



3 May 2005

By fax (2147 3873) and by post

Our Ref.: C/TXM, M34533

Mr. Frederick Ma Si-hang
Secretary for Financial Services and the Treasury
Financial Services and the Treasury Bureau
8/F, West Wing
Central Government Offices
Ice House Street
Hong Kong

Dear

Review of the Inland Revenue Ordinance (Cap. 112)

--- Please find attached a letter to the Hon. Mandy Tam, which the Institute has sent out today to confirm its position on Ms. Tam's calls for a comprehensive review of the Inland Revenue Ordinance (Cap.112) ("IRO").

As you will note from the letter, we do not support the proposal for a root and branch examination of the ordinance. However, at the same time, we believe that there are various specific, significant issues relating to the IRO, tax policy and the administration of the tax system, that need to be addressed. We refer to some of these in the letter. A number of such issues have previously been raised in budget submissions to the Financial Secretary ("FS"), most recently in the 2005/06 Budget Proposals document (*In FOCUS – The Core Strengths of Hong Kong's Tax System*) issued to the FS in December 2004, as well as in our annual meetings with the Commissioner and senior staff of the Inland Revenue Department. It is the Institute's intention to emphasise to the FS the importance of addressing these various concerns as matters of priority.

Yours sincerely,

Edward K.F. Chow
President

EC/PMT/ay
Encl.



3 May 2005

By fax (2537 1425) and by post

Our Ref.: C/TXM, M34532

The Hon. Mandy Tam
Legislative Council
Room 425, West Wing
Central Government Offices
11 Ice House Street
Central
Hong Kong

Dear *Mandy*,

Review of the Inland Revenue Ordinance (Cap.112)

I am writing as a follow up to the discussion at the meeting of the Council of the Hong Kong Institute of Certified Public Accountants held on 15 March 2005, which you attended, and the meeting between yourself and representatives of the Institute's Taxation Committee on 1 March 2005. At these meetings, your views on the Inland Revenue Ordinance ("IRO") and your proposal to conduct a complete review of the legislation were discussed. I should like to clarify the Institute's position in this regard.

We agree that there are technical issues relating to the IRO, its interpretation and application that are of concern to practitioners, professional accountants in business and to the business sector. There are also questions of tax policy that need to be addressed and areas where the practices of the Inland Revenue Department ("IRD") would benefit from further clarification. The Institute has provided a number of examples of such matters in its annual budget proposals submission to the Financial Secretary and in the annual meeting with the Commissioner of Inland Revenue ("CIR"). Issues of concern and/or areas where improvements could be made, either through legislation or otherwise, would include:

- Offshore profits claims, particularly in the case of manufacturing and trading profits.
- Non-Hong Kong employment claims.
- The measurement of profits and timing of income following the decision in *CIR v. Secan*.
- Re-opening of prior year assessments and the application of the Assess First Audit Later procedure.



- Application of the penalty policy under section 82A and the implementation of the anti-avoidance provisions under section 61A of the IRO.
- Publication of the assessor's manual.
- Introduction of group loss relief and loss-carry back provisions.

However, we do not consider that addressing the above issues, which are quite specific, would necessitate a comprehensive review of the IRO. We believe that, in practice, embarking upon a comprehensive review, which would imply a root and branch examination, extending to, for example, the source-based principle and schedular basis of taxation, could distract attention from the need to deal with these very important and urgent ad hoc matters. Furthermore, it appears to the Institute that a number of the concerns that you have raised, which may be valid concerns, relate to matters of interpretation and application of the law, and the way in which the system is administered, rather than pointing clearly to need for a thorough-going review of the law itself and its underlying principles.

As you may be aware, in the past the Institute itself has suggested that a review of the IRO may be desirable, in particular in its 2000/2001 budget proposals. However, we no longer consider this to be a priority given that certain of the main issues that, at that time, led us to form this view, are now being, or have been, addressed, including the need for a broader base of taxation and for reform or abolition of the estate duty regime.

In conclusion, therefore, although the Institute is not prepared to support calls for comprehensive review of the IRO, for the reasons given above, we should be happy to assist you in putting forward proposals to address specific problems, such as those listed above. We should also be willing to attend a meeting of the Legislative Council to elaborate on our position if this would be helpful and we were invited to do so.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Winnie Cheung', written in a cursive style.

Winnie C.W. Cheung
Chief Executive & Registrar

WCC/PMT/ay