Hong Kong Institute of
Certified Public Accountants
香港會計師公會

Dear Assignment / News / Business Section Editor

Hong Kong Institute of CPAs' budget proposals ask government to take advantage of an improving economy to strengthen business competitiveness and families

(Hong Kong, 18 January 2010) – The Hong Kong Institute of CPAs' budget proposals released today recommend reducing taxes for companies and improving benefits for individuals, increasing certainty in the tax system, and adopting measures to support the development of Hong Kong's new and "pillar" industries.

The Institute is suggesting that corporate tax rates be reduced to 16 percent for 2010-11 and the salaries tax allowances for dependants be increased by 20 percent, among other salaries tax benefits.

"As Hong Kong continues its gradual and steady recovery from the financial crisis, we need to build on our economic strengths and improve our competitive position for the future. As the Chinese economy continues to grow and mainland enterprises look for overseas investments, Hong Kong should be ready for these business opportunities," says Ayesha Macpherson, the Institute's taxation committee chair. "A combination of tax reductions and a clear tax system will help Hong Kong locally and internationally."

Cuts and competition

Based on Hong Kong's improving economy, the Institute is suggesting a reduction in corporate profits tax rate for 2010-11 from 16.5 percent to 16 percent, and to 15 percent over the longer term. The standard rate should remain at 15 percent. Looking ahead and with an eye toward the city's future growth, the Institute is calling for a comparative study of effective tax rates within the region, with the aim of assessing whether it is appropriate for Hong Kong to reduce the corporate profits tax to below 15 percent. The Institute notes that Hong Kong's regional competitors, such as Singapore, have drastically dropped their tax rates over the past decade.

"While we still have a low-tax regime, the gap between Hong Kong and other markets has been narrowing significantly in recent years," says Macpherson. "We must not become complacent or take it for granted that the tax system here gives us an unrivalled advantage," she adds. "We should upgrade and improve it where necessary."

The Institute is recommending more support for families and the hard-pressed, middle income group with 20 percent increases in child allowances and allowances for dependent parents, grandparents, and disabled family members. In addition, an increase in the deduction for elderly residential care should assist those who face increasingly expensive bills for close relatives requiring institutional care. The Institute has also proposed a new deduction for private medical insurance to encourage more people to consider the option of private medicine to help ease the burden on public health services.

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"The cost of living in Hong Kong remains high and the financial crisis did not seem to have lasting impact on property or other prices," explains Florence Chan, convenor of the Institute's budget proposals sub-committee. "Our proposed increases in allowances will go some way to help with the costs of maintaining a household."

Certainty attracts businesses

For years, the Institute has been an advocate for a clearer tax system and streamlined administration, arguing that businesses need to know where they stand from a tax point of view when they submit their returns. One unclear but fundamental part of our tax code concerns whether particular profits are to be treated as onshore and so taxable or offshore and not taxable. This is a sore spot in particular given the volume of international transactions carried out in the territory, according to Macpherson.

Another important area of uncertainty is transfer pricing, where there is a risk of double taxation if the rules on acceptable pricing of transactions between related parties are not laid out transparently. To keep up with peers, Hong Kong also needs to put in place a group loss relief system.

There is also uncertainty, in practice, in determining whether an increasingly mobile and international workforce is employed in, and taxable in, Hong Kong or employed offshore. The taxability of employees who travel frequently is an issue for business decision-makers who choose regional headquarters for their companies. To address this problem more effectively, the Institute recommends adopting an approach similar to that adopted in many overseas markets. That is to base the "source" of employment income on the place where services are actually rendered, subject to the existing 60-day exemption rule.

Driving economic growth

Financial services and professional services, two of Hong Kong's cornerstone businesses, could benefit from tax measures to expand the market and open new niches; for example, fund management, insurance, and Islamic financing are all sectors within the financial services industry that could be encouraged with tax breaks.

For professional and producer services, many international companies look to set up regional offices and headquarters. For these businesses, where much of the work is cross-border, concessionary tax rates for management fees from overseas associates and tax exemptions for loan interest from overseas associates should be considered, according to the Institute.

While the Institute's submission points out that pillar industries, such as financial services and producer and professional services, continue to be engines of economic growth for Hong Kong, it is not clear how long the HKSAR can stay ahead of the pack.
"We need to explore opportunities to diversify our economy and develop new industries for the future, like those identified by the chief executive in the policy address," says Chan.

To genuinely move Hong Kong towards a more knowledge-based economy, the Institute is advocating expanding the territory's research and development capabilities The budget proposals include "super deductions" (i.e. more than 100 percent) for research and development expenses to stimulate research and development.

To attract more investment in the form of intellectual property development and licensing in Hong Kong, the Institute proposes adopting a "place of use" test to determine source of royalty income; a 100 percent deduction for intellectual property acquisition costs (for trademarks, copyrights, brand names, licensing rights, on top of patents and know-how) and a more favourable tax treatment for the disposal of intellectual property rights.

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Note to editor

About the Hong Kong Institute of CPAs

The Hong Kong Institute of CPAs is the only body authorized by law to register and grant practising certificates to Certified Public Accountants in Hong Kong. The Institute has more than 29,000 members and 13,000 registered students. Members of the Institute are entitled to the description *certified public accountant* and to the designatory letters *CPA*.

The Hong Kong Institute of CPAs evolved from the Hong Kong Society of Accountants, which was established on 1 January 1973.

The Institute operates under the Professional Accountants Ordinance and works in the public interest. The Institute has wide-ranging responsibilities, including assuring the quality of entry into the profession through its postgraduate Qualification Programme and promulgating financial reporting, auditing and ethical standards in Hong Kong. The Institute has responsibility for regulating and promoting efficient accounting practices in Hong Kong to safeguard its leadership as an international financial centre.

The Hong Kong Institute of CPAs is a member of The Global Accounting Alliance - an alliance of the world's leading professional accountancy bodies, which was formed in 2005. The GAA promotes quality services, collaborates on important international issues and works with national regulators, governments and stakeholders.

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