposal (which dramatically penalizes the more expensive sectors of the market). On behalf of all of our members, who represent all sectors of the market, the MTA believes that this approach would be fairer to all sectors, would keep job losses to a minimum and would ensure that no segment of the market is more savagely impacted than others.

The following graph shows the tax difference between the two proposals versus the original FRT, covering vehicles within four different price ranges (before tax): \$150,000, \$300,000, \$500,000 and \$1,000,000. MTA's proposed rate is a median between previous and proposed Government figures, thereby offering greater balance within each market sector.



Some of our members only operate in the single-brand high-end price sector, distributing automobiles such as Porsche and Ferrari, and they do not have the capacity to diversify their inventories. These dealers are already under enormous pressure because their operating expenses have been hit by extreme tax increases on their sector of the market. It is in no one's interest to see their businesses taxed out of the marketplace.

The Government argues in its paper that some in the trade could adjust their pricing structures to accommodate the tax increases. But margins are already extremely thin in this weak market environment and to try and support what could be substantial increases in costs for consumers would drive many motor traders deep into losses. That, together with the current gloomy economic circumstances, would mean very few distributors would have the ability to adjust their margins to make up for what is in some cases a +40% increase on the retail price due to the new FRT rates.

In addition, foreign exchange rates have already cut deeply into dealer margins. In the past year, the EURO to Hong Kong Dollar rate has moved from 7.05 to 8.87, a 25% increase. The story for the Japanese Yen is similar, with the rate rising from 0.061 to 0.0665, or a 9% increase. Manufacturers bill in their home currencies and Hong Kong dealers have been required to absorb these rate changes rather than pass them along to the consumer. The Government needs to understand the gravity of the foreign exchange impact on our industry and realize there is very minimal flexibility in our margins.

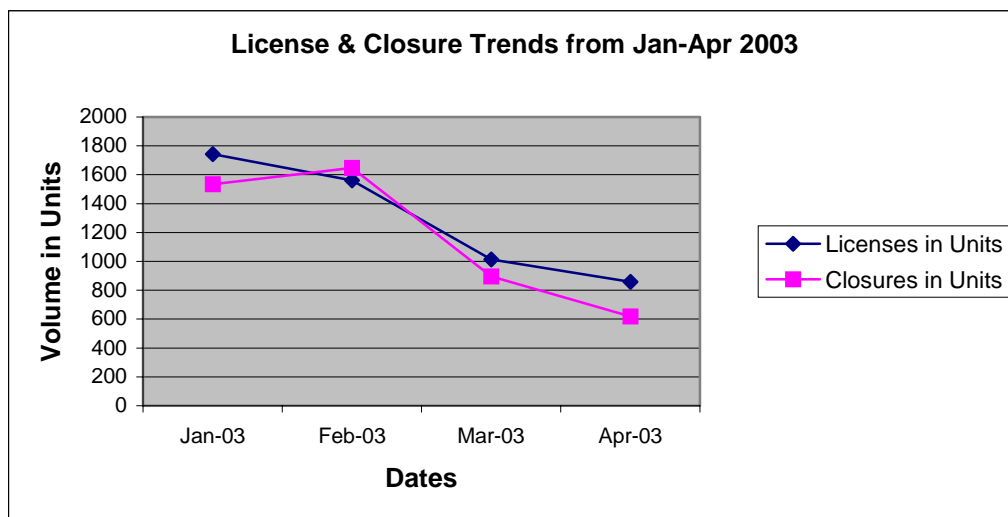
Impact on Sales

The Government argues that the introduction of higher FRT rates would only cause a short-term dip in new car sales. We did not believe this claim to be well founded even before the SARS outbreak. In the wake of SARS, we must now strenuously object to this assessment. The high tax rates, together with today's dire economic straits, have already had a catastrophic impact on our sector. The charts below show the downward trend of licenses and closures over the past four months. Licences in units in April plummeted by 51 per cent when compared with January. Closures in units dropped by 60 per cent during the same period.

License and Closure Records January to April 2003

Date	Licenses in Units	% Change from January	Closures in Units	% Change from January
January 2003	1742	***	1534	***
February 2003	1562	-10%	1647	7%
March 2003	1014	-42%	896	-42%
April 2003	858	-51%	619	-60%

(Figures provided by leading MTA members)



In view of the exceptionally negative business outlook, MTA members have already readjusted their yearly sales targets but the situation is still grave. The attached annexes show comparisons of sales forecasts annualized for the 2003

calendar year, from distributors representing the lower, middle and upper end segments of the market.

Estimates of Additional Revenue

The Government has used previous yearly sales figures to calculate its projected revenue gain of HK\$700 million under the new FRT. But that figure is based on a 15% drop in first registrations for 2003-4. Today we face a new economic reality. Relying on the Government's old revenue projection targets is now wholly inappropriate.

As members of this Committee can see from the charts presented earlier, the real drop in first registration could be more along the lines of 30% instead of 15%. With MTA's proposed rates, our research predicts that the drop would be around 18% instead of 30%. The additional revenue gain for Government would be HK\$308 million.

MTA has no intention of ducking its responsibility and not contributing its fair share of taxes, but MTA believes that a more equitable structure can be put in place which at the same time protects real Government tax revenues.

Workforce Impact

The unemployment issue is naturally of great concern to this Committee and the MTA. According to a recent survey of MTA members, some startling statistics have surfaced:

- 92% of respondents plan to lay off workers. Only one MTA member has no plans to institute a redundancy programme.
- 38% of MTA members have already laid off staff this year.
- On average, respondents will lay off 20% of their staff.
- 61% of MTA members will put forward salary cuts / unpaid leave schemes or they have already done so this year.

The motor trade in Hong Kong employs about 12,000 staff and there is an immediate danger of 2,400 redundancies due to the grave loss of revenue. It is important to recognise that each sector of the market represents not simply one dealer, but an entire workforce that is dedicated to the maintenance and service of all vehicles sold. Attempts to target certain levels of the car market end up affecting the livelihoods of employees in associated parts of the trade.

Conclusion – Working in Partnership

May I reiterate that the MTA, as an organisation that represents 90% of Hong Kong's trade in new motor vehicles, is supportive of the new tax structure and recognizes that all parts of the Hong Kong community must share in the burden of increased taxes. However, the new proposed rates are far beyond the market tolerance level and will powerfully deter new car buying. That in turn will result in a diminished market and would, ironically, depress expected tax revenues for the Government. Our aim is to support a system that is beneficial to the Government in the form of increased tax revenues, but it has to be one that is not overwhelmingly destructive in its effect on the industry and consumers. We hope that the Committee will seriously consider and adopt our proposal.

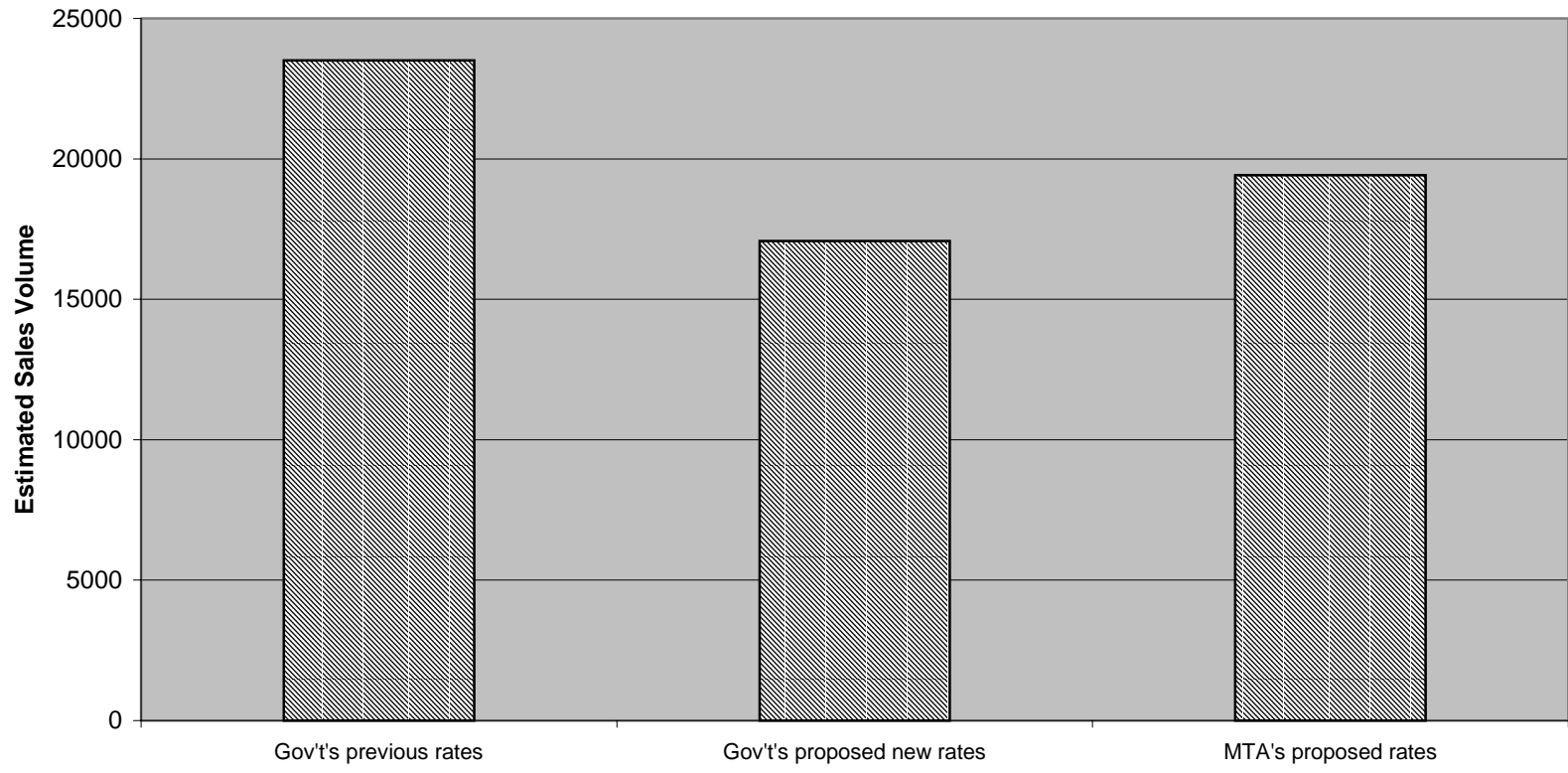
The Motor Traders Association of Hong Kong

Annex A

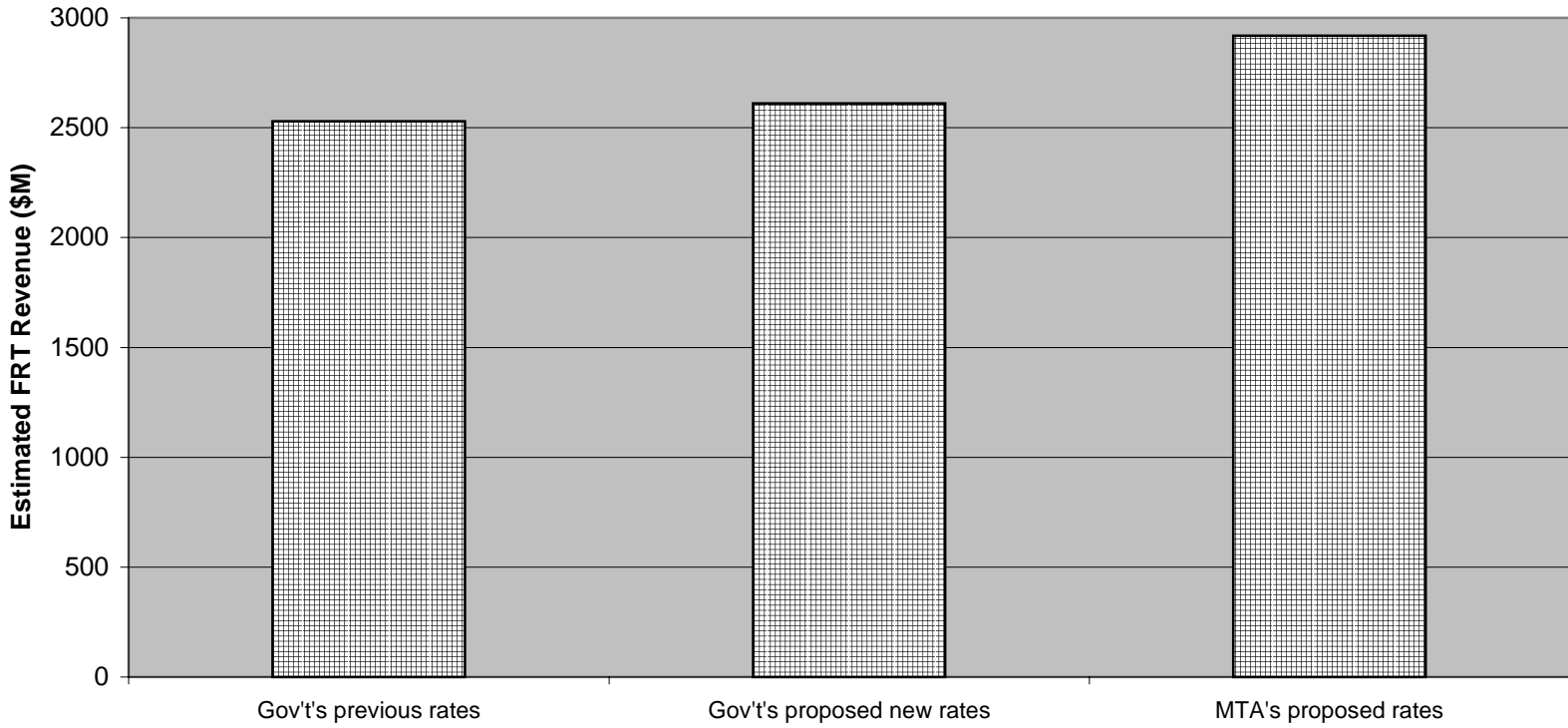
Forecast Impact on Sales and FRT Revenue Under Different FRT Scenarios
For all Vehicles (2003)

	Previous FRT rates	Gov't's proposed new rates	MTA's proposed FRT rates
Estimated sales volume (% change from Gov't's previous FRT rates)	23500	17076 (-27.3%)	19416 (-17.4%)
Estimated FRT generated(\$M) (% change from Gov't's previous FRT rates)	2530	2611 (+ 3%)	2919 (+15%)

**Forecast Impact on Sales volume Under Different FRT Scenarios for All Vehicles
(2003)**



**Forecast Impact on FRT Revenue Under Different FRT Scenarios for All Vehicles
(2003)**

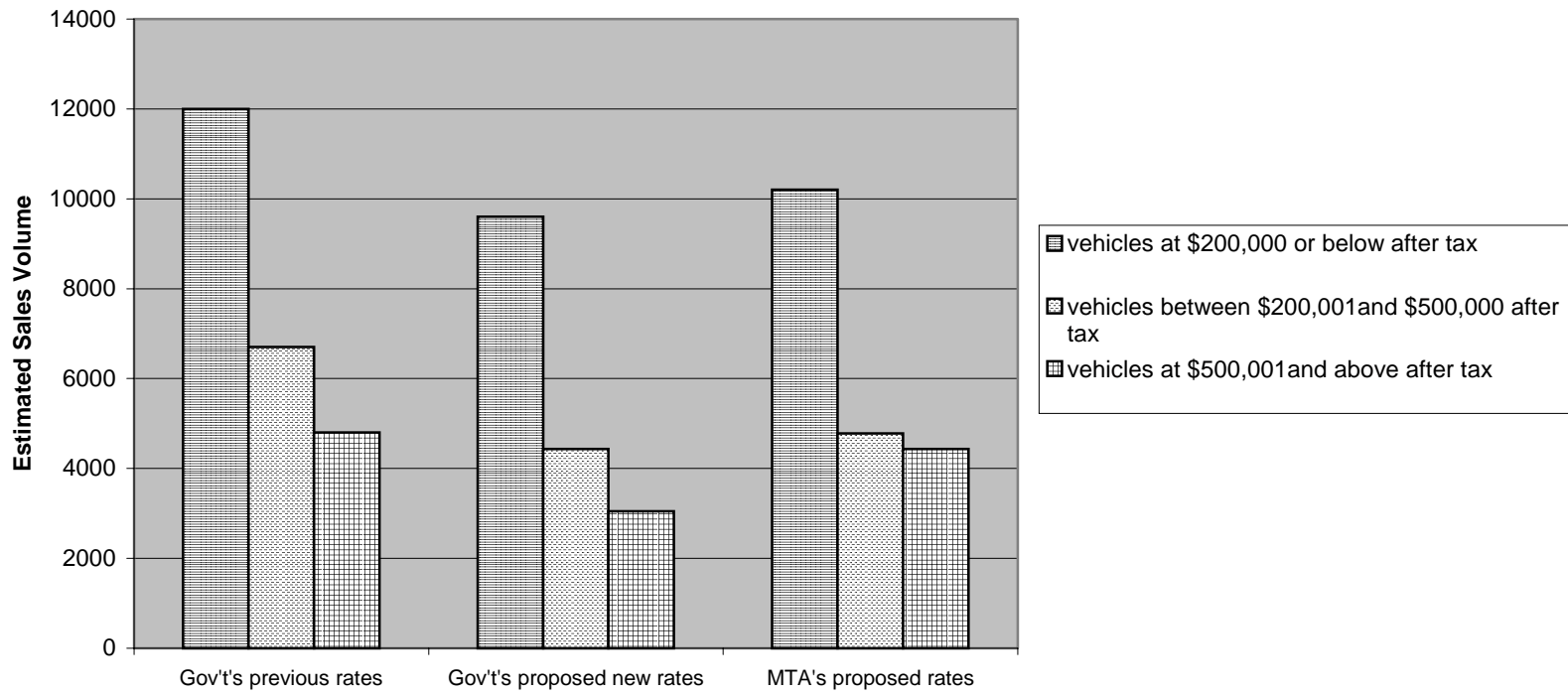


Annex B

**Forecast Impact on Sales and FRT Revenue under Different FRT Scenarios
For Various Market Segments (2003)**

After tax value	Previous FRT rates		Gov't's new FRT rates		MTA's proposed rates	
	Units	Revenue (\$M)	Units (% change from Previous FRT)	Revenue (\$M) (% change from Previous FRT)	Units (% change from Previous FRT)	Revenue (\$M) (% change from Previous FRT)
\$200,000 and below	12000	334	9600 (- 20%)	399 (+19.5%)	10200 (-15%)	424 (+27%)
\$200,001- \$500,000	6700	431	4430 (- 34%)	515 (+19.5%)	4780 (-29%)	498 (+16%)
\$500,001 and above	4800	1765	3046 (-37%)	1697 (- 4%)	4436 (-8%)	1997(+13%)
Total	23500	2530	17076	2611	19416	2919

2003 Sales Volume Forecast for Different Market Segments Under Different FRT Scenarios



2003 FRT Revenue Forecast for Different Market Segments Under Different FRT Scenarios

