

**The Government's response to the draft Committee Stage Amendments
proposed by the Hon Abraham SHEK Lai-him and
Hon Andrew LEUNG Kwan-yuen**

This paper sets out the Government's response to the draft Committee Stage Amendments (CSAs) proposed by the Hon Abraham SHEK Lai-him (*LC Paper No. CB(1)1826/12-13(01)*) and Hon Andrew LEUNG Kwan-yuen (*LC Paper Nos. CB(1)1826/12-13(02) and (03)*).

Draft Committee Stage Amendments (CSAs) proposed by the Hon Abraham SHEK Lai-him

2. The CSAs proposed by the Hon Abraham SHEK specify that the Buyers Stamp Duty (BSD) paid by a company owned by Hong Kong Permanent Residents (HKPRs) (i.e. HKPR companies) in acquiring a residential property can be refunded three years after the acquisition at the earliest, subject to the meeting the following conditions which include –

- (a) the company has no more than five HKPR-members, who are acting on their own behalf in holding the shares of the company as the registered and the beneficiary owner;
- (b) the company has no more than three directors and all of them are HKPRs;
- (c) during the three years after property acquisition there has not been any change in shareholding and the property has not been disposed of; and
- (d) each of the HKPR-members and HKPR-directors should declare, amongst other things, that the member is holding his or her share(s) in the company as the registered and beneficial owner, and the member / director is a HKPR, etc.

3. After thorough consideration, we consider that the proposed CSAs will lead to adverse implications with regard to the policy objectives and the effectiveness of the BSD.

Implications of the CSAs for the policy objectives of the BSD

4. As we have reiterated in our previous replies to the Hon SHEK,

granting BSD exemption to companies owned by HKPRs is contrary to our policy objective to accord priority to HKPRs in order to address their home ownership needs. Due to excessive liquidity worldwide, many major international cities, including Hong Kong, are facing the risk of a property market bubble. Until the property market returns to a normal state, the Government must put in place effective demand-side management measures to curb market exuberance and to safeguard the healthy and stable development of the property market.

Implications of the CSAs for the effectiveness of the BSD

5. The Hon SHEK's CSAs, if implemented, would undermine the effectiveness of the BSD by creating loopholes that are very difficult, if not impossible, to plug. In Hong Kong, it is commonly known that the cost of setting up a company is low and the procedures involved are simple. Besides, to acquire the ownership and control of assets held by a company (including residential properties) through changing the shares and ownership of the company holding such assets is a very common commercial activity in Hong Kong. The crux of the problem is that there are numerous means to transfer company shares and ownership. Under the current regime, the validity of the transfer of the ownership in the company would not be affected even if such transactions are not registered with the Companies Registry and the instruments involved (which may need to be stamped) are not presented to the Inland Revenue Department (IRD) for stamping.

6. In other words, if HKPR-owned companies were exempted from the BSD, people outside Hong Kong could easily make use of various means which would be hard to uncover or trace to acquire the beneficial interest of the shares of the company and gain control of the company in a concealed way.¹ This would in effect allow that person outside Hong Kong to gain control of the residential property owned by the company, and at the same time evade the BSD.

7. A person from outside Hong Kong may also, through arrangements and ways that are hard to be traced, acquire the control of the HKPR company concerned behind the scene, and in turn assume the effective ownership of the residential properties held by the company, thus successfully evading the BSD. As we have repeatedly pointed out, fundamental changes to the existing simple yet effective taxation and company regimes will be required if we are to plug

¹ For example, through a company with only one HKPR as its shareholder and director who is asked to sign a blank instrument of transfer and surrender all seals of the company to the person from outside Hong Kong.

these loopholes². Furthermore, even if the present taxation and company regimes were changed, there is still no guarantee that the IRD could uncover the non-compliance cases. The effort required would be disproportionate when seen against the implementation of an extraordinary measure such as the BSD.

8. On the face of it, the CSAs which propose BSD be refunded after three years seem to impose a condition on or set a barrier for the exemption of the BSD. However, the truth is that it will disseminate a message to the market that upon expiration of the specified period, the residential properties concerned will “defrost”. Rationalising the refund of the BSD would actually bring about an adverse impact by providing an even greater incentive for tax evasion. People from outside Hong Kong would be encouraged to make use of arrangements as mentioned above to the effect that they could legitimately acquire, upon the lapse of the freezing period, all the shares of the HKPR-companies concerned and in turn, acquire directly the ownership of the residential properties held by the companies. In this scenario of course, the BSD paid would be refunded, thus effectively nullifying the duty.

9. In addition, the proposed BSD refund mechanism would encourage more HKPRs to purchase residential properties in the name of a company, since they can sell the shares of the properties holding the companies concerned to any person (including a person from outside Hong Kong) after the property is “defrosted”. By then, even if the BSD is still in effect, purchasers who are from outside Hong Kong would nonetheless not subject to the BSD³. In other words, there may be an increase of HKPRs purchasing residential properties in the name of a company for investment or speculation purpose, as they will be able to stock up residential properties which will be free from any BSD liabilities after the freezing period. This is inconsistent with our policy objective to accord priority to HKPRs to address their home ownership needs. Moreover, the proposed three-year “freezing period” would lapse together with the holding period in respect of the Special Stamp Duty (SSD). These would stimulate an immediate demand for residential properties and render the Government’s demand-side management measures meaningless.

10. Even with the proposed introduction of a refund mechanism alongside a statutory declaration mechanism and heavier penalties, the aforementioned

² Such as making fundamental changes to the Company Ordinance and the Stamp Duty Ordinance by requiring that the Company Registry and the IRD should be informed of all actions that involve changes in company controlling stake. This will result in actual changes to the operation of all companies.

³ The ad valorem stamp duty rate for share transfer is 0.2% of the consideration. In contrast, when an HKPR sells a residential property under his/her name to a person from outside Hong Kong, the transaction is subject to an ad valorem stamp duty for the property transfer. Not only is the rate higher than that of the share transfer, the person from outside Hong Kong will also be subject to the BSD, if the measure is still in effect.

loopholes simply cannot be effectively plugged. As we have repeatedly explained, there are various means to transfer company shares and ownership which can effectively get around verification provided under the current regime. The proposed statutory declaration mechanism will be rendered ineffective as a result and the penalty, however heavy, can hardly be of any deterrent value. In view of the substantial amount of the BSD at stake (i.e. 15% of the consideration of the relevant residential property transaction), coupled with the fact that there are situations where the transfer of shares and ownership may be concealed, the relevant exemption will provide substantial incentive for BSD evasion. We should not underestimate the risk of BSD evasion arising from the aforesaid loopholes. The proposed exemption will create real loopholes that are very difficult to plug. Under the current extraordinary situation where supply remains tight and the property market remains exuberant, being a responsible Government, we cannot simply ignore the obvious loopholes that may be created by exempting companies owned by HKPRs from the BSD. Particularly when these would significantly undermine the effectiveness of the BSD to cool down the property market and thwart the policy intention of according priority to the home ownership needs of HKPRs.

11. As mentioned in LC Paper No. CB(1)893/12-13(01), the Government is concerned about the impact of exempting companies from the BSD on the effectiveness of the various demand-side management measures which the Administration has introduced. The enhanced Special Stamp Duty, the introduction of the BSD and the increase in the ad valorem stamp duty rates (new AVD) target different specific buyers. These measures are interrelated and work collectively to achieve the objectives of combating speculations and managing demand. Under the proposed new AVD regime, in determining whether a HKPR has possessed more than one residential property and hence subject to the new AVD, the residential property held by that HKPR through a company of which he is a shareholder would not be taken into account. If companies of which all shareholders are HKPRs were to be exempted from the BSD, those who wish to possess more than one residential property might simply purchase a residential property in the name of a company without the need to pay the BSD. At the same time, they can also circumvent the new AVD when they purchase another residential property in their own names. If so, this would undermine the effectiveness of the proposed new AVD regime. These persons would be able to avoid the BSD and new AVD, which would be inconsistent with the policy intent of the series of demand-side management measures and would seriously undermine the effectiveness of these measures in achieving their objectives to manage demand.

Definition of HKPR companies under the CSAs

12. Under the BSD refund mechanism proposed by the Hon Shek, the number of HKPR members of the eligible company should not be more than five, while the number of HKPR directors should not be more than three. However, the justifications for these arrangements are not clear. The Government is concerned that without a clear logic for the selection of a particular number of shareholders and directors there will be debates in society over the reasonable number of members or directors, and the inevitable question of whether the proposed measure is discriminatory against other types of companies. This question leads direct to the related question of whether or not the long-existing 'level playing field' among companies in Hong Kong can be maintained.

13. In conclusion, the Government is firmly of the view that the proposed CSAs will only incentivise non-HKPRs to ride on companies owned by HKPRs to evade the BSD in a convenient manner. The Government considers that it would be extremely difficult to plug the loopholes created by the CSAs, which will undermine the effectiveness of the BSD to cool down the property market substantially, thereby affecting the policy objective to accord priority to the home ownership needs of the HKPRs.

Draft CSAs proposed by the Hon Andrew LEUNG

14. The Hon Andrew LEUNG's proposed amendment is to set a date on which the SSD and BSD would lapse, that is, a so-called 'sunset clause'. As we have reiterated repeatedly, it is impossible for the Government to predict future market changes and various external factors, and come up with a date as to when the demand-side management measures would no longer be applicable. Therefore, any prescribed sunset clause may only disseminate erroneous messages to the market and fuel demand, thus undermining the effectiveness of the measures.

15. Moreover, the sunset clause proposed by the Hon LEUNG in respect of the SSD, which specifies that section 29CA, 29DA of and 1(1AA) and 1(1B) of the First Schedule to the Stamp Duty Ordinance (Cap.117) will expire by midnight on 26 October 2015, will result in the both the existing SSD regime currently in place by virtue of the Stamp Duty Ordinance and the enhanced SSD as proposed in the Bill expiring on the specified date (or any other date determined by a Legislative Council Resolution). As the purpose of the Bill is limited to imposing a higher rate of duty for residential properties acquired on or after 27 October 2012 according to the length of period for which they had been held, the Government is of the view that the Hon LEUNG's proposed

amendments are beyond the scope of the Bill.

Transport and Housing Bureau
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