

**Bills Committee on Revenue (No. 2) Bill 2003**

The Administration's response to the issues raised by Members during the meeting of the Bills Committee on 27 May 2003 is set out below:-

**Impact of the outbreak of the Severe Acute Respiratory Syndrome (SARS) (including the proposed relief measures) on revenue estimates**

2. The outbreak of SARS has had adverse impacts on the economy. As released on 30 May 2003, Government's forecast growth of GDP for 2003 is now put at 1.5% in real terms and -2% in nominal terms as compared with 3% in real terms and 1% in nominal terms forecast in the 2003 Budget Speech. The downward revision in the economic forecast has taken into account the impact of the outbreak of SARS and the relief and support measures announced by Government on 23 April 2003.

3. Given the downward revision of the economic growth for 2003 and the financial implications of the SARS relief and support package, we expect that the Government revenue outturn for 2003-04 will be less than the original estimates of \$193.5 billion, which include \$6.1 billion to be generated by the revenue raising measures proposed in the Budget Speech.

4. It is expected that an associated drop in profits and income levels in 2003/04 will lead to more applications for holding over of the 2003/04 provisional tax charged and a higher arrears rate by the year end than originally estimated. In addition, we also expect drops in collections from betting duty, stamp duty and hotel accommodation tax in view of the falling attendances at horse racing meetings, the sluggish property market and low hotel occupancy rates. However, it is too early at this stage to make a meaningful forecast of the outturn revenue for 2003-04. The position will be closely monitored, and the actual position reported on a monthly basis in line with the International Monetary Fund's Special Data Dissemination Standards.

**Information on deeming assessable profits related to royalty payment received by film distributors of foreign films and the tax paid by them in the past two years**

5. Clause 5 of the Bill proposes to increase the rate of deeming the assessable profits related to royalty payments to non-residents for the purpose of ascertaining the

rate of withholding tax. This is not confined to income from exhibition of foreign films in Hong Kong, but applies also to cases where other types of intellectual property, such as design, trade marks, patents etc. are used in Hong Kong and fees for usage are paid.

6. Statistics on the amount of royalties paid by Hong Kong businesses to non-residents and the corresponding withholding tax receipts from such payments, as well as the estimated figures in respect of royalties for foreign films are set out in the table at *Appendix A*. As regards breakdown of information in relation to Hong Kong subsidiaries of foreign film producers and local independent film distributors, IRD does not have the exact figures. Only estimates are available. IRD also does not have information broken down by the origin of foreign films and thus could not provide information related in particular to US films.

7. As illustrated in the table, royalties from foreign films constituted only around 3% (2.8% for 2000/01 and 2.6% for 2001/02) of all royalty payments made to non-residents. The proportion of withholding tax from the film industry to the total withholding tax was only about 1% (0.89% for 2000/01 and 0.83% for 2001/02).

8. It is estimated that out of the royalties on foreign films, the royalties paid by local independent distributors amounts to roughly \$70 million per annum (\$75 million for 2000/01 and \$65 million for 2001/02). This represented about 2% of the total royalties (1.88% for 2000/01 and 1.82% for 2001/02). The withholding tax they paid was roughly \$1 million per annum (\$1.2 million for 2000/01 and \$1 million for 2001/02). This was about 0.6% of the total amount of withholding tax (0.59% for 2000/01 and 0.55% for 2001/02).

9. Concern was expressed at the last meeting that the increase in deeming profits rate would result in a corresponding rise in royalty payments which would ultimately be borne by Hong Kong distributors. As we have made clear at the time, the tax is on the receiver of royalty payments and collected in the form of a 'withholding tax'. Whether the new deeming rate will be factored into the bidding price made by Hong Kong distributors for foreign films is a matter of commercial decision and is determined by the market.

**Drafting consistency of clauses 2, 9(b) and 12(b) as referred to by SALA in his letter dated 12 May 2003**

10. As explained in our reply to SALA on 22 May 2003, clause 2 of the Bill as currently drafted will not adversely affect the operation of the amendment ordinance nor the Inland Revenue Ordinance. As for clauses 9(b) and 12(b), the present draft does not, and indeed cannot, prohibit the legislature from making amendments to the rates, etc in the future. Nevertheless, in view of Members' concern, we will move Committee Stage Amendments (CSAs) to further clarify the situation. The revised CSAs are at *Appendix B*.

**To consider rephrasing “as appropriate” to “as the case may be” for clause 15(6) as suggested by Ms Audrey EU**

11. We agree that clause 15(6) could be further clarified and will propose CSAs in this respect. The revised CSAs are at *Appendix B*.

Financial Services and the Treasury Bureau  
June 2003

**Analysis of Tax Payments on Royalties**

	<u>2000/01</u>	<u>2001/02</u>
	\$	\$
(a) Total royalties	3,989 m.	3,575 m.
(b) Royalties on foreign films [see Note 1]	112.5 m.	93.8 m.
(c) % of film royalties to total royalties [(b)/(a)]	2.8%	2.6%
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(d) Tax on total royalties	202 m.	181 m.
(e) Tax on royalties on foreign films [(b) x 10% x 16%]	1.8 m.	1.5 m.
(f) % of film royalty tax to total royalty tax [(e)/(d)]	0.89%	0.83%
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(g) Royalties on films paid by local independent film distributors [see Note 2]	75 m.	65 m.
(h) % of (g) to total royalties [(g)/(a)]	1.88%	1.82%
(i) Tax paid by local independent film distributors [i.e. (g) x 10% x 16%]	1.2 m.	1 m.
(j) % of (i) to tax on total royalties [(i)/(d)]	0.59%	0.55%

Note: (1) No separate figures for US films and non-US films.

(2) The rest of the film royalties (i.e. \$37.5 million for 2000/01 and \$28.8 million for 2001/02) are paid by Hong Kong subsidiaries or agent of foreign film producers, Hong Kong television companies, etc. No separate data for these entities are available.

(Draft as at 3 June 2003)

REVENUE (NO. 2) BILL 2003

**COMMITTEE STAGE**

Amendments to be moved by the Secretary for Financial Services  
and the Treasury

<u>Clause</u>	<u>Amendment Proposed</u>
2	By deleting “This Ordinance applies” and substituting “Sections 3 to 6 and 9 to 15 apply”.
3	By deleting the clause and substituting – <b>“3. Definition of income from employment</b> Section 9 of the Inland Revenue Ordinance (Cap. 112) is amended – (a) by repealing subsection (1)(a)(i), (ii) and (iii); (b) in subsection (2A) – (i) by repealing paragraph (a) and substituting – “(a) any benefit that is – (i) provided by an employer otherwise than in connection with a holiday journey; and

- (ii) capable of being converted into money by the recipient;”;
- (ii) in paragraph (b), by repealing the comma at the end and substituting “; or”;
- (iii) by adding –
  - “(c) any amount paid by an employer in connection with a holiday journey,”;
- (c) in subsection (6), by adding –
  - ““holiday journey” (度假旅程) means –
    - (a) a journey taken for holiday purposes; or
    - (b) where a journey is taken for holiday and other purposes, the part of the journey taken for holiday purposes;”.”.

9(b) By deleting “until superseded” and substituting “for each year after that year”.

12(b) By deleting “until superseded” and substituting “for each year after that year”.

15(6) By deleting “, as appropriate”.