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Report of the Bills Committee on Inland Revenue (Amendment) Bill 2014

Purpose

This paper reports on the deliberations of the Bills Committee on Inland Revenue (Amendment) Bill 2014 ("the Bills Committee").

The Bill

2. The Inland Revenue (Amendment) Bill 2014 ("the Bill"), which was gazetted on 25 April 2014 and first read at the Legislative Council ("LegCo") meeting of 7 May 2014, seeks to amend the Inland Revenue Ordinance (Cap. 112) ("IRO") to give effect to the proposals concerning tax concessions in the 2014-15 Budget, and to provide for relevant transitional matters. The tax concession proposals are to: –

(a) increase the dependent parent or grandparent allowance and the additional dependent parent or grandparent allowance under salaries tax and tax under personal assessment, both from $38,000 to $40,000, for each eligible parent or grandparent aged 60 or above[1];

(b) increase the dependent parent or grandparent allowance and the additional dependent parent or grandparent allowance under salaries tax and tax under personal assessment, both from $19,000 to $20,000, for each eligible parent or grandparent aged between 55 and 59;

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[1] That allowance may also be claimed in respect of a dependent parent or grandparent who is under the age of 60 and is eligible to claim an allowance under the Government's Disability Allowance Scheme ("GDAS"), as provided for under sections 30(1) and 30A(1) of IRO.

(c) raise the deduction ceiling for elderly residential care expenses under salaries tax and tax under personal assessment from $76,000 to $80,000 for each eligible parent or grandparent[2]; and

(d) reduce salaries tax, tax under personal assessment and profits tax for the year of assessment 2013-14 by 75%, subject to a ceiling of $10,000 per case.

3. The main provisions of the Bill are as follows –

(a) Clause 3 amends section 89 of IRO to provide that the transitional provisions set out in the new Schedule 31 (added by clause 7) have effect in relation to a person liable to pay provisional salaries tax in respect of the year of assessment 2014-15;

(b) Clause 4 adds a new section 96 to IRO. The new section and the new Schedule 32 (added by clause 7) provide for the reduction of salaries tax, tax under personal assessment and profits tax payable for the year of assessment 2013-14 by 75%, subject to a maximum of $10,000 in each case;

(c) Clause 5 amends Schedule 3C to IRO to increase the maximum amount of elderly residential care expenses deductible from assessable income from $76,000 to $80,000 for the year of assessment 2014-15 and subsequent years of assessment;

(d) Clause 6 amends Schedule 4 to IRO to stipulate the increases set out in paragraphs 2(a) and (b) above and that the increases will take effect for the year of assessment 2014-15 and subsequent years of assessment; and

(e) Clause 7 adds new Schedules 31 and 32 to IRO. The new Schedule 31 provides for the transitional arrangements relating to the assessment of, and holding over of payment of, provisional salaries tax for the year of assessment 2014-15.

4. The Bill contains no commencement provision. By virtue of section 20(2) of the Interpretation and General Clauses Ordinance (Cap. 1), the Bill, if passed, would come into operation on the day the enacted amendment ordinance

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2 Who is either aged 60 or above or who is under the age of 60 and is eligible to claim an allowance under GDAS, as provided for under section 26D(1) of IRO.

is published in the Gazette.

The Bills Committee

5. At the House Committee meeting on 9 May 2014, Members agreed to form a Bills Committee to study the Bill. The membership list of the Bills Committee is at **Appendix I**. Under the chairmanship of Hon Kenneth LEUNG, the Bills Committee has held one meeting with the Administration. The Bills Committee has posted a notice on the website of LegCo and written to the 18 District Councils ("DCs") to invite the public and the DCs for written views on the Bill, but has not received any submission.

Deliberations of the Bills Committee

6. The Bills Committee supports the Bill in principle. The major deliberations of the Bills Committee are set out in the ensuing paragraphs.

Rationales for the tax concession proposals

7. Noting that there have been different views and suggestions from various sectors of the community on the tax concessions to be introduced, the Bills Committee has enquired about the rationale for and the considerations underlying the tax concessions proposed in the 2014-15 Budget.

8. The Administration has responded that in formulating each year's budget, the Financial Secretary will engage the public and meet with LegCo Members, professional bodies and other relevant parties to gauge their views and suggestions. The Financial Secretary will take into account the views expressed by the public and various stakeholders during the consultation, together with the Administration's assessments of the prevailing local and external economic environment, the economic outlook, the impact of the proposed measures on Government's fiscal position as well as the taxation regime, etc., in finalizing the concessionary tax measures to be introduced.

9. The Administration has further advised that adjustments to tax allowances and deductions have long-term fiscal impact. In the 2012-13 Budget, the Administration increased across the board all the allowances under salaries tax and tax under personal assessment. In the three previous Budgets,

there was an aggregate increase of 40% in the child allowances. Increases in the dependent parent/grandparent allowance and the additional dependent parent/grandparent allowance were also proposed in the 2011-12 and 2012-13 Budgets but not in the 2013-14 Budget. Having regard to the views gathered during the Budget consultation, the Administration considers it appropriate to propose increases in the dependent parent/grandparent allowances and the deduction ceiling for elderly residential care expenses in the 2014-15 Budget to alleviate taxpayers' burden in maintaining dependent parents or grandparents. In addition, the Administration has proposed a one-off reduction of salaries tax, tax under personal assessment and profits tax for the year of assessment 2013-14 as one of the counter-cyclical one-off relief measures in the 2014-15 Budget.

10. With regard to profits tax, the Bills Committee has enquired whether the Administration has considered the suggestion from some sectors in the community of adopting a two-tier profits tax system whereby a lower profits tax rate would apply to enterprises with smaller assessable profits. The Administration has responded that since profits tax is the biggest source of government revenue, such suggestion requires careful examination, having regard to such factors as the fairness principle, the financial implications to the Government and the susceptibility of such a two-tier profits tax system to tax avoidance arrangements by way of splitting businesses, thus calling for anti-avoidance provisions which would inevitably complicate the existing simple tax regime. The Administration has also pointed out that in recent years, only around 90 000 of some 900 000 registered corporations have to pay profits tax based on their assessable profits, indicating that Hong Kong’s tax base is already narrow. Adopting such a two-tier profits tax system would cause government revenue to be more reliant on a relatively small number of large corporations, which in turn would result in greater volatility in tax revenue at times of fluctuations in economic conditions.

<u>Financial implications of the proposed tax concessions</u>

11. The Bills Committee notes that about 550 000 taxpayers would benefit from the proposed increases in allowances and deduction ceiling under salaries tax and tax under personal assessment. The revenue forgone is estimated to be about $300 million a year.

12. As for the proposed one-off tax reduction for the year of assessment 2013-14, the Bills Committee notes that about 1.74 million taxpayers will benefit from the proposed one-off reduction of salaries tax and tax under personal assessment and the revenue forgone is about $9.2 billion, whereas the proposed one-off reduction of profits tax will benefit about 126 000 tax-paying companies and unincorporated businesses and the revenue foregone is about $1 billion.

Joint assessment under salaries tax and tax under personal assessment

13. The Bills Committee notes that a married couple who receives employment income is assessed under salaries tax as separate individuals. However, they may elect to be jointly assessed if the election can reduce their overall tax liability. If the husband and/or wife of a married couple have income that is chargeable to profits tax and/or property tax, the married couple may elect for personal assessment to reduce their tax liability, but separate taxation for the couple is not applicable under personal assessment.

14. In this regard, the Bills Committee has sought information on the relevant arrangements in overseas jurisdictions, and statistics on the election of joint assessment under salaries tax and on the election of personal assessment in the past years. The information provided by the Administration is in **Appendix II**.

Due dates for tax payments

15. Noting that for salaries tax and tax under personal assessment, the due dates for tax payments differ among individual taxpayers, the Bills Committee has enquired how the payment due dates are determined. The Administration has advised that under IRO, a taxpayer is obliged to pay salaries tax or tax under personal assessment in respect of a particular year of assessment in one go by a date to be specified by the Commissioner of Inland Revenue ("CIR"). In practice, CIR exercises his discretion under IRO to allow taxpayers to pay the tax by two installments, usually in January and April of the relevant year. In determining the payment due dates for individual taxpayers, the Inland Revenue Department would give consideration to various factors. Generally speaking, taxpayers required to pay larger amounts of tax are likely to be subject to earlier payment due dates, and similar payment due dates would apply to the same taxpayer in subsequent years to facilitate his/her financial planning.

Transitional provisions relating to provisional salaries tax in respect of year of assessment 2014-15 (Clause 7)

16. The Bills Committee has noted that section 3 of the proposed Schedule 31 to IRO under clause 7 of the Bill provides that a taxpayer may apply for holding over payment of provisional salaries tax on the ground that the aggregate amount of the elderly residential care expenses paid or to be paid by the taxpayer or his/her spouse during the year of assessment 2014-15 exceeds or is likely to exceed $76,000 in respect of a parent or grandparent of the taxpayer.

17. In reply to the Bills Committee's enquiry about the rationale for the above proposed provision, the Administration has explained that a taxpayer may apply for holding over payment of provisional salaries tax on certain grounds as specified in IRO, namely –

(a) the taxpayer has become entitled to an allowance, which was not given in the notice for payment of provisional tax, for example, child allowance for his/her newborn baby, or dependent parent allowance for his/her parent who has attained the qualifying age in the year of assessment for which provisional tax was charged;

(b) the taxpayer's net chargeable income for the year of assessment for which provisional tax was charged is, or is likely to be, less than 90% of the net chargeable income for the preceding year or of the estimated sum in respect of which he/she is liable to pay provisional tax;

(c) the taxpayer has ceased, or will before the end of the year of assessment for which provisional tax was charged cease, to derive income chargeable to salaries tax; or

(d) the taxpayer has objected under section 64 of IRO to his/her assessment to salaries tax for the year preceding the year of assessment.

The proposed provision seeks to provide an additional ground for taxpayers to apply for holding over payment of provisional salaries tax in the year of assessment 2014-15 if the taxpayer is entitled to a deduction for elderly residential care expenses that is likely to exceed $76,000 in that year of assessment.

18. The Chairman of the Bills Committee has suggested that instead of enacting transitional provisions each time adjustments are made to the deduction items, the Administration should consider introducing a standing provision in IRO to include entitlement to deductions exceeding a certain amount as a ground for application for holding over payment of provisional salaries tax. The Administration agrees to give consideration to this suggestion.

<u>Legal and drafting aspects</u>

19. The Bills Committee has examined the Bill clause by clause, and has not identified any difficulties relating to the legal and drafting aspects of the Bill.

Committee Stage amendments

20. No Committee Stage amendments to the Bill have been proposed by the Administration or the Bills Committee.

Resumption of the Second Reading debate

21. The Bills Committee supports the resumption of the Second Reading debate on the Bill at the Council meeting of 25 June 2014.

Consultation with the House Committee

22. At its meeting on 13 June 2014, the House Committee noted the deliberations of the Bills Committee.

Council Business Division 4
<u>Legislative Council Secretariat</u>
16 June 2014

Appendix I

Bills Committee on Inland Revenue (Amendment) Bill 2014

Membership list

Chairman	Hon Kenneth LEUNG
Members	Hon LEE Cheuk-yan Hon CHAN Kam-lam, SBS, JP Hon Alan LEONG Kah-kit, SC Hon Gary FAN Kwok-wai Hon Charles Peter MOK Dr Hon Fernando CHEUNG Chiu-hung Hon SIN Chung-Kai, SBS, JP (Total : 8 Members)
Clerk	Ms Anita SIT
Legal Adviser	Miss Evelyn LEE

Bills Committee on Inland Revenue (Amendment) Bill 2014

The Administration's Responses to Matters Arising from the Meeting held on 27 May 2014

This paper sets out the Administration's responses to the matters raised at the meeting on 27 May 2014, covering -

(a) information on overseas jurisdictions in respect of their adoption of joint assessment arrangements for taxpayers similar to those provided for married couples under salaries tax in Hong Kong; and

(b) the respective numbers and percentages of taxpayers in past years -
  (i) who elected joint assessment under salaries tax;
  (ii) who actually benefited from reduced tax liability as a result of the election of joint assessment;
  (iii) who elected personal assessment; and
  (iv) who actually benefited from reduced tax liability as a result of the election of personal assessment.

Joint Assessment for Married Persons in Hong Kong

2. Under salaries tax, a married person is responsible for all aspects of his or her own tax affairs including lodgement of returns and payment of tax assessed. However, if the aggregate salaries tax of a married couple under separate assessments is greater than it would have otherwise been when they are jointly assessed, they may elect joint assessment. In other words, all married couples with joint assessments raised receive tax benefits.

3. The numbers and percentages of salaries tax payers who elected and benefited from joint assessment for the years of assessment 2010/11 to 2012/13 are tabulated below -

Year of Assessment	2010/11	2011/12	2012/13
Number of taxpayers who elected and benefited from joint assessment	267 360	286 956	318 766
As a percentage of the total number of individuals subject to salaries tax	11.7%	11.8%	12.7%

Personal Assessment in Hong Kong

4. Personal assessment provides a means whereby an individual can elect to be assessed on his or her total income from three taxable sources: profits from trade, income from employment and rentals from properties. The individual can claim deduction of business losses, deduction of interest incurred to produce rental income, as well as concessionary deductions and personal allowances under salaries tax. Progressive rates under salaries tax are also applicable to personal assessment.

5. The numbers and percentages of taxpayers who elected and benefited from personal assessment for the years of assessment 2010/11 to 2012/13 are tabulated below -

Year of Assessment	**2010/11**	**2011/12**	**2012/13**
Number of taxpayers who elected and benefited from personal assessment	291 522	299 206	321 994
As a percentage of the total number of individuals subject to profits tax, salaries tax and property tax	12.0%	11.5%	12.0%

Taxation Arrangements in Overseas Jurisdictions

6. Based on information available to the Inland Revenue Department, married couples are either taxed separately, or taxed jointly/as a family unit in other jurisdictions (see table below).

Jurisdictions	**Separate Taxation**	**Joint or Family Unit Taxation**
Australia	✓	
Austria	✓	
Belgium		✓
Canada	✓	
China	✓	
Denmark	✓	
France		✓
Germany(Note)	✓	✓
Ireland(Note)	✓	✓
Italy	✓	
Japan	✓	
Korea	✓	
Netherlands	✓	
New Zealand	✓	
Norway(Note)	✓	✓
Singapore	✓	
Sweden	✓	
Switzerland		✓
United Kingdom	✓	
United States	✓	✓

(Source: International Bureau of Fiscal Documentation)

Note: These jurisdictions allow married couples to enjoy the lower of the tax liability from either separate taxation or joint/family unit taxation.

Financial Services and the Treasury Bureau
June 2014