Tax policy and budget proposals 2022-23

Building a Sustainable Future for Hong Kong, its economy and community

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

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  - Consider incentives for downstream recycling, waste-to-resources/ energy infrastructure, e.g. subsidies on land costs and facilities; and explore and encourage second-life applications of EV batteries.

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- The EV-charging at Home Subsidy Scheme should be continued and expanded and the approval process should be expedited.
- The Government should continue to encourage and support public transport operators to explore and test the application of green innovative transport technologies, e.g., hydrogen fuel cell EVs.

Introduction

The COVID-19 pandemic ("Covid"/ "the pandemic") has been affecting economies across the world for nearly two years. Although the quick development and introduction of Covid vaccines has enabled some normality, the virus continues to have significant impacts on the daily lives of people, public health systems and economic growth worldwide. The new Omicron variant, first detected in November in Africa, has led to a resurgence in cases and the reintroduction of travel and social distancing restrictions in many jurisdictions.

Although many countries have experienced economic bounce-backs, inflation is becoming a concern, which may impact further recovery. The Federal Reserve has signalled that there will be three rates increases in 2022,[1] and central banks worldwide are beginning to unwind the support they provided markets during the pandemic.

Locally in Hong Kong, after going through four waves of coronavirus infections, the pandemic appears to be largely under control. With the concerted efforts of the Government of the Hong Kong Special Administrative Region ("the Government"), health authorities, businesses and the community, it is encouraging to note that economic activities picked up in the second half of 2021, with the financial secretary ("FS") announcing an increase in Hong Kong's projected economic growth for 2021 as a whole to 5.5%-6.5%. Yet this has been at the expense of some of the strictest quarantine arrangements in the world and virtually closed borders to non-residents. As a result, the economic recovery has been uneven, with exports of goods surpassing the high recorded in the same period of 2018 by a considerable margin while inbound tourism remains frozen[2].

There have been some significant developments this year that affect Hong Kong, and the Government should consider how it reacts to them in order to maintain Hong Kong's status as a world-leading international financial centre.

Revitalizing Hong Kong's economy

Reopening the border for quarantine-free travel between Hong Kong and Mainland China ("the Mainland") has been the priority of the Government. Reopening the border is vital in order to support Hong Kong's position in the country, and its development under the 14th National Five-Year Plan, which was released in 2021. The quarantine-free arrangements were announced in November 2021 and the chief executive of Hong Kong ("CE") does not expect that the Omicron variant will alter the plans to reopen the border.[3] Hong Kong's health code system for cross-border travel opened for registrations on 10 December[4] and attracted over 440,000 registrations in the first 5 days.[5]

Reconnecting Hong Kong to the Mainland is key to Hong Kong's future development and implementation of the 14th National Five-Year Plan. The plan, published in March, provides Hong Kong a role in the "dual circulation" economic development of the country, driven by innovation and domestic demand. The plan sees Hong Kong become a "participant" in domestic circulation and a "facilitator" of international circulation in the "dual circulation" development strategy[6]. It builds on Hong Kong's strengths in four key areas as an international financial centre, transportation centre, trade centre, and legal and dispute resolution services.

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[1] https://www.reuters.com/markets/us/fed-prepares-stiffen-inflation-response-post-transitory-world-2021-12-15/

[2] https://www.hkeconomy.gov.hk/en/situation/development/index.htm

[3] https://www.bloomberg.com/news/articles/2021-12-14/hong-kong-says-china-border-plans-still-on-after-omicron-case

[4] https://www.info.gov.hk/gia/general/202112/09/P2021120900238.htm

[5] https://www.thestandard.com.hk/breaking-news/section/4/184514/Cross-border-quota-to-open-to-public-on-first-come-first-serve-basis

[6] https://www.brandhk.gov.hk/docs/default-source/factsheets/hong-kong-themes/2021-10-05/hong-kongs-role-in-the-national-14th-five-year-plan-e.pdf

As well as the four traditional areas, the plan calls for Hong Kong to develop as an aviation hub, an innovation and technology centre, a regional intellectual property ("IP") trading hub, and a hub for arts and cultural exchanges. The development of the Greater Bay Area ("GBA") is further prescribed in the plan, with Hong Kong as one of the main cities of the GBA it has the opportunity to develop and integrate into the economy of the country.

Importance of sustainability

The 2021 United Nations Climate Change Conference COP26, took place in October 2021, and led to the agreement for countries to produce stronger 2030 emissions reductions targets by COP27 in 2022, and to curb methane emissions. It was also the first time that countries had explicitly committed to reducing the use of coal, one of the most environmentally damaging fuels[7]. The president of COP26 noted that the Glasgow Climate Pact emphasized the urgent need to accelerate efforts to turn targets into action to keep 1.5% within reach (i.e. the limit on the global average temperature rise)[8]. Hong Kong should, therefore, consider how it can play its part in this monumental agreement.

Also at COP26, the International Financial Reporting Standards Foundation announced the formation of the International Sustainability Standards Board ("ISSB") to develop sustainability reporting foundations. The new board will work to consolidate various international standards and produce a single set of sustainability reporting standards. Hong Kong has committed to implementing these new standards[9], and should seek to contribute to their development, as it does with other international accounting and related standards.

BEPS and the international tax landscape

COP26 was not the only major international agreement this year. The latest developments in the international tax landscape, including the European Union ("EU")'s review of harmful tax practices and the Organization for Economic Cooperation and Development ("OECD")'s Base Erosion Profit Shifting ("BEPS") 2.0 project, have brought about significant challenges to Hong Kong's simple tax system. The BEPS 2.0 proposals were set out in a statement issued by the OECD in October 2021, and cover two pillars - Pillar One is the allocation of some taxing rights to consumer markets, and Pillar Two is the right to tax corporate income that has suffered a jurisdictional effective tax rate of below 15%. Model rules for Pillar Two, for incorporation into domestic laws, were published on 20 December 2021 and additional substantive and technical details for key elements of both pillars are yet to be released. It is expected that Pillar Two will be brought into effect in 2023, with certain exceptions. Hong Kong therefore needs to prepare for these developments.

To continue the momentum towards a sustainable recovery the Institute makes 15 recommendations in these budget proposals.

[7] https://www.wri.org/insights/cop26-key-outcomes-un-climate-talks-glasgow

[8] https://ukcop26.org/cop26-president-remarks-at-closing-plenary/

[9] https://www.bloomberg.com/news/articles/2021-11-05/hong-kong-to-implement-new-climate-audit-standards-by-end-2022

I. Revitalizing Hong Kong's economy

Issue 1: Promote digital transformation

During the Covid pandemic, many businesses have had to rely on virtual tools to minimize the disruption to their operations. Various factors, such as the increase in remote working, customer demand for online purchasing/services and migration of data to cloud storage, have speeded up the adoption of digital technologies. An increasing number of companies and organizations have adopted a hybrid model, which incorporates a mixture of in-office and remote working. It is believed that these changes will remain after the pandemic and we cannot expect a return to pre-Covid norms[10].

Hong Kong is no exception to this world-wide pattern and the second edition of Hong Kong's Smart City Blueprint[11], issued in December 2020, set out a wide range of initiatives on the development of innovation and technology with the aim of building a world-renowned Smart Hong Kong characterized by a strong economy and a high-quality living environment. Yet, support in this area for small and medium-sized enterprises ("SMEs"), which are the backbone of the economy, is patchy and SMEs often seem to be unaware of what is available for them.

Review and rationalize information technology ("IT")-related funding schemes for SMEs and startups

New technology can help SMEs to optimize their operational processes and reduce operating costs. It is expected that more SMEs will need to undergo digitalization in the coming years to ensure the sustainability of their business. They will also be asked to play their part in Hong Kong's transformation to a carbon neutral economy in the longer term and digitalization can help them move away from paper based processes and to operate more sustainably generally. However, SMEs are among the worst hit by the pandemic, as they tend to rely heavily on a small number of suppliers and customers and may not have the know-how or the resources to adapt.

While there are various information technology ("IT") support schemes to help SMEs digitalize, such as the Technology Voucher and Distance Business ("D-Biz") Programmes administered by the Hong Kong Productivity Council, we believe that there is scope for more promotion and for outreach to companies.

We also suggest that the Government should review and, where possible, rationalize and consolidate these different schemes. They should consider forming a central contact point or one-stop shop to assess potential applicants, and advise them on the most efficient route to apply for the relevant support programmes. Singapore, for example, established StartupSG to unify efforts to support the startup ecosystem under its various initiatives and programmes. The StartupSG website appears to be well organized and systematic in illustrating specific schemes for different stages of startups[12].

[10] McKinsey Global Survey of executive: https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/how-covid-19-has-pushed-companies-over-the-technology-tipping-point-and-transformed-business-forever

[11] https://www.smartcity.gov.hk/

Second edition: https://www.smartcity.gov.hk/modules/custom/custom_global_js_css/assets/files/HKSmartCityBlueprint(ENG)v2.pdf

[12] https://www.startupsg.gov.sg/programmes/

IT support for SMEs

In addition, the existing IT-related funding schemes tend to provide one-off project-based subsidies, while SMEs may also require continuing digitalization and IT support. Given that they often find it difficult to recruit suitable personnel and that more advanced technology may require ongoing maintenance, we suggest supporting SMEs to hire IT specialists, and/ or up-skill their employees and their proprietors to improve their IT capability. An arrangement could be put in place along the lines of the Research Talent Hub for Innovation and Technology Fund projects ("RTH-ITF")[13] under the Innovation and Technology Commission, or a more tailored version of YOUTH, the Financial Industry Recruitment Scheme for young graduates, with an emphasis on engaging more experienced IT (post) graduates and specialists.

We would also suggest establishing a more focused version of the Continuing Education Fund ("CEF"), or expanding the CEF, to cover practical training for company staff and proprietors in IT and digitalization. In addition to increasing digital awareness and helping SMEs to tackle the basic question of "how and where do we start", SMEs awareness of other related areas, including cyber security and data protection also needs to be strengthened.

Continue to develop a user-friendly electronic tax filing system

Since early 2021, the Inland Revenue Department ("IRD") has been undertaking a two-phase project on e-filing of profits tax returns. In the first phase, the existing eTax Portal will be enhanced by 2023 to enable more businesses to voluntarily file profits tax returns electronically, together with their financial statements and tax computations. In the second phase, a new Business Tax Portal will be developed by 2025 for the e-filing of profits tax returns, with the ultimate goal of achieving full-scale implementation of mandatory e-filing by 2030.

The IRD consulted on a proposed Taxonomy Package in January, aimed at facilitating the electronic submission of financial statements and tax computations in inline eXtensible Business Reporting Language ("iXBRL") format. Furthermore, the Inland Revenue (Amendment) (Miscellaneous Provisions) Ordinance 2021 was enacted in June. Among other things, the ordinance seeks to enhance the statutory framework for the e-filing of tax returns. Another consultation paper was issued on 4 November setting out proposals on the further development of the e-filing system.

The Institute made submissions on the proposed Taxonomy Package and on the legislation. We have all along encouraged digitalizing the tax return filing process. Any e-filing system needs to be user-friendly and compatible with the way business is conducted and how businesses and their professional advisers interact. We are pleased to note, therefore, that the IRD is aware of the importance of providing greater clarity in relation to the penalty provisions applicable to persons who, under the ordinance, may furnish a return on the taxpayer's behalf, which is an area of concern for practitioners.

Ultimately, the system should help to improve efficiencies and align Hong Kong with international best practices. To ensure the most effective outcome, the Government should

[13] https://www.itf.gov.hk/en/funding-programmes/nurturing-talent/research-talent-hub/research-talent-hub-for-itf-projects-rth-itf-/index.html

continue to conduct detailed discussions and consultations with the market and the profession on the design and operation of the system.

We propose therefore the following specific measures:

- **Increase awareness of Government IT support programmes for SMEs and establish a central contact point/ one-stop shop for applicants to receive advice and be directed to, and assisted with, the most appropriate source of funding.**
- **Set up a scheme subsidizing SMEs to hire an IT specialist (e.g. a recent (post-) graduate). We suggest offering a subsidy of 50% of the employment cost, up to a ceiling of HK$16,000 per month for up to 36 months (c.f. the subsidies under the RTH-ITF**)[14].
- **Establish a new fund, or expand the CEF, to cover practical training for company staff and proprietors in IT and digitalization**.
- **Ensure a practical, user-friendly e-filing system that helps improve efficiencies and aligns Hong Kong with international best practices. Closely consult the users on the design and operation of the system to achieve the best outcome.**

Issue 2: Taking advantage of opportunities in the Greater Bay Area

The GBA serves as a platform to forge stronger ties and synergies among Hong Kong, Macau and the nine Mainland cities. Being an international commercial and financial centre with high-quality professional services, Hong Kong has long been leveraging its unique advantages as a gateway to the GBA and rest of Mainland China. Hong Kong continues to serve as a "super connector" for multinational companies accessing the Mainland market and Mainland companies seeking to expand overseas. The GBA strategic development brings valuable opportunities to Hong Kong's businesses to expand their base in the Mainland, particularly in the area of innovation and technology ("I&T") development, and strengthen Hong Kong's gateway role through greater collaboration with other cities within the GBA. Against this background, we make the recommendations outlined below.

Improve Hong Kong professionals' awareness of opportunities in the GBA and seek a level playing field for suitably-qualified Hong Kong professionals to practise in the GBA or relevant areas in it

It is necessary to increase awareness of the context, markets and business environment in the GBA cities. The Institute successfully applied for funding from the Government's Professional Services Advancement Support Scheme ("PASS") to support a series of activities catering to members' needs in the GBA, including a series of "Working and Living in the GBA" webinars, to help members understand the local policies and business environment in different GBA cities. A Cross-border Internship Programme has also been formulated to support young accountants in pursuing job and internship opportunities in the region. However, the PASS funding scheme serves a broad scope of activities and is subject to various constraints. Therefore, we would suggest that Government set up a dedicated and flexible fund to support business promotion and development in the GBA, to which eligible Hong Kong professionals can apply. It could also be used for, e.g., internships for young professionals that may not be covered by existing GBA youth employment and internship funding programmes.

[14] See Footnote 13 above

We would also call upon the Government to assist Hong Kong professional accountants, where appropriate, to practise and serve their clients who establish a presence in the GBA. For example, Macau registered auditors and accountants have been granted certain rights to practise tax in the Shekou and Qianhai, as have some Hong Kong tax advisers. The Institute runs an intensive, examined, Professional Diploma in China Tax programme[15], which includes 45 teaching hours, nine workshops and seven tutorials in China tax, with additional coverage of international tax and professional ethics. In order to obtain the diploma qualification, members must also complete a workshop in professional ethics and an examined International Tax Course. Since the Professional Diploma in China Tax started, there have been around 160 graduates of the course. We propose that members who are full-time tax practitioners and, in particular, those members who have successfully completed the Institute's Professional Diploma in China Tax programme should also be granted certain practising rights to perform tax services in the GBA, or at least in relevant areas of Shenzhen and would urge that the Government lend its support to achieving a level playing field for all suitably-qualified Hong Kong professionals in the GBA.

Permit depreciation allowances to be claimed on plant and machinery, and allow the deduction of capital expenditures incurred on the purchase of intellectual property rights used in the GBA, i.e. partially relax the restrictive requirements of section 39E and 16EC of the Inland Revenue Ordinance ("IRO")

To encourage Hong Kong companies extending operations into the GBA, the restrictive requirements of sections 39E(1)(b) and 16EC(4)(b) of the IRO, which disallow claims for depreciation allowances for leased plant and machinery ("P&M") and deductions of capital expenditure incurred on the purchase of intellectual property ("IP") rights used outside Hong Kong, should be relaxed, specifically within the GBA area.

We note that the Hon Jimmy Ng, representing the Industrial (Second) Functional Constituency in the Legislative Council ("LegCo"), recently sought clarification from the Government in a LegCo question that touched on a related issue[16]. The Government replied to the relevant part of the question:

"In accordance with the established "territorial source" and "tax symmetry" principles, the IRD will not charge profits tax on profits which are derived outside Hong Kong. Similarly, depreciation allowance will not be granted for any machinery and plant solely used in manufacturing activities outside Hong Kong. Section 39E of the IRO aims at preventing tax avoidance opportunities arising from machinery or plant leasing arrangements, and similar requirements are also imposed under section 16EC of the IRO in relation to the purchase of intellectual property rights for use outside Hong Kong by other parties."

The Government's reply does not take into account the fact that the commercial objective of providing the P&M and IP rights is to secure the supply of goods to be traded by the Hong Kong taxpayers. As such, it is our view that the relevant costs should be regarded as incurred

[15] https://www.hkicpa.org.hk/en/Professional-development/Specialist-Practice-Development/Specialist-training--programmes/Taxation
[16] https://www.ird.gov.hk/eng/ppr/archives/21032401.htm

by the Hong Kong taxpayers for the production of their trading profits, which are generally fully chargeable to tax in Hong Kong.

However, we are aware that this is a long-standing issue and the LegCo question concerned the use of P&M and IP rights used in production processes in the Mainland's overseas Economic and Trade Co-operation Zones rather than the GBA. We consider that the denial of claims for depreciation allowances for leased P&M and deductions for capital expenditure incurred on the purchase of IP rights used outside Hong Kong under sections 39E(1)(b) and 16EC(4)(b) could hinder Hong Kong companies expanding into the GBA. Given the special status of the GBA and its unique connection with Hong Kong, therefore, we recommend the relaxation of the requirements within this limited geographical area, so that depreciation allowances for leased P&M, and the deduction of capital expenditure incurred on the purchase of IP rights, will be allowed, as long as they are used in the GBA. This would also be in keeping with common business practices and commercial realities.

Make research and development ("R&D") deduction rules more flexible within the GBA

Across the GBA cities, governments are prioritizing I&T development. For example, preferential tax treatments and incentives are offered by both the tax authorities in the Mainland and Hong Kong for companies engaging in R&D activities.

The Government in Hong Kong has introduced enhanced tax deductions for qualifying R&D expenditure, where the first HK$2 million of eligible R&D expenditure will enjoy a 300% tax deduction, with the remainder at 200%. However, these "super deductions" are applicable only to qualifying R&D activities conducted in Hong Kong, either in-house or by a designated local research institution. The underlying intention of increasing R&D activities, attracting talent and employment in Hong Kong is well understood, but these activities can be costly. To encourage further integration of Hong Kong within the GBA, and for Hong Kong businesses leveraging GBA's well-established I&T ecosystem, we recommend that the Government extend the enhanced R&D deductions to cover Hong Kong-controlled R&D activities carried out within the GBA, or relevant parts of the GBA.

Provide non-tax incentives/ subsidies to Hong Kong companies and individuals in the GBA

In addition to tax incentives, we suggest the Government should consider non-tax incentives and/ or subsidies to help attract talent and assist businesses and individuals to capture opportunities under the GBA initiatives. For example, a one-off relocation subsidy for overseas talents moving to Hong Kong under a GBA initiative.

We propose therefore the following specific measures in relation to leveraging on GBA opportunities:

- **Set up a dedicated and flexible GBA fund to support business promotion and development in the GBA, to which eligible Hong Kong professionals can apply.**
- **Support a level playing field for suitably-qualified Hong Kong professionals to practise in the GBA.**
- **Partially, relax the restrictive requirements of sections 39E and 16EC of the IRO, to permit depreciation allowances for leased P&M, and the deduction of capital expenditure on the purchase of IP rights, to be claimed for use by Hong Kong taxpayers within the GBA.**

- **Extend the enhanced R&D deductions to cover Hong Kong-controlled R&D activities carried out within the GBA, or relevant parts of the GBA.**
- **Consider other non-tax incentives and/ or subsidies to assist businesses and individuals to capture opportunities under the GBA initiatives, such as a one-off relocation subsidy for overseas talents moving to Hong Kong under a GBA initiative.**

Issue 3: Attract overseas investment

Promote and maintain Hong Kong as an international commercial centre

Hong Kong is ranked as the world's freest economy again in the latest Economic Freedom of the World 2021 Annual Report issued by the Fraser Institute[17]. However, there is little room for complacency because, as the authors point out, the report was based on 2019 data, which may not reflect the latest economic, legal and social developments in Hong Kong. It is essential, therefore, that Hong Kong maintains an investor-friendly environment, the rule of law, a relatively simple and low-rate tax system, and a quality of life to attract investment and overseas talent, as well as to nurture and to retain local talent, if Hong Kong aims to maintain its international rankings.

Review investment promotion strategies and policies and explore possible tax and non-tax incentives

In the light of changing international perceptions about Hong Kong, and against the background of a rapidly evolving international tax environment, referred to *Section II* below, which could make it more complicated to rely on tax incentives and a low tax regime alone to attract future investment, we would suggest that there is a need to review Hong Kong's investment promotion strategies and policies. Consideration needs to be given to Hong Kong's positioning and to potential non-tax incentives and advantages that can be offered to boost Hong Kong's standing and reputation as a good location for investment and place to live and work. It would be worthwhile to hold a major conference/ symposium on this theme, or a series of forums/ focus group discussions, to generate fresh, new and innovative ideas from a diverse range of stakeholders.

Take steps to maintain/ improve standards of English and Mandarin

To maintain Hong Kong's competitive edge as an international financial centre, action needs to be taken to address perceptions of declining standards of, and interest in, English in the community. In order to take full advantage of the opportunities generated by the Mainland's development, particularly in the GBA, attention also needs to be given to enhancing the general standard of Mandarin. The Government needs to support the objective of making Hong Kong truly a bi-literate (Chinese and English) and trilingual (Cantonese, Putonghua and English) society by setting out its strategy and policies for achieving this, both within the formal education system and through support for good-quality language courses offered by other training institutes and adult education centres.

[17] https://www.fraserinstitute.org/sites/default/files/economic-freedom-of-the-world-2021-execsumm.pdf

Revise tax rules to promote Hong Kong as an intellectual property hub

With the aim of developing Hong Kong into a regional IP trading centre, in the Policy Address 2021, the CE indicated that the Government is planning to implement a series of initiatives to promote the development of IP trading in Hong Kong. It will also strengthen Hong Kong's IP regime, as well as stepping up promotion, education and external collaboration. Among these initiatives, the public is currently being consulted on the modernization of the copyright regime in light of the digital environment. In connection with this consultation exercise, the secretary for commerce and economic development stated[18] that the "*Outline of the 14th Five-Year Plan for National Economic and Social Development of the People's Republic of China and the Long-Range Objectives Through the Year 2035*" approved by the National People's Congress in March 2021 raises, for the first time, the support for Hong Kong to develop into a regional IP trading centre. We believe that it is high time to revive the copyright review exercise."

In addition to the above, Hong Kong should strive to provide a tax environment that is conducive to supporting the global operations of IP-related businesses. This is particularly important in light of the recent growth of innovative industries, such as pharmaceuticals, gaming and high-tech businesses, many of which are looking for the best location to list and house their IP. In recent years, an enhanced deduction for qualifying R&D expenditure has been introduced, as mentioned above, and three additional types of IP rights have been included in the deduction regime. Yet, these rules remain complex with many restrictions. Some of the anti-avoidance rules also hinder genuine restructuring and mergers and acquisitions from taking place in a tax efficient manner.

In addition to the measures regarding sections 39E and 16EC of the IRO, relating specifically to the GBA, other measures that should be considered to further enhance the IP tax regime include the following:

- Modify the enhanced R&D tax deduction rules, taking into account the real commercial constraints of businesses engaged in R&D activities, which are unable to enjoy the deduction (normal or enhanced). Consider the possibility of R&D tax credits for start-up businesses.
- Relax the anti-avoidance provisions under the IP deduction rules to allow genuine commercial transactions to enjoy the benefits.
- Expand the scope of tax deductions on expenditure in relation to certain "intangible assets", e.g., upfront lump-sum payments made for acquiring a licence or franchise, spectrum utilization fees and payments for indefeasible rights of use.
- Provide more certainty in terms of the taxation of royalty income whilst amending the tax law to address the EU's concerns on offshore passive income.

Explore the possibilities to extend the re-domiciliation rules to limited companies

Hong Kong, being a relatively low tax jurisdiction, could be an attractive jurisdiction for companies that are doing substantial business in Hong Kong, but which have their legal base elsewhere, to relocate their base and relatively mobile group activities. However, at present the Hong Kong Companies Ordinance (Cap. 622) does not provide for foreign companies re-domiciling into Hong Kong. There were requests from the business sector for introducing re-

18 https://www.info.gov.hk/gia/general/202111/24/P2021112400481.htm?_cldee=dmlja3l5dUBoa2ljcGEub3JnLmhr&recipientid=contact-5edfd2b54537ea11b8100050568d1b3e-420b9a3963ca478590502490248e46c0&esid=41d132b2-7256-ec11-b81a-0050568d4f85

domiciliation rules into the Companies Ordinance in 2019 in response to certain offshore jurisdictions, including the British Virgin Islands, Cayman Islands and Bermuda, introducing new economic substance laws; however, this was not regarded a policy priority by the Government at that time.

As the international tax landscape is evolving rapidly, multinational enterprises ("MNEs") have been assessing the potential impact on their operations, and may consider carrying out some cross-border group restructuring to lower their overall effective tax rates. While re-domiciliation mechanisms were introduced under the open-ended fund companies and limited partnership fund regimes in 2021, no similar arrangements have been put in place for other types of businesses. We suggest that the Government consider introducing general re-domiciliation rules in the Companies Ordinance.

Expedite treaty negotiations with major trading partners

We appreciate that the Government has been making strenuous efforts to expand Hong Kong's tax treaty network, even during the pandemic. Currently, 45 comprehensive avoidance of double taxation agreements ("CDTAs") have been signed. However, the number of CDTAs in place is still well below that in other major jurisdictions (e.g., the Mainland, the United Kingdom ("UK"), Japan and Singapore have each signed over 90 CDTAs). It is important that Hong Kong continues to expand it treaty network, particularly with major trading partners.

We propose, therefore, the following specific measures in relation to improving the investment environment:

- **Review Hong Kong's investment promotion strategies and policies and consider possible non-tax incentives and advantages that can be offered to boost Hong Kong's standing and reputation as a good location for investment, and as a place to live and work. Hold a major conference/ forums on this theme to gather views from a diverse range of stakeholders.**
- **Support the objective of making Hong Kong a truly bi-literate and trilingual society by setting out the strategy and policies for achieving this, both within the formal education system and through support for other good-quality language courses offered by other training institutes and adult education centres.**
- **Consider introducing general company re-domiciliation rules in the Companies Ordinance.**
- **Strive to provide a tax environment that is conducive to supporting the global operations of IP-related businesses, by, for example:**
    - **Modifying the enhanced R&D tax deduction rules, taking into account the real commercial constraints of businesses engaged in R&D activities and considering the possibility of R&D tax credits for start-up businesses.**
    - **Relaxing the anti-avoidance provisions under the IP deduction rules to facilitate genuine commercial transactions.**
    - **Expanding the scope of tax deductions for certain intangible assets.**
    - **Providing more certainty in terms of the taxation of royalty income while amending the law regarding offshore income.**
- **Continue to expand Hong Kong's network of CDTAs, particularly with major trading partners.**

Issue 4: Provide tax incentives and subsidies to targeted industries

Introduce tax incentives to companies engaged in IT businesses and green industries

Looking ahead, the green economy will become increasingly important in helping Hong Kong to achieve its goal of carbon neutrality by 2050, in line with the target of the Paris Agreement and COP26. While developing Hong Kong into a regional green finance hub is part of the strategy, this will not be sufficient by itself. It will also be important to encourage the development of industries that can contribute to the green economy and making Hong Kong more sustainable, as well as R&D in the areas such as new energy sources and applications, energy conservation, and use of IT to create a more energy efficient and less wasteful society. There are opportunities for Hong Kong as a densely-populated, highly-developed territory, surrounded by sea and hills, and receiving quite high levels of sunlight annually, to conduct more research into the generation and application of renewable energy, from sources such as wind and solar power.

The Government should consider introducing tax measures that support the policy objectives of developing green industries and promoting digital transformation.

We propose, therefore, consideration of the following specific measures in relation to supporting targeted industries:

- **Providing tax credits for start-up companies engaged in relevant IT businesses and green industries.**
- **Subject to the constraints of international tax developments regarding minimum effective rates of corporate tax (see Issue 5 below), introducing lower profits tax rates for qualifying IT and green industries for the first 5 years of profits (i.e., beyond the existing general concession on the first $2 million of assessable profits).**

Provide certainty and tax concessions for family offices [19]

In 2020, Hong Kong had over 9,500 people considered to be ultra-high net worth ("UHNW"), each with over US$30 million (HK$233 million) of assets. Coupled with over 10,000 UHNW families in the Mainland, Hong Kong is considered to have clear potential to develop as a hub for family offices for UHNW families within the region[20]. There are obvious advantages to pursuing this objective, e.g. attracting more capital into Hong Kong, boosting Hong Kong's finance and investment-related employment, and increasing the demand for the associated sectors, such as legal and accounting services.

As mentioned in the Policy Address 2021, the Government will step up its efforts to attract more family offices to establish a presence in Hong Kong by considering the provision of tax concessions, thereby enhancing Hong Kong's status as an international asset and wealth management centre. In June 2021, InvestHK set up FamilyOfficeHK[21], a dedicated team, to

[19] Financial Services Development Council proposals: https://www.fsdc.org.hk/media/lrej3ikz/fsdc_paper_no_45_family_wisdom_a_family_office_hub_in_hong_kong_paper_eng.pdf

[20] https://www.legco.gov.hk/research-publications/english/essentials-2021ise23-facilitative-measures-on-promoting-family-offices-in-singapore.htm#endnote11

[21] https://www.investhk.gov.hk/en/news/investhk-builds-familyofficehk-team-promote-hong-kong-leading-hub-family-offices-asia.html

offer “one-stop support services” for family offices. However, there are ongoing concerns that tax regulations are not conducive to Hong Kong’s being competitive as a regional hub for family offices.

We suggest below some considerations towards helping strengthen Hong Kong’s position as a hub for family offices.

Tax concessions

In recent years, Singapore has become one of the most favoured destinations in Asia for setting up new family offices and/or relocating existing ones through streamlining regulation and introducing various incentives.

Similar to Hong Kong, Singapore does not impose taxes on investment income accrued by individuals. Family offices in Singapore may also apply for tax exemption on the investments that they manage under various regimes, in accordance with their investment holding structures and the residence of family members. Those regimes include under Singapore’s Income Tax Act, section 13CA (Offshore Fund Tax Exemption Scheme), section 13R (Onshore (Singapore Resident Company) Fund Tax Exemption Scheme), section 13X (Enhanced Tier Fund Tax Exemption Scheme), section 13Z (Capital Gains Safe Harbour Exemption), and section 13G (Qualifying Foreign Trust Exemption).

Hong Kong should consider further concessions for family offices, where they are not eligible for either one of the Hong Kong’s two existing fund exemption regimes (e.g., a Hong Kong resident fund not qualifying as a collective investment scheme under the unified fund exemption regime). These can be made subject to certain minimum requirements to ensure that adequate benefits accrue to Hong Kong, such as a minimum of HK$2 million business spending per year and employment of, at least, two staff members during the year, etc. (c.f. the new regime for carried interest in the funds industry).

Certainty

There is no statutory definition of "family offices" in the Securities and Futures Ordinance (Cap. 571). In January 2020, the Securities and Futures Commission (“SFC”) issued a circular clarifying that family offices need not be licensed as entities like asset management companies, insofar they are serving only "related entities" (e.g., wholly-owned subsidiaries), but not a third party, and not engaged in a "regulated activity", as laid down in the ordinance. While the SFC reiterated that it has no intention to regulate single-family offices (“SFOs”), those family offices with more complicated structures may need to seek legal advice for regulatory certainty.

In Singapore, the Monetary Authority of Singapore introduced a licensing exemption regime to eligible family offices (mostly SFOs). Successful applicants are not subject to any licensing requirement under the Securities and Futures Act on the one hand, but are still entitled to tax exemptions under the Income Tax Act on the other. This represents a noticeable contrast with the licensing dilemma faced by SFOs in Hong Kong, whose investments in non-private companies could involve a trade-off between tax benefits and concern over compliance costs.

We suggest that the Government should consider the issuance of detailed guidance to provide more certainty on the potential licensing obligations for family offices. If it is not the intention for the SFC to license and regulate SFOs and certain multi-family offices, albeit, strictly speaking, some may be required to be licensed under the law, it is worth exploring the feasibility of issuing a specific exemption to such structures. This would put Hong Kong on a more equal footing with competing jurisdictions.

We propose, therefore, the following specific measures in relation to family offices:

- **Consider further tax concessions for family offices, where they are not eligible for either one of the Hong Kong's two existing fund exemption regimes. This should be subject to requirements to ensure that adequate benefits accrue to Hong Kong, in terms of, e.g., minimum business spending per year of, say, HK$2 million and a minimum of two employees.**
- **Consider specific licensing exemptions to enhance certainty and put Hong Kong on a more equal footing with competing jurisdictions.**

II. Comprehensive review of the Hong Kong tax system

Issue 5: Align tax policies with international tax rules

Many jurisdictions have been undergoing tax reforms or updating their tax laws, e.g., United States ("U.S.") tax reforms; and the introduction of diverted profits tax in Australia and the UK, in order to align their regimes with the changing international business and tax environment.

The latest developments in the international tax landscape, including the EU's review of harmful tax practices and the OECD's Base Erosion Profit Shifting ("BEPS") 2.0 project, have brought about significant challenges to Hong Kong's simple and low tax system. We understand that, Hong Kong will seek to comply with the international standards while striving to maintain the key advantages of Hong Kong's tax regime in terms of simplicity, fairness and relatively low rates. Meanwhile, the Government should also consider non-tax measures to promote business and maintain Hong Kong's competitiveness.

Respond to the evolving global tax landscape and review the relevant impact

BEPS 2.0

According to the latest BEPS 2.0 proposals, which have been endorsed by the OECD/ G20 Inclusive Framework on Base Erosion and Profit Shifting (of which Hong Kong is a member), and the statement issued by the OECD in October 2021 ("the October Statement"), new tax rules will be implemented in relation to two key areas:

- Pillar One: This amends the rules for allocating taxing rights over the profits of MNEs and, for the largest MNEs, allocates greater taxing rights to market jurisdictions, where their consumers are located. This will apply, initially, only to in-scope MNEs with global turnover above 20 billion euros and profitability above 10%.

- Pillar Two: This pillar will give the parent and source jurisdictions in which the relevant MNEs operate a right to tax undertaxed income where the MNEs effective tax rate in a jurisdiction is below 15%. Known as the Global Anti-Base Erosion ("GloBE") rules, these rules seek to ensure that MNEs pay a minimum level of tax in each jurisdiction in which they operate and to dissuade them from shifting profits to low tax jurisdictions. This pillar could have a more substantial impact on Hong Kong. With some exceptions, the GloBE rules will apply to MNEs that have group consolidated revenue of 750 million euros or more.

Model rules for domestic legislation for Pillar Two were agreed and published on 20 December 2021 and Pillar Two will be brought into effect by 1 January 2023.

The GloBE rules will have a significant impact on large MNEs and, potentially, on how they perceive Hong Kong as a location to invest. An MNE's income that is not subject to tax at an effective tax rate of at least 15% in a jurisdiction, may be subject to "top-up tax" in the jurisdiction of its ultimate parent entity. While Hong Kong's headline profits tax rate is currently 16.5%, effective tax rates of operations in Hong Kong are often lower, due to Hong Kong's territorial tax system, exclusion of capital gains and various tax concessions and incentive regimes.

The Government has set up an advisory panel to review the possible impact of BEPS 2.0 on the competitiveness of Hong Kong's business environment, and has also reached out to different stakeholders to collect views. The Institute welcomes these actions while urging that the Government's action plan in response to BEPS 2.0 should take into account the following:

- MNEs will make decisions based on the information available to them. At present, very little substantive information has been released about how the Government will respond to the Pillar Two proposals and the reactive changes that MNEs will need to make are likely to take effect shortly. Therefore, the Government should release a proposed action plan as soon as possible. Further guidance on how the relevant tax rules would be implemented would also be welcome.

- The impact of the GloBE proposal on business in Hong Kong and the competitiveness of Hong Kong's tax system should be kept to a minimum, as far as possible. The GloBE rules are aimed at large MNEs. While Hong Kong should adopt the rules, there is no requirement to make wholesale changes to Hong Kong's tax system, or to undermine the competiveness of the system, in order to accommodate the rules. Changes should be made on the basis of creating the least possible disruption to the existing system, and making any unavoidable changes in a way that is as painless as possible for in-scope MNEs.

- While Hong Kong's headline corporate profits tax rate is 16.5%, as indicated above, effective rates can be much lower. Therefore, Hong Kong may seek to prevent the loss of taxing rights and potential revenue. One option, which has been advocated by certain stakeholders as an appropriate defensive measure, would be to implement a domestic "alternative minimum tax" under the local tax law, mirroring the tax base and rate of GloBE. However, the Government should consider carefully the feasibility and possible impact of this option. The purpose of such a measure would be to ensure that in-scope MNEs' effective tax rate in Hong Kong would be at least equal to the agreed minimum rate and no more, and to ensure that the application of GloBE rules would not result in other jurisdictions collecting the tax differential on business conducted in or from Hong Kong. Further discussion with stakeholders is needed and time is of the essence.

- Hong Kong should focus on attracting investment and business with real substance, involving a relocation of MNEs' people and tangible assets, as well as, where appropriate, their intangible assets (see Issue 3) to Hong Kong through non-tax incentives, such as relocation benefits, as proposed above (see Issue 2).

- Whilst Hong Kong's tax rate will remain relatively low, in practice, as a result of the GloBE rules, the gap between this and the effective tax rates of other competing jurisdictions may become narrower. Some jurisdictions are considering non-tax incentives to continue to attract international investment. Non-tax incentives should also be explored to attract investors to Hong Kong.

- In this regard, the Government should also focus on other factors that facilitate and attract business to Hong Kong, such as the education of the workforce, technology and infrastructure, ease of international trade, children's education. Furthermore, as proposed above (see Issue 3), Hong Kong should actively continue to expand its network of CDTAs, free trade agreements and investment agreements.

Review of harmful tax practices

The impact of the ongoing review by the EU on harmful tax practices and territorial-based tax regimes should be monitored closely.

On 5 October 2021, the Council of EU added various jurisdictions, including Hong Kong, to the revised EU list of non-cooperative jurisdictions for tax purposes (commonly known as the "grey list") with immediate effect, following a review of their foreign source income exemption regimes. These jurisdictions may need to make changes to their legislation by 31 December 2022 in order to avoid being moved to the blacklist.

While the EU Code of Conduct Group ("COCG") does not view a territorial tax regime as necessarily problematic, it considers that problems arise when such regimes create situations of double non-taxation. Based on the guidance agreed by the COCG on the approach to assessing foreign source income exemption regimes, passive foreign source income that is fully exempt, without clear conditions, is considered harmful. If the passive income exemption is to be retained, adequate substance requirements on the entities concerned should be implemented. Having in place anti-abuse rules and removing any administrative discretion would also be required.

We understand that the Government has committed to amending Hong Kong's tax system by the end of 2022, with the amended system taking effect by 1 January 2023, without grandfathering arrangements. While we understand the value of co-operating with the EU with a view to addressing this issue, stakeholders in Hong Kong also need to be kept abreast of developments and consulted where appropriate, and the earlier the better. We suggest that, in the near future, the Government should issue further information on how the relevant tax laws will be revised and implemented.

In addressing the EU's concerns, the Government should seek to make the minimum necessary changes required to the tax system. Furthermore, any substance requirements that are to be introduced should take into account the practicality and commerciality of such measures. For example, it is common for groups, particularly in regulated industries, to employ staff in one service entity that undertake work for the entire group. As such, any substance requirements should be assessed on the basis of the group's substance in Hong Kong. Similarly, many listed ultimate parent companies of Hong Kong groups do not employ staff or own tangible assets directly, but it would be an odd outcome if they were considered to lack sufficient substance in Hong Kong when the group has substantial activities in Hong Kong. Therefore, consideration could also be given to a listed company exception from any substance requirements. Arrangements to facilitate re-domiciliation of offshore companies to Hong Kong, as proposed above (see Issue 3), could assist businesses to relocate to a reputable jurisdiction, as Hong Kong is, and build substance here in alignment with the EU's objectives.

Meanwhile, it would be advisable to ensure that incentives outside the scope of BEPS 2.0 do not fall foul of EU/ OECD measures on harmful tax practices, by conducting a more extensive review of Hong Kong's tax system. Going forward, the latest international requirements should also be taken into account when introducing new tax incentives.

We propose, therefore, the following specific measures in relation to the impact of international tax measures:

- **The Government should release a proposed action plan on how it will be responding to BEPS 2.0, in particular Pillar Two.**
- **Any changes should be made on the basis of the least possible disruption to the existing system, by avoiding affecting businesses that are not within scope and making any unavoidable changes in a way that is as painless as possible for in-scope MNEs.**
- **The Government should carefully consider the feasibility and possible impact of implementing options such as an "alternative minimum tax", under the domestic tax law, to mirror the tax base and rate of GloBE.**
- **Non-tax incentives and other factors to attract investors to Hong Kong should also be seriously considered.**
- **Regarding Hong Kong's inclusion on the EU "grey list", the Government should issue further information on how relevant tax laws will be revised and implemented in the near future.**

Issue 6: Review of Hong Kong's tax system

We continue to believe that a more extensive review of Hong Kong's tax system is called for, given, among other things:

- The need for broader-based taxes to ensure stability of revenues in the future, to help address the longer-term public finance needs and avoid structural deficits. This remains important given Hong Kong's aging population; lack of indirect; consumption-based taxes; and over-reliance on a few sources of revenue, primarily profits tax, salaries tax, land premiums, stamp duty (a large proportion of which is also property-related), and investment income - all of which are quite volatile.

- We note that, in the 2021/22 Budget Speech, the FS indicated that he had asked for a review the rating system to be undertaken, as the system has not undergone any major change since 1995. It was proposed to: (a) introduce a progressive element to the rating system, (b) provide rates concession to owner-occupied properties on a regular basis, and (c) shift the primary liability for rates payment from the occupier to the owner of a property to reflect that the ultimate responsibility with regard to a property should rest with its owner. In this regard, property rates represent a fairly broad-based form of taxation. We would suggest that the Government provides more detailed information on what it has in mind, as well as the timeline of the review.

- The overall competitiveness of the system needs to be considered, what might be possible and what would not be, in the light of international tax developments, such as those outlined above, and what Hong Kong's positioning should be from a tax perspective in the future. Existing policies and tax incentives also need be monitored and reviewed regularly for their effectiveness in achieving their objectives.

- The Hong Kong tax system is still based largely on legislation introduced in 1947. The last major review was undertaken well over 40 years ago. Since then, and in particular, more recently, in response to changes in the international tax landscape, the IRO has been amended and expanded in reactive manner. A more extensive review of the tax system is needed to bring the framework up to date, take account of new business models (including different forms of e-commerce and online businesses), and ensure that it remains fit for purpose.

- The Government should research into how the tax system could be used to support policy objectives, such as developing Hong Kong's role as an IP hub, and providing more assistance to start-up businesses that cannot make use of the existing incentives. Given the increasing focus on, and importance of, sustainable development, the Government should consider green taxes and incentives (e.g., emission taxes, additional carbon taxes, incentives for energy conservation, etc.). Push and pull measures can be used to increase the take up of electric vehicles ("EVs") and encourage the development of new energy vehicles, including commercial vehicles and public transport, in order to help achieve a carbon neutral Hong Kong by 2050 (see Section IV below).

- More generally, there is a need to provide greater clarity and certainty of tax treatment, which has come to rely too heavily on debatable interpretations of court judgments, and non-statutory interpretations through IRD departmental interpretation and practice notes, and, in some cases, informal administrative arrangements.

- Since it was established, the Budget and Tax Policy Unit formerly known as the Tax Policy Unit, which is located within the Financial Secretary's Office, has conducted research into R&D incentives and other specific projects, but it has not taken up broader, more strategic tax issues at the fiscal policy level that could help support Hong Kong's economic development and competitiveness. Its responsibilities and expertise should be expanded, so that Hong Kong's economic growth can benefit more extensively from the support of appropriate tax policies. This unit could play a leading role in any broader review of the tax system.

We propose, therefore, the following specific measures in relation to reviewing Hong Kong's tax system:

- **A more extensive review of Hong Kong's tax system is called for to examine:**
  - **Options for broader-based taxation**
  - **The overall competitiveness of Hong Kong's system, particularly in the light of recent international developments in taxation.**
  - **Modernization of the framework, to take account of new business models, etc.**
  - **How the tax system could be used to support policy objectives, such as sustainable development and achieving carbon neutrality by 2050.**
  - **How to provide greater clarity and certainty of tax treatment.**
- **Expand the responsibilities and expertise of the Budget and Tax Policy Unit to enable it to play a leading role in any broader review of the tax system**.

III. Community and targeted relief measures

Issue 7: Introduce tax loss carry-backward in profits tax regime

Due to the economic slowdown as a result of the pandemic, businesses in a number of sectors are suffering from cash flow problems. It is important for the Government to help businesses in the most directly affected sectors to cope with their cash flow problems. Allowing tax loss carried backward for the years of assessment ("YAs") 2021/22 and 2022/23 could be an effective means to help such businesses

Temporary tax loss carried backwards is nothing new. Singapore[22] introduced the Loss Carry-back Relief in 2006, allowing taxpayers to carry back the current year unutilized capital allowances and trade losses for one year. The scheme has been enhanced and extended to YA 2021. Businesses may elect to carry back unutilized capital allowances and trade losses from YA 2021 for up to the immediately preceding three years (i.e., YAs 2018, 2019 and 2020).

Similarly, in view of the pandemic, the U.S. Federal Government[23] has allowed businesses to carry back net operating losses arising in 2018, 2019 and 2020, for five years, and has provided cash tax refunds to taxpayers accordingly.

We propose therefore the following specific measure in relation to loss carry back:

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[22] https://www.iras.gov.sg/irashome/Businesses/Companies/Working-out-Corporate-Income-Taxes/Claiming-Reliefs/Loss-Carry-Back-Relief/

[23] https://home.kpmg/cn/en/home/insights/2020/04/tax-alert-4-hk-us-income-tax-relief-in-response-to-coronavirus.html

- **Allow temporary tax loss carried backward for the years of assessment 2021/22 and 2022/23**

Restrictions could be imposed to reduce the impact on the revenue, e.g., cash tax refunds could be subject to a limit per taxpayer.

<u>Issue 8: Measures to help employees</u>

In April 2020, the Institute's president wrote to the secretary for labour and welfare urging a review of the payment limits under the Protection of Wages on Insolvency Fund ("PWIF"), especially the caps on wages in arrears and wages in lieu of notice.

While employees may need to rely on the PWIF for immediate support, the PWIF may not be in position to provide the level of support that is called for in economic downturns, such as the situation faced during the height of the pandemic in Hong Kong. One reason for this is the very low limits on some of the categories of ex-gratia payments that may be made by the PWIF, especially the ceiling on unpaid wages. This, and the ceiling on wages in lieu of notice, have not been increased for over 20 years. Currently, the former stands at a maximum of $36,000, for up to four months wages in arrears, and the latter, at up to $22,500 for one month's wages. Not only are they out of alignment with one another, but they are also out of step with other benchmarks, which, historically, have been used as references for the caps (e.g., the median monthly wage and/ or the proportion of claims that can largely be met by the existing ceilings).

We are pleased to note that, on 27 December 2021, the Commissioner for Labour indicated that the PWIF payment limits will be reviewed and increased in accordance with the median monthly wage, and the inflation of prices, in view that the limits were not adjusted in the past two decades. The underlying legislative procedures should be completed in 2022.

We propose, therefore, the following specific measure in relation to employees made redundant by insolvent employers:

- **Raise the payment limits under the PWIF, especially the caps on wages in arrears and wages in lieu of notice, up to a level that the relevant employees are able to sustain their temporary living in Hong Kong.**

<u>Issue 9: Encourage people to adopt a healthier lifestyle</u>

The Active Healthy Kids 2018 Hong Kong Report Card produced by the Chinese University of Hong Kong gave a D grade[24] for Hong Kong children and young people's physical fitness, showing that Hong Kong children's fitness levels have been declining in recent years. Some experts believe this is partly because of insufficient facilities, or neighbourhood parks, that promote opportunities for active play and outdoor play. No doubt, the popularity of computer games rather than outdoor pursuits has not helped. The situation has been exacerbated

[24] https://activehealthykidshongkong.com.hk/en/report_card/2018/Physical_Fitness.asp

during the Covid pandemic, with more children having to stay at home for their schooling. At the same time the pandemic has offered a chance to rethink Hong Kong's approach to fitness.

While Hong Kong's best-ever performance in the Olympics, in Tokyo, the achievements in the National Games and, even more recently, the first world record in swimming by a Hong Kong athlete, are still fresh in the community's mind, the opportunity should be taken to keep the momentum going and build on the burgeoning interest in sport. Participation in sport and physical recreation is good for numerous reasons, in addition to improvements in health, and should be encouraged. It can be a stress reliever and help to develop sense of positive competition and, particularly for team sports, a sense of camaraderie, mutual support and shared goals.

In order to help develop sport and recreation in Hong Kong at the community level, in addition to the elite level, improve the population's overall health and wellbeing and, so also, in the long term, reduce the burden on the health services, the Government should consider ways to encourage people to adopt a healthier lifestyle.

We note that fitness coaching and sports and management are among the disciplines under the Study Subsidy Scheme for Designated Professions/ Sectors and some courses in related areas are included under the CEF list of reimbursable courses. These should be further promoted and expanded, where appropriate.

We propose therefore the following specific measures in relation to encouraging participation in sport and physical recreation:

- **Allow a tax deduction for expenses incurred on approved sports training courses and activities, including expenses incurred by taxpayers or their dependants. The deduction per taxpayer and his/ her dependants should be capped at HK$12,000 per person**.

- **Introduce tax super deduction of, say, 150%, for sponsorships of approved community sports events activities by enterprises, up to an annual ceiling of HK$100,000.**

- **Incentivize developers (e.g., with Gross Floor Area concessions) to include more recreation and sports facilities in residential and commercial developments (including sports facilities for the disabled).**

- **Promote and, where appropriate, expand the range of courses in sports management, coach-training and community sports organization courses available through government subsidized schemes such as the Study Subsidy Scheme for Designated Professions/ Sectors and CEF list of courses.**

<u>Issue 10: Rationalize personal allowances</u>

The amount of personal allowances under salaries tax and personal assessment have not been revised since 2018/19. The basic personal allowances should be increased at least in line with inflation, as this can help retain more money in consumers' pockets.

The Government should also review and rationalize the allowances for dependants. Allowances for children and other dependants have been revised at various times over the past decade or so, with different levels of increases for each. For example, since 2017/18 while allowances and additional allowances for dependent parents and grandparents have been increased by around 8.7%, allowances for dependent siblings have not been increased at all, while child allowances have been increased by 20%. Pending a review, the allowances for dependants should also be increased in line with inflation.

Post review, any future adjustments should be made on a more transparent and consistent basis. Where there are sound policy, or other, reasons for differential adjustments, these should also be made clear.

We propose therefore the following measures in relation to personal allowances under salaries tax:

- **The Government should review and rationalize personal allowances and allowances for dependants, which, in the past, have been increased by differential amounts for different types of dependants, and which have not been revised at all since 2018/19. Following a review, make future adjustments on a more transparent and consistent basis.**
- **Meanwhile, these allowances should be increased at least in line with inflation to help keep more money in consumers' pockets.**

Issue 11: Targeted relief measures

As the course and pace of economic recovery is still uncertain, the Government should continue to provide targeted relief measures to support businesses and individuals. We suggest considering measures across three areas.

Another round of domestic consumption subsidies

Based on the figures of retail sales released by the Census and Statistics Department, the year-on-year growth in the value of total retail sales picked up notably to 11.9% in August 2021[25]. While this dropped back to 7.8% in September, October showed another substantial gain, of 12%. These figures suggest that, coupled with the stable local Covid situation and improved labour market conditions, the Consumption Voucher Scheme ("CVS"), under which the first batch of vouchers were issued in August and the second in October, has helped boost the local economy, particularly retail sales. However, further research is needed to understand the real impact of the scheme, given that the 2021 figures also represent a comparison from a low base figure from one year ago.

According to the annual Poverty Situation Report[26] released in November, the underlying number of people living below the poverty line increased from 1.49 million to 1.65 million, and the pre-intervention poverty rate climbed to 23.6%, hitting a 12-year high. However, after government policy intervention (taking into account all selected recurrent cash, non-recurrent cash and means-tested in-kind benefits), the report indicates that the overall poverty rate fell by 1.3 percentage points from 2019 to 7.9% in 2020. The number of overall

[25] https://www.info.gov.hk/gia/general/202109/30/P2021093000311.htm
[26] https://www.censtatd.gov.hk/en/data/stat_report/product/B9XX0005/att/B9XX0005E2020AN20E0100.pdf

poor households and the size of the poor population decreased by 45,000 and 88,000 to 0.242 million and 0.554 million, respectively, over the same period. Therefore, the Government's one-off measures to relieve the burden of the grassroots effectively suppressed the surge in the poverty rate that would have otherwise occurred during the economic downturn.

In view of the above, further relief may be needed in the coming year. On the basis that the CVS can generate a multiplier effect on the economy, the Institute considers that the CVS is preferable to, and has been more efficiently administered, than the Cash Payout Scheme implemented in 2020. Therefore, if further stimulus and support is needed in 2022, which seems to be the case with, among other things, the ongoing lack of in-bound tourism in Hong Kong, the Government should consider providing another round of the CVS in 2022. Given the slight improvement in the local economy, albeit not evenly distributed at this stage, we suggest considering a lower amount of, say, HK$3,000 per person.

Continue to waive surcharges for payment of tax by instalments for 2021/22

Since the outbreak of Covid, some business and individual taxpayers have been facing a difficult time and struggling to stay afloat amidst the resulting economic downturn. With in-bound tourism at a fraction of the normal levels, travel restrictions and some limitations on group gatherings still in place, many businesses will still be encountering operational difficulties, including cash flow problems.

We support the IRD's move to allow taxpayers facing financial difficulties to apply for payment of tax by instalments and to waive the surcharge on instalment settlement for YAs 2018/19 to 2020/21. To ease the burden on taxpayers during these times of uneven recovery, we suggest that the Government extend these measures to YA 2021/22.

Support for middle-class households and small businesses

This year, according to the Institute of Human Resource Management, workers received an average salary increase of 1%. Adjusted for inflation, the net pay rise was minus 0.4%. They have projected a 3% pay increase for workers next year[27]. Therefore, depending on the state of the economy at the time of the 2022 Budget Speech, the situation could remain difficult for many middle-class taxpayers and small businesses.

Under the circumstances, we suggest that salaries tax, tax under personal assessment and profits tax for 2021-22 be reduced by 100% subject to a ceiling of HK$20,000 in the coming budget.

The cost of private housing has continued to rise even during the Covid pandemic and it remains unaffordable for many Hong Kong people. On the other hand, the waiting list for public housing is several years long. We have been proposing for a number of years that the Government introduce a home rental deduction, with a similar ceiling as the home loan interest deduction, of up to HK$100,000 per year (for people who are not provided with other housing benefits, such as housing benefits from their employers). This could be introduced on temporary basis to provide relief during the economic downturn arising for

[27] https://news.rthk.hk/rthk/en/component/k2/1615743-20211018.htm

the pandemic, if further study of the longer-term impact were still needed. It could even be considered to be offered on a retrospective basis for more immediate relief.

We propose therefore the following measures in relation to targeted relief:

- **Consider providing another round of the CVS in 2022, at a lower amount than in 2021 of, say, HK$3,000.**
- **Continue to waive surcharges for payment of tax by instalments for 2021/22.**
- **Give a tax reduction of 100%, subject a ceiling of HK$20,000 on salaries tax, tax under personal assessment and profits tax in 2021/22.**
- **Consider introducing a home rental deduction, with a ceiling of HK$100,000 per year, on a temporary basis, initially.**

IV. Environmental measures to achieve carbon neutrality

Issue 12: Promoting the adoption of environmental, social and governance (ESG) and sustainable finance

ESG reporting and practices are becoming an increasingly important focus for businesses and investors. Meanwhile, Hong Kong is also aiming to become a regional hub for sustainable finance. The Government has been actively promoting the development of green and sustainable finance, encouraging institutions to conduct relevant investment, financing and certification activities and attracting top-notch institutions and talent to Hong Kong to provide the relevant services. We welcome the initiatives made by the Government in these areas to boost Hong Kong's competitiveness, including the Green Bond Programme, consolidated Grant Schemes, and the establishment of the Green and Sustainable Finance Cross-Agency Steering Group ("GSFSG"). The Hong Kong Quality Assurance Agency's Green and Sustainable Finance Certification Scheme is also a helpful element in coordinating the efforts of government agencies.

In view of the growing demand for green financing, we note that the FS announced in his 2021-22 Budget a plan to double the original borrowing ceiling of the Government Green Bond Programme to HK$200 billion, allowing for the further issuance of green bonds totalling HK$175.5 billion in the next five financial years[28]. Furthermore, the Government has signed the *Green Bond Pledge*[29], becoming the first signatory in Asia, under which the Government is committed to supporting the growth of a green bond market and to issuing bonds for infrastructure as green bonds, whenever applicable. These are positive moves.

Going forward, we expect there will be further collaboration between the Government and financial institutions to develop more green finance products in addition to green bonds. To maintain the momentum in developing Hong Kong's position as a regional green and sustainable finance hub, the Government should consider a range of additional measures.

In terms of ESG development, the Institute has been actively supporting members to provide ESG assurance to companies that wish to obtain independent assurance for their ESG/ sustainability reports or elements of them. In December 2020, we issued guidance to assist members and other practitioners in performing ESG assurance engagements, in

[28] https://www.hkgb.gov.hk/en/others/documents/Green_Bond_Report_2021.pdf
[29] https://www.greenbondpledge.com/

accordance with Hong Kong Standard on Assurance Engagements ("HKSAE") 3000, which is the benchmark most commonly used by assurers[30]; and we have recently published short study of the status of ESG assurance among December 2020 year-end listed companies in Hong Kong[31].

As noted above, at COP26, the International Financial Reporting Standards Foundation Trustees announced the setting up of the ISSB, to help meet the growing demand from international investors with global investment portfolios who are calling for high-quality, transparent, reliable and comparable reporting by companies on climate and other ESG matters. The Institute will also be working closely with the GSFSG on the implementation of sustainability reporting standards in Hong Kong. We recommend, therefore, that funding be provided to enable the Institute and the profession in Hong Kong to play an active part in the initiative, including to participate actively in international and regional meetings on the development and implementation of relevant standards.

In relation to supporting Hong Kong's position as a regional green and sustainable finance hub, and to further the development of sustainability reporting and assurance in Hong Kong, we propose, therefore, that consideration by given to various specific measures such as:

- **Enhance ESG integration into Hong Kong's role as a regional wealth management hub, such as introducing this element into the Cross-boundary Wealth Management Connect Scheme[32].**
- **Encourage and provide incentives to financial institutions in Hong Kong to integrate sustainability and ESG considerations, as well as the management of climate risks, into their banking and financing products.**
- **Develop and promote policies to support more aggressive renewable energy targets and technologies, including expansion of feed-in tariff arrangements[33], and potentially linking with carbon trading mechanisms (with an initial focus in the GBA).**
- **Carry out extensive advocacy work to raise climate literacy amongst corporates, as well as the community, in Hong Kong, in particular on low-carbon transition pathways, and encourage corporates to seek sustainable financing solutions.**
- **Provide training programmes and certification schemes for ESG and/or sustainable finance professionals.**
- **Develop an over-arching strategic plan incorporating finance, technology, business sectors and the territory's own climate transition so as to provide needed steer.**
- **Regarding the development of international sustainability reporting standards by the ISSB, and ESG assurance, providing funding support for, say, the next five years, to enable the Institute and the Hong Kong profession to participate**

[30] https://www.hkicpa.org.hk/-/media/HKICPA-Website/New-HKICPA/Standards-and-regulation/SSD/03_Our-views/TB_-Cir/Auditing/aatb5_20.pdf
[31] https://www.hkicpa.org.hk/-/media/Document/APD/BCGESGA/2021_ESG_Assurance_Research.pdf
[32] https://www.hkma.gov.hk/eng/key-functions/international-financial-centre/wealth-management-connect/
[33] https://www.gov.hk/en/residents/environment/renewable/feedintariff.htm

actively in international and regional meetings on the development and implementation of standards.

Issue 13: Green taxes and incentives

In the 2020 Policy Address, the CE committed to striving to achieve carbon neutrality by 2050. We are pleased to note that, on 8 October 2021, the Environmental Bureau released Hong Kong's Climate Action Plan 2050 ("CAP")[34], setting out the vision of "Zero-carbon Emissions−Liveable City−Sustainable Development", and outlining the strategies and targets for combating climate change and achieving carbon neutrality, together with certain quantitative targets. Under the CAP, the Government will pursue more vigorous interim decarbonization targets to reduce Hong Kong's carbon emissions by 50% before 2035 as compared to the 2005 level.

Tax can be used as an integral part of the Government's anti-pollution and decarbonization strategy, and to promote sustainability and conservation of resources, and encourage socially conscious behaviour by companies and individuals. With a view to helping to achieve a carbon neutrality by 2050, the Government should explore options, including "green" taxation and incentives for good practices, making reference to examples adopted overseas and based on the "polluter pays" principle, as well as other non-tax measures. In terms of energy and resource conservation, this issue has been thrown into sharper relief with the drought currently been experienced in Guangdong and Shenzhen[35], which serves as a stark warning of, potentially, chronic shortfalls that may affect Hong Kong's main supply of water in the years ahead.

Measures that could be further considered include:

- Emission taxes (e.g., vehicle first registration taxes based on their emissions)
- Tax levies based on polluting inputs
- Credits for emission reductions
- A charge on the producers of plastic beverage containers
- A levy scheme to ban the free provision of disposable plastic tableware[36]
- Incentives for energy and water conservation, and higher charges for usage above a certain thresholds.

The passage of the Waste Disposal (Charging for Municipal Solid Waste) (Amendment) Bill 2018[37] is supported as it is a major step in waste management in Hong Kong. While we understand that the system, which will require residents to buy government-made bags to dispose of their trash, will not be set up for at least 18 months, we suggest that the Government issue further guidelines and promote the waste charging scheme more actively to get citizens prepared. Setting out a concrete implementation timeline will be important to obtaining "buy-in" from the community.

To strengthen the support for waste reduction and recycling at the district level, the Environmental Protection Department has been actively building a new community recycling

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[34] https://www.info.gov.hk/gia/general/202110/08/P2021100800588.htm

[35] https://www.reuters.com/markets/commodities/chinas-southern-megacities-warn-water-shortages-during-east-river-drought-2021-12-09/

[36] https://www.legco.gov.hk/research-publications/english/essentials-2021ise22-measures-to-curb-disposable-plastic-tableware.htm

[37] https://www.news.gov.hk/eng/2021/08/20210826/20210826_130833_725.html

network (i.e., Green@Community[38]) across 18 districts. The recyclables collected are sorted and then delivered to the downstream recyclers for subsequent processing in transforming them into quality recycled materials. While supporting the upstream collection network, the Government should expand the downstream recycling capabilities as well. We suggest that the Government should consider providing incentives to facilitate the development of downstream waste-to-resources/ energy infrastructure. Subsidies on the relevant land cost and facilities could be considered. Integrated waste solutions and facilities, similar to I•PARK[39], which is under construction and will come into operation by 2025, should also be explored.

All types of waste car batteries, including those arising from EVs, are hazardous and must be handled as chemical waste. With the increasing popularity of EVs in recent years, the increase in number of retired EV batteries has become a subject of concern. Since retired EV batteries still have 70% to 80% of their electricity storage capacity, the Government should explore and encourage second-life applications of EV batteries. For example, an initiative was launched in Japan to pair old EV batteries with solar panels to power convenience stores[40].

Introduce an enhanced industrial and commercial building allowances in the tax system for "green" buildings

Sections 16H-K of the IRO allow accelerated tax deductions on certain specified capital expenditure incurred by taxpayers for their environment-friendly initiatives. "Specified capital expenditure" means any capital expenditure incurred on the provision of any environmental protection machinery or environmentally-friendly vehicles; or the construction of any environmental protection installations, where "environmental protection installation" includes 11 types of environmentally-friendly installations, e.g., solar water heating, solar photovoltaic, wind turbine, hydroelectric, etc.

While, in principle, these measures can help develop Hong Kong as a greener city, as Hong Kong is primarily an international financial centre and services economy, not many taxpayers will employ local environmental installations. Hence, the effectiveness of these environmental tax measures is questionable. Meanwhile buildings in Hong Kong constitute the largest source of energy usage. The CAP notes: "Buildings account for about 90% of Hong Kong's total electricity consumption, and over 60% of our carbon emissions is attributable to generating electricity for our buildings"[41]. However, new buildings that are not very energy efficient are still being constructed, while green building codes such as BEAM Plus[42], in Hong Kong, remain voluntary.

In addition to considering mandating key elements of green building codes in new building and incentivizing/ subsidizing retrofitting, where feasible, providing enhanced industrial building and commercial building allowances for new commercial and industrial complexes that adopt approved, environmentally-sustainable, designs could be an effective means to encourage developers to build greener, more energy-efficient buildings. This would help Hong

[38] https://www.wastereduction.gov.hk/en/community/crn_intro.htm
[39] https://www.enb.gov.hk/sites/default/files/pdf/waste_blueprint_2035_eng.pdf
[40] https://www.theverge.com/2019/11/6/20951807/electric-vehicles-battery-recycling
[41] https://www.climateready.gov.hk/files/pdf/CAP2050_booklet_en.pdf (see 2.9, page 13)
[42] https://www.hkgbc.org.hk/eng/beam-plus/beam-plus-new-buildings/index.jsp
Other code adopted quote widely around the world include BREEAM (UK) (https://www.breeam.com/) and LEED (U.S.) (https://www.usgbc.org/leed)

Kong achieve carbon neutrality by 2050 and could also benefit the living and working environment.

At the same time, following the disastrous fire in Grenfell Tower in London in 2017, we would strongly recommend that the Government review the current situation and adopt rigorous standards in relation to the use of building materials in Hong Kong, including supposedly "energy efficient" materials and construction, to ensure that they do not constitute a fire hazard to occupants.

We propose, therefore, the following specific measures in relation to green taxation and incentives:

- **Explore options for "green" taxation based on the "polluter pays" principle, and incentives for good practices and better energy and resource conservation, as well as other non-tax measures.**
- **Introduce enhanced industrial and commercial building allowances for green, energy-efficient buildings (e.g., an initial allowance of 25% and an annual allowance of 5% for industrial buildings and, say, an annual allowance of 6.5% for commercial buildings).**
- **Consider providing incentives to facilitate the development of downstream recycling, waste-to-resources/ energy infrastructure, e.g., subsidies on the relevant land cost and facilities.**
- **Explore and encourage second-life applications of EV batteries.**

Issue 14: Incentives for replacing aged commercial vehicles

To further improve roadside air quality to enhance public health, since 2000, the Government has implemented some key measures including promoting the replacement of diesel taxis and minibuses with liquefied petroleum gas vehicles, gradually tightening the emission requirements of newly registered vehicles, phasing out pre-Euro IV diesel commercial vehicles from 2014 to 2020, as well as launching a scheme, in 2020, to further phase out Euro IV diesel commercial vehicles. At the same time, the Government has retrofitted Euro II and Euro III franchised buses to tighten the air pollutant emission standard to Euro IV[43]. These efforts have seen roadside air quality in Hong Kong improve significantly over the past two decades.

However, while most passenger vehicles in Hong Kong meet the Euro VI standard and there is a policy in place such that, in practice, no new diesel passenger vehicles has been able to be registered in Hong Kong since 2017, commercial vehicles are still mainly diesel or LPG-powered with high-pollutant emissions.

We suggest that the Euro VI emission standard should be adopted for all commercial vehicles as soon as possible. Plans should be made to end the use of Euro V commercial vehicles, following the phasing-out of pre-Euro IV and Euro IV vehicles. In addition to this, electric commercial vehicles should be explored as a method to remove these major emission

[43] https://www.enb.gov.hk/sites/default/files/pdf/EV_roadmap_eng.pdf

contributors from the roads. We also propose that further incentive measures be considered to expedite the complete replacement of polluting commercial vehicles.

We propose, therefore, the following specific measures in relation to incentives for replacing aged commercial vehicles:

- **Adopt the Euro VI emission standard for all commercial vehicles as soon as possible.**
- **Consider further incentive measures to expedite the complete replacement of pre-Euro VI polluting commercial vehicles.**

Issue 15: Electric vehicles

The development and use of green transport has seen something of a boom in recent years. Different jurisdictions around the world have been setting targets to actively promote the adoption of EVs.

The worldwide EV market has taken a huge leap forward in the past decade, as also reflected in the share price of a number of EV manufacturers (e.g., the share price of Tesla has surged more than several thousand percent in the past 10 years). In fact, the technology of electric private cars has become relatively mature and their market supply is increasing quickly, gradually replacing conventional fuel-propelled private cars. The technological development of other types of EVs is also anticipated to catch up with that of electric private cars in the next few years. According to BloombergNEF, within four years, one quarter of new cars bought in the Mainland China and nearly 40% of those purchased in Germany are expected to be electric[44]. Hong Kong also announced the first Roadmap on Popularization of Electric Vehicles in March 2021[45], which sets out strategies for achieving the goal of zero vehicular emissions in the long run and a target of no new registrations of fuel-propelled private cars in 2035 or earlier. While the total registration number of EVs in Hong Kong has increased substantially from 162 in 2010 to 18,361 in 2020, the ratio of public chargers to EVs plunged from 0.30 to 0.18 from 2015 to 2018[46], which is clearly not beneficial to the long-term development of the EV market.

The establishment of a charging network sufficient to support EVs is vital. As mentioned under *Issue 13*, appropriate handling of retired EV batteries should also be considered thoroughly in the course of attaining zero vehicular emissions.

Against this background, we make the further recommendations below.

Extend the EV-charging at Home Subsidy Scheme

The Institute has proposed several times that the infrastructure for EVs needs to be further enhanced and we have suggested that using tax incentives could be one way of encouraging this. Whether incentivized by tax measures or other means, it is important that potential owners of private EVs are not discouraged from replacing their existing fuel-propelled cars with EVs, or from buying an EV as a first car, due to a lack of suitable

[44] https://www.ft.com/content/fb4d1d64-5d90-4e27-b77f-6e221bc02696
[45] Ibid.
[46] https://www.legco.gov.hk/research-publications/english/2021issh26-usage-of-electric-vehicles-in-hong-kong-20210528-e.pdf

infrastructure, including-readily available fast charging stations where they live or in convenient locations.

The Government has launched the $2 billion *EV-charging at Home Subsidy Scheme*[47] to subsidize private building owners to install charging stations in car parks of existing private residential buildings and it was expected that about 60,000 parking spaces in existing private residential buildings would be provided with an EV charging-enabling infrastructure under the scheme. However, we understand that applications are already oversubscribed as the total amount of subsidies reserved for applications received has reached the ceiling of the total funding available. This huge response clearly indicates that the scheme needs to be continued and expanded as matter of priority. In addition, there is feedback that the application process can take as long as 2.5 years. Therefore, we suggest that the Government should expedite the approval process if the scheme is expanded.

Provide incentives to explore option for switching to EVs and new energy vehicles

Greater efforts should also be made to encourage owners of commercial vehicles to switch to EVs and to introduce more public transport that does not run on fossil fuels. Many cities are doing this already and it has been discussed in Hong Kong for a long time. While we understand that, with current battery technology, there is problem for taxis to be converted to EVs, as they may need to run 24/7, other options should be explored, such as the battery swapping system adopted for some EVs in Beijing, and in various other places in the Mainland and elsewhere around the world.

On top of the New Energy Transport Fund[48], which was set up in 2011 to subsidize the transport section, charitable organizations and non-profit-making organizations to try out green innovative transport technologies, the Government should continue to encourage and support public transport operators (including bus and public light bus) to explore and test the application of some green innovative transport technologies, e.g., hydrogen fuel cell EVs. In this regard, the Government should consider setting a timeline for phasing out the reduced rates of duty on diesel that franchised bus companies benefit from.

We propose, therefore, the following specific measures in relation to electric vehicles:

- **The EV-charging at Home Subsidy Scheme should be continued and expanded and the approval process should be expedited.**
- **The Government should continue to encourage and support public transport operators (including bus and public light bus operators) to explore and test the application of green innovative transport technologies, e.g., hydrogen fuel cell EVs.**

[47] https://www.evhomecharging.gov.hk/en/
[48] https://www.epd.gov.hk/epd/english/environmentinhk/air/prob_solutions/new-energy-transport-fund.html

Appendix 1: Proposed changes for salaries tax allowances and deductions[49]

Allowances and deductions	Existing (HK$)	Proposed (HK$)
Allowances[50]:		
- Basic	132,000	134,640
- Married person	264,000	269,280
- Child (annual, each dependant, the 1st to 9th child)	120,000	122,400
- Child (initial, each dependant, the 1st to 9th child)	120,000	122,400
- Dependent brother or sister (each dependant)	37,500	38,250
- Dependent parent/ grandparent (each dependant)		
- aged 60 or above or is eligible to claim an allowance under the Government's disability allowance scheme	50,000	51,000
- aged 55 or above but below 60	25,000	25,500
- Additional dependent parent/ grandparent (each dependant)		
- aged 60 or above or is eligible to claim an allowance under the Government's disability allowance scheme	50,000	51,000
- aged 55 or above but below 60	25,000	25,500
- Single parent	132,000	134,640
- Personal disability	75,000	76,500
- Disabled dependant (each dependant)	75,000	76,500
Deductions, maximum limit:		
- Self-education expenses	100,000 limited to claims by taxpayer	100,000 limited to claims by taxpayer
- Private healthcare insurance premiums	8,000	8,000
- Rental payment for taxpayer's primary residence	-	100,000

[49] The forecast rates of underlying and headline consumer price inflation for 2021 are maintained at 1% and 1.6% respectively.
https://www.hkeconomy.gov.hk/en/situation/development/index.htm
https://www.hkeconomy.gov.hk/en/pdf/21q2_pr.pdf

[50] For illustration purposes, the proposed allowances are increased on the assumption that the benchmark is set at current levels and the inflation rate is 2%.

Appendix 2: Proposed changes in salaries tax allowances and deductions - impact on a typical individual

Example: Single person

This example illustrates the impact of[51]:

- an increase of basic allowance to HK$134,640
- a deduction of rental payment with annual limit of HK$100,000

	Existing (HK$)		Proposed (HK$)		Savings (HK$)	Savings (%)
Income		300,000		300,000		
Allowances/ deductions:						
Basic allowance	132,000		134,640			
Mandatory MPF contribution	18,000		18,000			
Private healthcare insurance	8,000		8,000			
Rental payment	-		100,000			
Total allowances/ deductions		158,000		260,640		
Net chargeable income		142,000		39,360		
Tax payable		8,200		787	7,413	90%

[51] Assumptions are as for Appendix 1.

Appendix 3: Proposed changes in salaries tax allowances and deductions - impact on a typical family

Example: Married person with spouse separately assessed, two children who are not newborns, and living with two dependent parents over 60 years of age throughout the whole year

This example illustrates the impact of[52]:

- an increase of basic allowance to HK$134,650
- an increase in child allowance to HK$122,400
- an increase in dependent parents allowance and additional allowance to HK$51,000

	Existing (HK$)			Proposed (HK$)			Savings (HK$)	Savings (%)
Income			750,000			750,000		
Allowances/ deductions:								
Basic allowance		132,000			134,640			
Child allowance	2 children 120,000 each	240,000		2 children 122,400 each	244,800			
Dependent parent allowance and additional allowance	2 parents 100,000 each	200,000		2 parents 102,000 each	204,000			
Mandatory MPF contribution		18,000			18,000			
Private healthcare insurance	1 taxpayer and 2 children 8,000 each	24,000		1 taxpayer and 2 children 8,000 each	24,000			
Total allowances/ deductions			614,000			625,440		
Net chargeable income			136,000			124,560		
Tax payable			7,600			6,456	1,144	15%

[52] Assumptions are as for Appendix 1.