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**Report of the Subcommittee on
Public Revenue Protection (Revenue) Order 2003 made under
section 2 of the Public Revenue Protection Ordinance (Cap. 120)**

Purpose

This paper reports on the deliberations of the Subcommittee on Public Revenue Protection (Revenue) Order 2003 made under section 2 of the Public Revenue Protection Ordinance (Cap. 120).

Background

2. Under section 2 of the Public Revenue Protection Ordinance (PRPO) (Cap. 120), if the Chief Executive (the CE) approves of the introduction into the Legislative Council (the Council) of a bill whereby, if the bill were to become law, any duty, tax, etc. would be imposed, removed or altered, the CE may make an order giving full force and effect of law to all the provisions of the bill. Section 5 of PRPO provides that an order so made shall come into force immediately upon signing by the CE, and shall expire and cease to be in force under the following specific circumstances:

- (a) upon the notification in the Gazette of the rejection by the Council of the bill in respect of which the order was made;
- (b) upon notification in the Gazette of the withdrawal of the bill;
- (c) upon the bill, with or without modification, becoming law in the ordinary manner; or
- (d) upon the expiration of four months from the day on which the order came into force.

After the expiry of the order made under PRPO, depending on the outcome of the bill, refunding and recovery of taxes collected in excess or underpaid when the order is in force will be arranged in accordance with sections 6 and 7 of PRPO respectively.

3. The order is a subsidiary legislation, subject to negative vetting under section 34 of the Interpretation and General Clauses Ordinance (Cap. 1). Section 34(2) of Cap. 1 provides that Members may amend subsidiary legislation in any manner whatsoever consistent with the power to make such subsidiary legislation. The power of the CE in Council under section 2 of PRPO is to make an order giving full force and effect of law to all the provisions of the bill contained in the order. Consistent with this power, the Council has the power to repeal the order but does not have power to amend the provisions therein.

4. In his Budget Speech for 2003-04, the Financial Secretary (FS) proposed to amend the first registration tax (FRT) system. Currently, FRT for motor vehicles is charged on the Published Retail Price (PRP) of vehicles and their accessories. Certain accessories, namely air-conditioners, audio equipment and anti-theft devices, as well as distributors' warranties are exempted from FRT and their values excluded from the calculation of taxable value. The FS proposed to abolish these exemptions and strengthen the anti-avoidance provisions, introduce a marginal tax system for certain motor vehicles, and make adjustment to tax rates for different classes of motor vehicles.

The Public Revenue Protection (Revenue) Order 2003

5. The Public Revenue Protection (Revenue) Order 2003 (the Order), made in accordance with PRPO, gazetted on 5 March 2003, was tabled at the Council on 12 March 2003. For revenue protection purpose, the Order gives temporary effect to the budget proposals relating to FRT starting from 2:30 pm on 5 March 2003 of the Budget Day. The Schedule to the Order contains provisions of the Revenue Bill 2003 which was introduced into the Council on 9 April 2003.

The Subcommittee

6. Members agreed at the House Committee meeting on 21 March 2003 to form a subcommittee to study the Order. Under the chairmanship of Hon Audrey EU, the Subcommittee has held three meetings including one with deputations to hear their views on FRT proposals and the Order. The membership list of the Subcommittee is in **Appendix I**. The list of organizations which have made written and/or oral representation to the Subcommittee is in **Appendix II**.

7. To allow sufficient time for the Subcommittee to study the Order, Members passed a motion at the Council meeting on 9 April 2003 to extend the scrutiny period to 30 April 2003.

Deliberation of the Subcommittee

8. The Subcommittee is aware that the purpose of the Order is for revenue protection. It has been the established practice to use Public Revenue Protection Orders (PRP Orders) to give temporary effect to those revenue-raising proposals which, if not implemented immediately upon announcement, will result in revenue loss through measures such as stockpiling and advance sale. Over the past years, the increases in the duty rates on cigarettes and alcoholic beverages, and increases in traffic-related licence fees have also come into immediate effect through the issue of PRP Orders. The Subcommittee notes the Administration's view that if FRT proposals are not effected immediately through the Order, but deferred until the Bill has been enacted, many vehicles buyers will advance their purchase in anticipation of the tax increases and avoid the taxes. The revenue loss will be tremendous.

9. The Subcommittee notes that while the motor trade associations are generally supportive to the proposal of removing tax exemptions for vehicle accessories and distributors' warranties, they are strongly opposed to the proposed increase in FRT rates. According to the trade associations, the high FRT rates will deter new purchases of motor vehicles which include cars and motorcycles, and would adversely affect the business of the motor trade and job opportunities in the trade and related sectors. The Subcommittee is aware that detailed examination of the specific FRT proposals should more appropriately be undertaken in the context of the scrutiny for the Revenue Bill 2003. However, as the Council has the discretion to repeal the Order, the Subcommittee considers it appropriate to look into the concerns of FRT proposals before recommending to the House Committee whether the Order should be repealed.

Impact of FRT proposals on the motor trade and related sectors

10. In view of the adverse impact of FRT proposals on the sales of motor vehicles, the trade associations urge for a reduction in the tax rates for private cars to mitigate the impact of the exemption abolition. In respect of the tax rate for motorcycles, the Subcommittee notes that the trade associations have also raised objection. According to some trade associations, after the Order took effect on 5 March 2003, due to the enormous increase in taxable value and FRT for vehicles, the sales on private cars and motorcycles have dropped seriously. The number of private cars registered was only 59 one week after the Budget Day as compared to 1,636 one week before the Budget Day. The number of registration for motorcycle also declined from 105 to 61 during the period. According to some trade associations, about 30% of orders for new private cars have been cancelled after the announcement of the tax increases and the cancelled stocks have an estimated value amount to \$400 million. Coupled with the current adversities in the economy, trade associations have expressed grave concern about the increasingly difficult business environment

for the motor trade. While some dealers have lowered the prices for vehicles to absorb part of the increase in taxes, as buyers could request for refund of their deposits, the motor trade, especially small and medium sized firms, are facing serious cash flow problem and many of them will eventually be forced to wind up. Some trade associations have therefore urged for a repeal of the Order to help the trade pass through the difficult period.

11 A summary of the views of the trade associations put forward to the Subcommittee is given at **Appendix III**.

12. Regarding the concerns of the trade over the rise in FRT for vehicles, the Administration explains that notwithstanding FRT proposals may lead to an increase in retail price ranging from 5% to 27% for representative vehicle models, the increase is mainly due to the abolition of the tax exemptions rather than increase in tax rates. The Administration has widened the bandwidths, introduced a marginal tax system and lowered the tax rates to mitigate the impact of the abolition of exemptions on lower-priced private cars. For commercial vehicles such as buses, light buses, and taxis etc, the tax rates are also lowered. Moreover, if distributors choose not to pass the full tax burden to consumers and change their pricing strategies, the increase in retail price will be smaller. Notwithstanding that the impact of tax increase will be higher for more expensive private cars, as these only represent a small portion of the private car market in Hong Kong (e.g. in 2002-03 only about 6% of the private cars first registered had a taxable value over \$500,000), the overall effect on the motor trade will not be significant. As regards the impact of FRT proposals on the motor trade, the Administration expects that the slow-down in car sales is only a temporary phenomenon. Indeed, the number of registration has started to pick up and is gradually rising back to its usual level. During the week from 24 March to 30 March, the number of first registration for private car and motorcycle has risen to 328 and 91 respectively. These represent 57% and 99% of the respective weekly averages for private car and motorcycle first registrations in 2002-03.

Consequences of repealing or not repealing the Order

13. As the Council is not empowered to amend the Order, the Subcommittee has discussed at length the consequences of repealing or not repealing the Order, in particular whether a repeal of the Order will help relieve the hardship facing the motor trade in the interim period before the Council completes scrutiny of the Bill.

14. The Subcommittee notes that by repealing the Order, FRT will be charged at the old rates as before the commencement of the Order. There is however no immediate refund in respect of the excess taxes collected when the Order was in force. As provided in section 34(2) of Cap. 1, the resolution to repeal the Order will not prejudice anything done under the Order. Section 5

of PRPO does not provide for the repeal of the Order and hence, the refunding arrangement provided under section 6 of PRPO will not apply when the Order is repealed. Members further notice that if the Order is repealed, in the event that Revenue Bill 2003 is subsequently passed without amendment, the Administration will have to arrange for recovery of the underpaid tax during the period after the repeal of the Order and before the passage of the Bill. If the Bill is not passed by the Council, there will be refund of the excess tax collected during the period when the Order was effective (up to its repeal). Under the scenario that the Bill is passed with lower FRT rates than proposed, registered car owners have to repay the tax underpaid during the period after the Order was repealed and before the passage of the Bill. As there are uncertainties on the outcome of the Bill, the Subcommittee agrees that repealing the Order will cause confusion to the trade and vehicle buyers and pose operational problems. Moreover, for those items with lower tax rates effected by the Order, repealing the Order will revert the rates to the original higher level thus depriving the trade of benefiting from the lower tax rates.

15. The Subcommittee also notes the view of the Motor Traders Association of Hong Kong (the major association representing car distributors) that in the absence of the Order, the gap between 5 March 2003 and the passage of the Bill will lead to chaos and disruption in the vehicle market. The Association is concerned that unscrupulous dealers may abuse the "grace period" to license unsold cars under company names and enjoy the low tax rate. These pile-up stocks will be slowly supplied to the market thus defeating the objective of the budget proposals.

16. On the other hand, the Subcommittee notes that if the Order remains in force, any excess tax collected under the Order will be refunded in the event that the Bill is subsequently passed with tax rates lower than proposed or not passed at all. The subcommittee considers that the refunding mechanism under PRPO is fair and the interest of car owners will not be jeopardized. The Administration stresses that the Order is a temporary measure to protect revenue. It is opposed to any attempt to repeal the Order which will be in conflict with public interest.

Exemption for orders placed before the Order took place

17. With a view to helping the motor trade to adapt to the new tax system and to be fair to car buyers who have placed orders before announcement of FRT proposals, some members support the trade associations' suggestion of granting exemption to distributors' stocks and cars for which orders have been placed and deposits paid before the Order took effect. The Administration stresses that FRT is a tax on the registration of vehicles for use in Hong Kong. It has been the practice for FRT adjustments in the past that the new rates were applied to all vehicles which had not been registered at the time when the changes took effect. This was also the practice for other tax measures, such as

duties on alcohol and tobacco. In respect of the proposal to grant exemption for cars ordered, the Administration explains that it will be difficult to verify the timing of orders placed by vehicle buyers. The proposed exemption may lead to abuse by people submitting back-dated orders to achieve tax savings. Moreover, documentary proof may not be available in all cases for verification purpose. As regards the suggestion to exempt cars imported before the Budget Day, the Administration considers it unjustified to exempt cars in the distributors' stocks, which may not be subsequently sold and registered in Hong Kong. According to the Administration's records, many of the cars imported into Hong Kong are never registered for use in Hong Kong but are eventually re-exported.

18. While taking note of the Administration's view, some members consider that the Administration should appreciate the genuine difficulties facing the trade and vehicle buyers. They agree that the Bills Committee formed to study the Bill should further examine the above exemption proposals in order to help the motor trade and vehicle buyers.

Recommendation and advice sought

19. Having considered the consequences of repealing the Order and the confusion it may result, the Subcommittee considers it inappropriate to repeal the Order. The Subcommittee understands the concerns and views of the motor trade. Members share the view that excessively high tax rates will have a strong negative impact on the motor trade and adversely affect job opportunities in the trade and related sectors. The Subcommittee recommends that a Bills Committee should be formed to scrutinize the Revenue Bill 2003. The Bills Committee should commence work as soon as possible so as to enable the early passage of the Bill.

20. Members are invited to note the deliberations of the Subcommittee and its recommendation in paragraph 19 above.

**Subcommittee on
Public Revenue Protection (Revenue) Order 2003 made under
section 2 of the Public Revenue Protection Ordinance (Cap. 120)**

Membership list

Chairman Hon Audrey EU Yuet-mee, SC, JP

Members Dr Hon David CHU Yu-lin, JP
Hon Cyd HO Sau-lan
Hon Mrs Selina CHOW LIANG Shuk-ye, GBS, JP
Hon CHAN Kam-lam, JP
Hon SIN Chung-kai
Hon Miriam LAU Kin-ye, JP
Hon Emily LAU Wai-hing, JP
Hon Abraham SHEK Lai-him, JP
Hon Michael MAK Kwok-fung

(Total : 10 members)

Clerk Ms Connie SZETO

Legal Adviser Mr Stephen LAM

Date 25 March 2003

**Subcommittee on
Public Revenue Protection (Revenue) Order 2003 made under
section 2 of the Public Revenue Protection Ordinance (Cap. 120)**

**List of individual/organizations which have made
written and/or oral representation to the Subcommittee**

1. Mr DIK Kong-sang
2. Hong Kong Motorcycle Association
3. Hong Kong Motorcycle of Commerce
4. Hong Kong Right Hand Drive Motors Association Ltd.
5. Hong Kong Small and Medium Enterprises Association
6. Hong Kong Vehicle Repair Merchants Association
7. Marketing Association of Chinese Mainland & Hong Kong SAR
8. Motor Alliance (also titled as “反對增加汽車登記稅大聯盟”)
9. The Motor Traders Association of Hong Kong
10. 電單車大聯盟

Council Business Division 1
Legislative Council Secretariat
23 April 2003

**Subcommittee on
Public Revenue Protection (Revenue) Order 2003 made under
section 2 of the Public Revenue Protection Ordinance (Cap. 120)**

Concerns and views of the motor trade on the motor vehicle first registration tax (FRT) proposals

| Association | FRT proposals | | | | Other views |
|--|---------------------------|---------------------|---|-------------------------|---|
| | Abolishing tax exemptions | Marginal tax system | Proposed tax rates | Anti-avoidance measures | |
| The Motor Traders Association of Hong Kong | support | support | Proposed tax rates for private cars are too high and should be reduced to 35%, 60%, 85% and 105% for the four new marginal tax bands. | support | High FRT rates will suppress vehicle sales and will be counter-productive to the objective of raising additional revenue. |

| Association | FRT proposals | | | | Other views |
|--|---------------------------|----------------------|---|---|---|
| | Abolishing tax exemptions | Marginal tax system | Proposed tax rates | Anti-avoidance measures | |
| Hong Kong Right Hand Drive Motors Association Ltd. | support in principle | support in principle | Strongly oppose to the proposed FRT rates and counter-propose to reduce the rates to 35%, 55%, 75% and 75% for the existing four tax bands. | <p>The requirement for registered owners of vehicles, registered distributors and associated persons to declare fitting of accessories and distributors' warranties is too complicated.</p> <p>Against extending the requirement for payment of additional FRT for accessories and distributors' warranties from three months after registration to six months.</p> | <p>High FRT rates will suppress vehicle sales and will be counter-productive to the objective of raising additional revenue.</p> <p>Vehicles imported or order placed before the Budget Day should be taxed at the old rates.</p> |
| Motor Alliance | ditto | ditto | ditto | ditto | ditto |

| Association | FRT proposals | | | Other views | |
|---|---------------------------|---------------------|---|-------------|---|
| | Abolishing tax exemptions | Marginal tax system | Proposed tax rates | | Anti-avoidance measures |
| Hong Kong Motorcycle Association Hong Kong of Commerce 電單車大聯盟 | support in principle | -- | Object to the higher tax rate of 40% for motorcycles and demand for reduction to 32%. | -- | High FRT rates will suppress vehicle sales and will be counter-productive to the objective of raising additional revenue. Vehicles imported or order placed before the Budget Day should be taxed at the old tax system. |