立法會
Legislative Council

LC Paper No. CB(1)889/17-18

Ref: CB1/BC/5/17

Paper for the House Committee meeting on 4 May 2018

Report of the Bills Committee on Inland Revenue (Amendment) Bill 2018

Purpose

This paper reports on the deliberations of the Bills Committee on Inland Revenue (Amendment) Bill 2018 ("the Bills Committee").

Background

2. To alleviate the burden of taxpayers, the Financial Secretary announced various proposals concerning tax concessions in the 2018-2019 Budget. The Inland Revenue (Amendment) Bill 2018 ("the Bill"), gazetted on 9 March 2018 and introduced into the Legislative Council ("LegCo") on 21 March 2018, seeks to amend the Inland Revenue Ordinance (Cap. 112) ("IRO") in order to implement the following adjustments for salaries tax and tax under personal assessment from the year of assessment ("YA") 2018-2019:[1]

(a) increasing the number of tax bands from four to five with marginal rates at 2%, 6%, 10%, 14% and 17% respectively and widening the tax bands from $45,000 to $50,000 each;[2]

(b) increasing both the child allowance for each eligible child and the additional child allowance in respect of each child born in the YA from $100,000 to $120,000 (hereafter referred to collectively as "child allowances");

1 All the provisions and schedules mentioned in the ensuing paragraphs of this report refer to those of IRO.

2 The existing marginal rates for the four tax bands are 2%, 7%, 12% and 17%.

(c) increasing both the dependent parent/grandparent allowance and the additional dependent parent/grandparent allowance for each eligible parent/grandparent from $46,000 to $50,000 (for aged 60 or above, or disabled) and from $23,000 to $25,000 (for aged 55 or above but below 60) (hereafter referred to collectively as "dependent parent/grandparent allowances");

(d) raising the deduction ceiling for elderly residential care expenses for each eligible parent/grandparent from $92,000 to $100,000; and

(e) introducing a new personal disability allowance of $75,000 for eligible taxpayers with disability.

The Bill also seeks to amend IRO to give effect to a one-off reduction of salaries tax, tax under personal assessment and profits tax for YA 2017-2018 by 75%, subject to a ceiling of $30,000 per case.

3. The Bill, if passed, would come into operation on the day on which it is published in the Gazette as an Ordinance.

The Bills Committee

4. The House Committee agreed at its meeting on 23 March 2018 to form a bills committee to study the Bill. The membership list of the Bills Committee is in **Appendix I**. Under the chairmanship of Mr WONG Ting-kwong, the Bills Committee has held one meeting to discuss the Bill with the Administration.

Deliberations of the Bills Committee

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

<u>Proposed adjustments to tax bands and marginal rates</u>

6. Mr KWOK Wai-keung conveys the support from Members belonging to The Hong Kong Federation of Trade Unions for the proposed widening of tax bands. Mr WU Chi-wai has stated that Members belonging to the Democratic Party ("DP") support the proposed adjustments to tax bands and marginal rates, which are in line with DP's aspiration that such measures should help achieve the broader objective of a better and fairer allocation of wealth and resources in the community, apart from alleviating the financial burden on taxpayers.

However, Mr WU queries why the Administration has not considered DP's long-advocated proposal of abolishing the standard rate of 15% for assessment of salaries tax and tax under personal assessment, such that the tax rate for the majority of the higher-income taxpayers will be raised from 15% (standard rate) to 17% (marginal rate for the highest tax band) if the progressive rate is the only option. In his view, this suggested arrangement is reasonable as those who earn more and can afford should pay more tax.

7. The Administration has explained that at present, salaries tax payable is calculated at progressive rates on a person's net chargeable income (i.e. assessable income after deductions and allowances) or at standard rate of 15% on the net total income (i.e. assessable income after deductions but before allowances). If the tax payable on the basis of a person's net chargeable income exceeds the tax charged at standard rate on the person's net total income, the person is only required to pay the lower amount of tax. This regime aligns with the policy intent to maintain the simple and low tax system of Hong Kong, and is commensurate with the recently introduced two-tiered profits tax rates regime. The Administration has advised that while there is no plan at this stage to abolish the standard rate for salaries tax and tax under personal assessment, it will continue to regularly review the taxation system of Hong Kong, including the tax bands and rates of various taxes.

8. The Administration has further informed members that currently, only some 20 000 to 30 000 taxpayers (around 1%) out of about 1.9 million taxpaying income earners in Hong Kong have been paying salaries tax or tax under personal assessment at the standard rate. It should be noted that a person's total annual income is not the sole determinant of whether the standard rate or progressive rates will be applied for assessment of such taxes. Other factors such as the person's family conditions (e.g. the number of dependants) and unique circumstances may also affect the amount of claimable allowances or deductible expenses for calculation of the net total income/net chargeable income of the person in relation to the standard rate or progressive rates.

9. The Administration has provided for members' reference supplementary information on the number of taxpayers who paid salaries tax or tax under personal assessment at the standard rate for YA 2016-2017, with breakdowns by income range, final tax assessed and the percentage out of the total salaries tax and personal assessment tax revenue; and the impact on tax revenue if the progressive rates are adopted instead.[3]

[3] Please refer to paragraphs 2 to 4 of the Administration's paper (LC Paper No. CB(1)864/17-18(02)) for the details.

Child allowances

10. Members welcome the proposal to increase the child allowances from $100,000 to $120,000. In view of the fact that non-taxpayers with newborns will not be able to benefit from this proposal, Mr KWOK Wai-keung has suggested the Administration introduce a direct subsidy in future in respect of each eligible child in the year of birth to alleviate the burden of infant care expenses on the parents. The Bills Committee has noted that the suggestion is not related to the Inland Revenue (Amendment) Bill 2018. The Chairman has advised that members may pursue the suggestion through other channels.

Dependent parent/grandparent allowances

11. Regarding the proposal to raise the dependent parent/grandparent allowances from $46,000 to $50,000 (for aged 60 or above, or disabled) and from $23,000 to S25,000 (for aged 55 or above but below 60), Mr YIU Si-wing considers that the amount of these allowances as well as the extent of the proposed increases are relatively small and not proportionate to those of the child allowances, and do not seem to provide strong incentives to encourage the younger generation to live with and/or take care of their parents/grandparents. Mr YIU calls upon the Administration to consider increasing the dependent parent/grandparent allowances at a greater magnitude in future, taking into account the ageing population in Hong Kong.

12. The Administration has advised that the dependent parent/grandparent allowances have been adjusted frequently in previous years, with the last upward adjustment made since YA 2016-2017. The Administration will continue to regularly review and propose adjustments as appropriate to the levels of the various allowances and deduction ceilings.

New personal disability allowance

13. Dr Fernando CHEUNG has commended the Administration for aptly introducing a new personal disability allowance for eligible taxpayers with disability since the existing disabled dependant allowance cannot benefit such taxpayers directly.[4] He believes that the newly introduced personal disability allowance will help relieve the financial burden of taxpayers with disability, and the tax savings can be used to support their healthcare and travelling expenses.

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4 A person can claim the disabled dependant allowance (currently $75,000 for each dependant) if the person or the person's spouse maintains a dependant who is eligible to claim an allowance under the Government's Disability Allowance Scheme.

Impact on wealth gap

14. Dr Fernando CHEUNG considers it unnecessary to include profits tax in the proposed one-off tax reduction as it may have the unintended effect of widening the wealth gap in Hong Kong and increasing the Gini coefficient by returning wealth to some already well-off members of the public. Dr CHEUNG opines that the Administration should give regard to the potential impacts when considering tax concession measures in future.

15. The Administration has advised that the proposed adjustments to allowances and deductions for salaries tax and tax under personal assessment will reduce tax revenue by $6.43 billion a year, while the proposed one-off reduction of salaries tax, tax under personal assessment and profits tax for YA 2017-2018 will result in revenue forgone in the amount of $25.5 billion in total ($22.6 billion for salaries tax and tax under personal assessment, and $2.9 billion for profits tax). Currently, about one-fourth of the government's tax revenue comes from profits tax amounting to some $130 billion a year, with the number of taxpaying enterprises in the region of 140 000. Hence, the some $2.9 billion revenue forgone as a result of the proposed one-off reduction of profits tax is not substantial and would not significantly impact on government revenue, nor would it have impact on the Gini coefficient.

16. The Administration has further advised that around 1.9 million out of some 3.8 million salaries earners are liable to salaries tax at present. The proposed adjustments to tax bands and marginal rates are expected to benefit taxpayers mainly in the middle to lower income groups.

17. At the request of Dr Fernando CHEUNG, the Administration has provided information on its assessment of the potential impact on the Gini coefficient arising from the adjustments to tax bands and marginal rates and the one-off reduction of profits tax. In gist, it is technically not feasible to assess the impact of the proposed adjustments to tax bands and marginal rates on the post-tax Gini coefficients, and that the proposed one-off reduction of profits tax had no impact on any of the Gini coefficients compiled by the Census and Statistics Department.

Other tax concession measures to be introduced by separate legislative exercises

18. Members note that the following measures will be implemented by separate legislative exercises: (a) introducing a new tax deduction for salaries tax and tax under personal assessment for Voluntary Health Insurance Scheme expenses with a ceiling of $8,000 per insured person a year; and (b) removing the restriction that a married person may only elect for personal assessment jointly with his/her spouse. In the above connection, Mr KWOK Wai-keung

considers that the proposed deduction ceiling in respect of Voluntary Health Insurance Scheme expenses should be raised with a view to covering more expenses incurred by taxpayers for taking out the insurance. The Chairman has advised that members may raise suggestions on the proposed measures on future occasions as and when the relevant legislative proposals are introduced into LegCo.

Drafting aspects

Clauses 5 to 9

19. For previous amendments to IRO to give effect to tax concessions in the Budget in recent years, the practice was to introduce new schedules containing, for instance, provisions on additional grounds for holding over of payment of provisional salaries tax or provisions relating to one-off reduction of certain taxes in respect of a specific YA to which the Budget proposals related. The Bills Committee notes that a different drafting approach has been adopted under clauses 5 to 8 of the Bill whereby the proposed additional grounds for holding over of provisional salaries and profits tax would be incorporated into the existing sections 63E and 63J respectively as standing provisions (i.e. new sections 63E(2)(ba) to (bd) and 63J(2)(ab)), and that a new section 63CA would be added to provide clarifications as to the meaning of certain references to other provisions.

20. The Bills Committee also notes that under clause 9 of the Bill, instead of providing for the proposed one-off reduction of certain taxes in a schedule as in the past few years, it is proposed that a new standing provision, namely section 100, be added for that purpose, while a new Schedule 44 is proposed to be added to prescribe the reduction percentages as well as the reduction ceilings for the different taxes.

21. The Administration has explained that the new drafting approach will obviate the need to introduce transitional provisions or new schedules each time for the purpose of implementing any adjustment in respect of an allowance or a deduction item, or providing one-off tax reduction. Mr Kenneth LEUNG welcomes the new arrangement as he had suggested when scrutinizing a similar bill (i.e. the Inland Revenue (Amendment) Bill 2014). At the request of the Legal Adviser to the Bills Committee, the Administration has provided a written response to elaborate on the reasons for adopting the new drafting approach in question, as well as to explain the legal effect and operation of the proposed provisions.[5]

[5] Please refer to the Legal Adviser to the Bills Committee's letter to the Administration (LC Paper No. CB(1)799/17-18(01)) and the Administration's reply (LC Paper No. CB(1)799/17-18(02)) for details.

New section 63CA

22. Referring to the heading of the new section 63CA ("Calculating net chargeable income for computing provisional salaries tax: meaning of certain references" / "為計算暫繳薪俸稅而計算應課稅入息實額：若干提述的涵義"), Mr Kenneth LEUNG has commented that the heading is insufficiently clear as to the purpose and effect of the proposed provision. The Administration has explained that the new section 63CA is an interpretation provision providing for the meaning of certain references in section 63C(1), and the heading reflects what is contained in the provision. Mr LEUNG has requested the Administration to continue improving the drafting of legislation in general with a view to enhancing their clarity and comprehensibility. The Administration has taken note of the member's views and suggestion.

Proposed amendments

23. As the Administration expects that the current Bill will be passed by LegCo before the Inland Revenue (Amendment) (No. 6) Bill,[6] it has proposed amendments to re-number the proposed "Schedule 44" as "Schedule 43" to reflect the actual order of the Schedule after passage of the Bill, as set out in **Appendix II**. The Bills Committee has examined and raised no objection to the proposed amendment. The Bills Committee will not propose amendments to the Bill.

Resumption of Second Reading debate on the Bill

24. The Bills Committee supports the resumption of the Second Reading debate on the Bill at the Council meeting of 16 May 2018.

Advice sought

25. Members are invited to note the Bills Committee's deliberations set out above.

Council Business Division 1
Legislative Council Secretariat
2 May 2018

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6 As at the time of submission of this report, the Inland Revenue (Amendment) (No. 6) Bill 2017 is under scrutiny by another bills committee.

Appendix I

Bills Committee on Inland Revenue (Amendment) Bill 2018

Membership list

Chairman	Hon WONG Ting-kwong, SBS, JP
Members	Hon James TO Kun-sun Hon WU Chi-wai, MH Hon YIU Si-wing, BBS Hon Charles Peter MOK, JP Hon LEUNG Che-cheung, SBS, MH, JP Hon Kenneth LEUNG Hon KWOK Wai-keung, JP Dr Hon Fernando CHEUNG Chiu-hung Dr Hon Elizabeth QUAT, BBS, JP Hon CHUNG Kwok-pan Hon Alvin YEUNG Hon Holden CHOW Ho-ding Hon YUNG Hoi-yan Hon Vincent CHENG Wing-shun, MH
	(Total : 15 members)
Clerk	Ms Angel SHEK
Legal Adviser	Miss Joyce CHAN

Appendix II

Committee Stage

Amendments to be moved by the Secretary for Financial Services and the Treasury

Clause	Amendment Proposed
9	In the proposed section 100(6), by deleting "44" (wherever appearing) and substituting "43".
16	By deleting "**Schedule 44**" (wherever appearing) and substituting "**Schedule 43**".