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Report of the Bills Committee on Stamp Duty (Amendment) Bill 2010

Purpose

This paper reports on the deliberations of the Bills Committee on Stamp Duty (Amendment) Bill 2010 (the Bills Committee).

Background

2. The increased global liquidity, very low interest rate environment and keen competition in the mortgage market have fuelled the surge in property prices recently. To reduce the potential risk of forming a property bubble, the Financial Secretary has announced in the 2010-2011 Budget speech a number of measures to stabilize the property market. These include measures to curb speculative activities by increasing the transaction cost of property speculation.

The Bill

3. Considering that there is a higher risk of speculative activities for flats with a transacted value above $20 million, the Bill seeks to amend the Stamp Duty Ordinance (Cap. 117) (SDO) to increase the rate of stamp duty payable in relation to transactions of immovable property valued more than $20 million from 3.75% to 4.25%, and to disallow deferment of payment of stamp duty chargeable on an agreement for sale made in respect of residential property valued more than $20 million.

4. The content of the Bill was published in the Public Revenue Protection Order 2010 (L.N.18 of 2010). The Order is a temporary measure taken under the Public Revenue Protection Ordinance (Cap. 120) to give effect to the two proposals as set out in paragraph 29 of the 2010-2011 Budget Speech. The Order will lapse on 1 August 2010.

The Bills Committee

5. At the House Committee meeting held on 7 May 2010, Members agreed to form a Bills Committee to study the Bill. Under the chairmanship of Hon CHAN Kam-lam, the Bills Committee has held four meetings. The membership list of the Bills Committee is in **Appendix I**.

Deliberations of the Bills Committee

6. The Bills Committee generally supports the need to curb property speculation. However, some members have questioned the efficacy of the two measures in curbing speculative activities. In the course of deliberation, members have examined issues relating to considerations for targeting at residential transactions valued above \$20 million, possible extension of disallowance for deferment of payment of stamp duty, other possible measures to curb speculation on residential properties, and proposed amendments to the Bill.

Considerations for targeting at residential transactions valued above \$20 million

7. The Bills Committee has enquired the bases upon which the threshold of \$20 million, and the rate of increase of stamp duty from 3.75% to 4.25% are arrived at. The Administration has advised that when considering the types of transactions which should be subject to higher stamp duty rate, reference has been made to the Hong Kong Monetary Authority's guidelines to banks in October 2009 to reduce the loan-to-value ratio from 70% to 60% for residential properties valued at \$20 million or more. Besides, foreign investors are more interested in properties of high value. To ensure that Hong Kong's competitive edge as an international city, headquarters of multi-national corporations in Asia, and a major global financial centre would not be undermined as a result of high stamp duty rate, reference has been made to the tax regime of neighbouring economies in considering the rate of increase of stamp duty. For property transactions of similar value, the tax rates in Singapore and Australia are 2.7% and 4.47% respectively. The Administration has considered it appropriate to increase the stamp duty rate on property transactions valued over \$20 million to 4.25% at this stage.

Extension of disallowance for deferment of payment of stamp duty

8. Some members have enquired whether consideration could be given to extending the disallowance for deferment of payment of stamp duty chargeable on an agreement for sale made in respect of residential property to properties valued more than \$10 million to further curb speculation. Other members however do not support the proposed extension as this may have impact on genuine middle-class home buyers. According to the Administration, it will not rule out the possibility of extending the two tax measures in the Bill to properties in the lower end in the event of rampant speculative activities in transactions valued below \$20 million. It will continue to closely monitor market development, and will consider reinstating appropriate measures, including prohibiting sub-sale through confirmor, imposing restrictions on

the target groups for sale of uncompleted residential flats, and requiring developers to put up for sale all flats within a specified period through the Lands Department's Consent Scheme, to ensure a healthy and stable development of the property market.

Measures to curb speculation on residential properties

9. Noting that the number of property transactions valued more than $20 million only comprised 1.9% of the total number of property transactions in 2009, and that over 90% of these transactions did not involve resale within two years of purchase, some members have questioned the efficacy of increasing the stamp duty of these transactions in curbing property speculation. To strike a balance between protecting the interest of genuine home buyers and curbing speculation, consideration should be given to raising the stamp duty and refunding the increased portion for properties which does not have transactions within a specified period say two years. The Administration has advised that if the proposal is adopted, over 90% of the property buyers will have to pay additional amount of stamp duty first, with a view to seeking refund two years later. This will not only cause inconvenience to the majority of home buyers, but also have additional resource implications on the Inland Revenue Department (IRD).

10. Some members have opined that target specific measures, such as introducing profits tax and capital gains tax for property transactions, prohibiting sub-sale through confirmor etc, would be more effective in curbing property speculation than increasing stamp duty. The Administration has advised that under SDO, no instrument chargeable with stamp duty shall be acted upon, filed or registered unless it is duly stamped. Under normal circumstances, stamp duty on instruments of transfer of property ownership will be secured as purchasers' solicitors will pass the duly stamped instruments to the Land Registry for registration to safeguard the interest of their clients. Stamp duty is one of the transaction costs of a property transaction. Increasing the rate of stamp duty and disallowing deferred stamp duty payment for transactions valued above $20 million will indeed increase the transaction cost of those transactions, reduce the cash flow of speculators, and make speculators act more prudently. Besides, the two measures in the Bill to increase the rate of stamp duty for transactions of properties valued more than $20 million, and to disallow deferment of payment of stamp duty in respect of such properties are only part of a package of measures to curb speculative activities. Other related measures include increasing the supply of land for private residential developments to address the fundamental issue, enhancing transparency in property transactions, and preventing excessive expansion in mortgage lending. Also, further measures will be considered as and when necessary.

Profits tax on property speculation

11. The Bills Committee has queried whether profits from property speculation are subject to profits tax. The Administration has advised that under the Inland Revenue Ordinance (Cap. 112) (IRO), all profits (except those from sale of capital assets) obtained by a person carrying on a trade, profession or business in Hong Kong will be subject to profits tax if such profits arise in or are derived from

Hong Kong. Property speculators are generally regarded as carrying on a business and have to pay profits tax under IRO. IRD has in place clear procedures for identifying and processing suspected property speculation cases. For a property transaction, IRD will take into account precedent court cases and consider all the relevant facts of the case, including the number of transactions, duration of the property held as well as the background, motive, financial arrangements and mode of operation, in determining whether the transaction should be treated as a business, and whether the vendor has to pay tax for the profits earned. Besides, some property speculators have opened tax files and report profits in their tax returns. For those with no tax files yet, IRD has established procedures to screen and identify, with the assistance of computer programme, cases suspected of involving property speculation for further examination. Enquiry letters will be issued to the parties concerned for details of transactions. IRD will scrutinize the information provided and consider other relevant information in determining whether speculation is involved. Cases which are regarded as involving property speculation, as well as unanswered cases, will be passed to IRD's Assessing Sections for profits tax assessment. Taxpayers who disagree to the assessment may raise objections with IRD. In 2007-08, excluding cases with existing tax files, IRD's computer programme identified 19 000 suspected cases of property speculations. 6 700 of them required follow-up actions after initial processing by IRD's officers. As at May 2010, 2 600 tax assessments were issued to 4 600 cases, of which 600 cases were confirmed to be taxable, 1 600 cases were considered to be not taxable, and the remaining 400 cases were still being processed.

Capital gains tax for property transactions

12. Some members have enquired whether consideration would be given to introducing capital gains tax for property transactions. According to the Administration, Hong Kong has all along maintained a simple tax regime with low tax rates. There is no capital gains tax in the prevailing tax system. Introducing capital gains tax for curbing property speculation will imply a fundamental change to the tax system of Hong Kong, and will require very careful consideration.

Sub-sale through confirmor

13. Given that there are confirmor cases in transactions of properties of all price ranges, some members have opined that prohibiting sub-sale through confirmor, or introducing an additional stamp duty on sellers of sub-sale through confirmor would be more effective in curbing speculation. Unlike the increase in stamp duty, these measures would unlikely affect genuine home buyers. The Administration is of the view that if a confirmor or a vendor selling a property is required to pay an additional amount of stamp duty, the issue of whether the additional stamp duty should be charged will depend on the types of vendor. The proposal will change the current assessment mechanism and related procedures on stamp duty. Substantial amendments to the Ordinance will also be required. The proposal is also unfair to those who have genuine need to sell their properties within the specified period, and will cause additional hardship to those in financial difficulties. In fact, not all property transactions generate profits. Those gaining profits from property

speculation are already subject to profits tax. The additional stamp duty will be considered as a kind of double taxation.

14. Other members have however pointed out that speculators could get round the increased stamp duty as proposed by the Administration using other possible means. For instance, a buyer can cancel a transaction with the developer and nominate another buyer to purchase the flat. The Administration has explained that developers will normally require the speculator to pay the stamp duty before executing the change in the names on the instruments of transfer of property ownership in order to protect their interest. Hence, the original buyer will have to pay the stamp duty under SDO when he/she cancels a transaction with the developer and nominates another buyer to purchase the flat. Besides, IRD will issue tax assessments to vendors of property transactions, regardless of the modes of transactions, which IRD considers to be in the nature of trade.

15. Noting that the statistics on confirmor cases only include individuals and not companies engaging in property speculation, some members have enquired about the prevalence of property speculation through transfer of shares of companies. The Administration has advised that limited companies in any trade or profession may engage in property transactions, but they are categorized according to their major businesses in tax assessment. It is therefore not possible for IRD to provide the total number of limited companies or individuals involved in property speculation. In 2007-08, IRD issued 25 000 tax assessments to limited companies which had existing tax files and were categorized as businesses engaging in property speculation, real estate development and property investment as declared. That said, profits from activities arising from property transactions should be recorded in the books of audited accounts of limited companies with existing profits tax files, regardless of how the companies are categorized for the purpose of tax assessment. IRD will, in accordance with the established rules and procedures, assess if such property transactions are in the nature of trade and should be subject to tax. In examining the tax returns of limited companies, IRD's assessors will ensure that profits tax derived from property speculation will be taken into account on tax assessment. For cases other than those which have existing profits tax files, IRD will select cases which meet the pre-set selection criteria of its computer programme for detailed examination. These criteria include whether the cases involve confirmor, whether the property is sold at a profit within a short period of time after purchase, and whether the same person or company has multiple property transactions within a certain period of time. For cases involving shares transfer of "property holding companies", IRD's Stamp Office, when stamping the transfer of shares in private companies, will refer suspected cases to the Assessing Unit for review. In the light of members' concern, IRD has compiled statistics on suspected cases in the form of transfer of "property holding companies" which have been referred to the Assessing Unit since April 2010. So far, there were 15 such cases, which accounted for less than 0.1% of the total number of property transactions (around 15 000 cases) in April 2010.

Proposed amendments to the Bill

16. Mr James TO has remained of the view that increasing the transaction costs of sub-sale through confirmor is a more effective measure to curb property speculation. In this connection, he has indicated intention to amend SDO to the effect that an additional stamp duty in a sum of X% of the amount or value of the consideration for the chargeable agreement for sub-sale exceeding $20 million shall be payable by the confirmor. Some members have noted that the policy intention of the proposed amendment is to impose an additional stamp duty on a sub-sale agreement of property valued more than $20 million. They have expressed concern that the proposal may not be fair to those who have genuine needs to sell their properties before completion of assignment. Besides, the proposal may drive speculation on properties valued less than $20 million. According to the Administration, the issue of effectiveness should be looked at holistically, taking into account that the two tax measures being proposed are part and parcel of a basket of measures of the Government to curb speculation and ensure the stable and healthy development of the property market. The Administration has also made some comments on the technical aspects of the proposed amendment. The Administration's response is set out in LC Paper No. CB(1) 2325/09-10(01).

Committee Stage amendments

17. Both the Administration and the Bills Committee will not move any Committee Stage amendments (CSAs) in their names. Hon James TO has indicated his intention to move CSAs.

Recommendation

18. The Bills Committee supports the Administration's proposal to resume the Second Reading debate on the Bill on 14 July 2010.

Consultation with the House Committee

19. The House Committee at its meeting on 25 June 2010 supported the recommendation of the Bills Committee in paragraph 18.

Prepared by
Council Business Division 1
Legislative Council Secretariat
8 July 2010

Appendix I

Bills Committee on Stamp Duty (Amendment) Bill 2010

Membership list

Chairman	Hon CHAN Kam-lam, SBS, JP
Members	Ir Dr Hon Raymond HO Chung-tai, SBS, S.B.St.J., JP Hon James TO Kun-sun Hon Miriam LAU Kin-yee, GBS, JP Hon Abraham SHEK Lai-him, SBS, JP Hon Audrey EU Yuet-mee, SC, JP Hon LEE Wing-tat Hon WONG Ting-kwong, BBS, JP Hon CHIM Pui-chung Hon WONG Kwok-kin, BBS Hon Paul TSE Wai-chun
	(Total : 11 Members)
Clerk	Miss Becky YU
Legal Adviser	Mr Stephen LAM
Date	17 May 2010