HKGCC
Hong Kong General Chamber of Commerce
香港總商會 1861

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Helping Business since 1861

12 January 2021

The Honourable Paul Chan Mo-po, GBS, MH, JP
Financial Secretary
25/F, Central Government Offices
2 Tim Mei Avenue, Tamar
Hong Kong

Dear Paul,

I am pleased to submit for your consideration the Hong Kong General Chamber of Commerce's proposals for the Government's forthcoming Budget.

These are unprecedented and trying times for Hong Kong. Amid the sea-change caused by man-made and natural crises, there needs to be a rethink of our approach to rebuilding a Hong Kong that is both flexible and resilient enough to withstand the economic and social demands of 2021 and beyond.

Despite these challenges and uncertainties, Hong Kong possesses a number of strengths and advantages: we have a strong fiscal war chest, unparalleled access to a strong and fast recovering market in China, and are at the centre of a thriving Asia-Pacific economy. As an additional advantage, Asia appears to be faring better and stands a better chance of rebounding quicker from the effects of Covid-19, although the fight to contain the pandemic could drag on.

We are also mindful of the need to ensure that Hong Kong maintains its competitive edge and continues to be a preferred business destination and, to that end, have included recommendations on both near- and long-term measures that the Government should consider to support our economy and protect the welfare of Hong Kong's society as a whole.

We hope that you will find our suggestions to be helpful.

Yours sincerely

Peter Wong
Chairman

Encl.

HKGCC Budget Proposals for 2021-2022

The economic situation in Hong Kong has been characterized by increased uncertainty since the last Budget Address with the Covid crisis wreaking havoc on Hong Kong as we contend with a fourth wave at the time of writing.

As mentioned in our earlier submission to the Chief Executive's 2020 Policy Address, immediate attention must be given to mitigating the devastating effects of the coronavirus. Although there may be light at the end of the tunnel with the roll out of approved vaccines, it appears that we will have to brace ourselves for a further worsening in conditions with the recent resurgence in new cases.

We therefore continue to call for near-term measures similar to those put forward in our submission to last year's Budget. We are also mindful of the need to transform Hong Kong's operating environment into one that is more sustainable and resilient under the "new normal" and have included recommendations below to achieve this goal.

A. <u>Emergency measures</u>

As the number of local cases continue to ebb and flow, businesses are struggling with a protracted period of uncertainty that has witnessed a dramatic and unprecedented shift in the business landscape. Responding to the unknown will be inherently challenging but we suggest that the Government should proactively develop scenarios on how the pandemic might play out in 2021 (and beyond), and to critically review the implications on local businesses so that we are not caught unprepared. In the near term, the rollout of various relief measures under the Anti-Epidemic Fund has provided some respite and we urge the Government to continue with such support programmes to help companies and their employees weather the impact of the coronavirus. To this end, we suggest:

1. **Extending the Employment Support Scheme (ESS) and Distance Business (D-Biz) Programme for another quarter or until an effective vaccine is made available.** This would help alleviate job losses in the case of ESS and facilitate digitization in the case of D-Biz. Continuity with such fiscal support is important, as pointed out in the latest OECD Economic Outlook, especially for many small and medium-sized businesses (SMEs) that are the main drivers of job creation. We understand and share the Government's concern about the need for fiscal prudence but as the OECD states, "*the economic damage would have been even worse without the massive government financial support now in place to help people and companies weather the shock. With very low interest rates expected to continue for some time,* ***exceptional spending can and should continue until the recovery gains momentum***." We also agree with the OECD that "*[p]olicy action should become better targeted to where it is needed most and to strengthen the recovery*." In that regard, we urge the Government to **extend its support measures <u>but in a targeted manner</u> to help SMEs especially those in the food and beverage, travel and tourism, lodging and recreation, and arts and entertainment sectors, which have been severely affected by the pandemic**.

2. **Suspend MPF contributions for three to six months.** This could either be applicable to all employees or limited to those with incomes or MPF contributions below a certain amount. This would be especially helpful to low-income employees in sectors that have borne the brunt of the coronavirus and suffered from substantial cuts to their take-home pay. A temporary holiday on MPF contributions would provide employees and employers with some relief respectively in terms of additional disposal income and cashflow .

3. **Waiving the provisional tax for the 2020/21 assessable period, and expedite tax refunds.** These measures would all help reduce the burden on taxpayers, which would in turn alleviate cashflow difficulties. We suggest drawing up a well-defined timetable for processing such refunds so that these are able to provide meaningful support to taxpayers. As such measures are mainly of an administrative nature, these can be implemented quickly without the need for legislative changes.

4. **Providing a Tax Rebate for the 2019/20 Financial Year.** As mentioned, cashflow is one of the key challenges now facing many firms that are struggling to stay afloat. By providing a rebate, this would throw companies a critical and much-needed lifeline that could mean the difference between remaining in or going out of business.

5. **Reducing profits and salaries tax rate by 1% for a year**. A tax cut would send a strong message to the markets and provide a much-needed boost to confidence even if the duration of such a reduction is only for a limited period. The cost arising from the revenue foregone would be more than offset by the likely benefits arising from the stimulative effects associated with such a measure.

6. **Introducing Loss Carry Back (LCB).** The introduction of LCB is timely as businesses in general are suffering from losses as a result of the effects of COVID-19. We suggest that this be implemented for a finite period during which companies can make LCB claims subject to a cap of between HK$2 million and HK$3 million in losses for the 2019/20 and 2020/21 periods.

B. Forward-looking measures

1. Issue government debt to preserve fiscal strength

A recurring and challenging issue for Hong Kong is its narrow tax base. As consideration is given to identifying new and sustainable sources of income, we suggest that the Government actively consider the issuance of treasury bonds as an alternative means to raising funds. The Financial Secretary's comments earlier this year[1] on issuing infrastructure bonds to pay for new projects is therefore welcomed and supported by the Chamber. In addition to easing the pressure on our fiscal reserves, the issuance of government bonds would also have the added benefit of strengthening Hong Kong's capital markets and our standing as an international financial centre.

[1] https://www.scmp.com/news/hong-kong/hong-kong-economy/article/3080116/coronavirus-hong-kong-finance-chief-rules-out

2. Deepen the long-term Hong Kong Dollar-denominated bond market

As Hong Kong's population ages, the sustainability of the public's financial future has become even more important especially with the current economic challenges. To reduce social dependence on the Government, there must be efforts to deepen the long-term saving and retirement income markets in Hong Kong. Hong Kong insurers are presently unable to provide adequate long-term Hong Kong Dollar denominated savings plans to residents due to the absence of a long-term Hong Kong Dollar bond market. To rectify this, we recommend deepening the long-term Hong Kong Dollar bond market through the (i) issuance of 30-year government debt; and (ii) introduction of fiscal incentives to Hong Kong-domiciled corporations issuing long-term bonds

3. Promote Green Finance

We welcome the measures unveiled by the Chief Executive in her recent Policy Address to enhance Hong Kong's capabilities and performance in achieving carbon neutrality before 2050. We believe that promoting Hong Kong as a leader in green finance is a logical initiative given our standing as an international financial centre, and in view of the growing importance of and attention given to addressing climate change. The Government should also proactively consider expanding the existing green bond programme as an alternative to financing green public projects through its Capital Works Reserve Fund. As mentioned in B1, such an approach would have the added benefit of promoting the growth of the local green bond market. The Chamber is looking into ways and means for Hong Kong to achieve such an objective and will be submitting our recommendations in due course.

4. Strengthen the Tax Policy Unit (TPU)

We continue to call for an upgrade of the TPU as a matter of urgency so that it is better able to achieve its mission of enhancing Hong Kong's tax competitiveness. As mentioned in our previous submissions, a well-resourced and well-staffed TPU should assume the primary responsibility for reviewing and making recommendations on policies of a fiscal nature. Such an approach to the division of labour would allow the Inland Revenue Department to concentrate its efforts on fulfilling its mandate of policy administration.

5. Conduct a Comprehensive Review of Hong Kong's Tax System

The OECD's BEPS 2.0 proposal to tax the digital economy and introduce a global minimum tax could have major implications on Hong Kong's tax system, especially its preferential tax regimes, and multinationals. As such and in the interest of Hong Kong's long-term tax competitiveness and fiscal sustainability, we suggest that the Government take the opportunity to conduct a comprehensive review to modernise our tax code.

6. **Incentivise the establishment of regional headquarters (RHQs)**

Hong Kong continues to provide a world-class and business-friendly environment for home-grown and overseas corporates wishing to access the dynamic markets in the Asia-Pacific region. Although we remain an attractive business destination, we should be mindful of the need to maintain our comparative advantage as a preferred gateway into the burgeoning Mainland market. Given that corporate treasury functions are typically operated through RHQs and there is already a corporate treasury centre regime under which pre-defined activities enjoy a concessionary tax rate of 8.25%, we reiterate our call to extend such a concession to RHQs for the purpose of enhancing Hong Kong's appeal as a centre for business operations.

7. **Expand Hong Kong's network of Comprehensive Double Taxation Agreements (CDTAs)**

We commend the Government for its efforts to actively pursue CDTAs with Hong Kong's trading partners and are pleased to note that there are 45 such agreements as of October 2020 with a further 12 that are under various stages of negotiation. This would be conducive to our recommendation in the foregoing on attracting more RHQs to Hong Kong given the benefits associated with a larger network of CDTAs. We support ongoing endeavours by and look forward to working closely with the Government in this regard.

8. **Conduct a Comprehensive Review of Hong Kong's MPF System and Retirement Policy**

There have been incremental changes made to Hong Kong's MPF system since its launch 20 years ago. Although these are welcomed, more substantive and substantial reforms are needed so that the original intent behind the scheme is to be fulfilled. This is because along with an aging population and increase in life expectancy, there is even greater urgency to address lingering issues such as adequacy of investment returns, and the ability or incentive to contribute more, if the funding of retirement needs is to be met. Efforts should be made to bolster contributions so that Hong Kong's replacement rate, which currently stands at around 40%, is on par with the OECD's average of 60%. The offset mechanism should also be reconsidered as part of such a comprehensive review.

9. **Streamline the Advance Pricing Arrangement (APA) Process**

Hong Kong should streamline the APA application process so that this can be completed within three months, which would be on par with the time taken in Shenzhen. This streamlined APA could then be extended across the GBA to provide certainty to taxpayers and facilitate commercial activities within the region.

10. Mitigate effects of amendments to DIPN 28

The Government's unilateral decision to make substantive changes to DIPN 28 without forewarning and consultation has introduced unwanted and unnecessary uncertainty to the tax environment in Hong Kong. As pointed out by the Chamber's LegCo representative Jeffrey Lam in his letter to the then Secretary for Financial Services and the Treasury, the revocation of a deduction of foreign withholding tax on gross income (including royalties, service, and management fees) would compromise Hong Kong's attractiveness and competitiveness vis-à-vis multinationals and put local taxpayers with overseas operations/investments at a disadvantage. In that regard, we suggest that unilateral tax relief be granted to taxpayers affected by such a revision.

11. Expedite the adoption of Industry 4.0

The pandemic has brought into sharp relief the urgent need to accelerate the adoption of Industry 4.0 in Hong Kong. Although the Government has set up a funding mechanism to encourage the resurgence of new pillar industries, more policy support is needed. This includes reviewing land use to ensure that the regulatory framework can support and sustain those companies considering the establishment of high value-added production lines in Hong Kong as the availability of industrial stock gradually declines. At the same time, the opportunity should also be taken to review dated legislation that could curtail interest in such investments, which would contribute to the diversification of Hong Kong's economic base and create jobs beyond the services sector.

HKGCC Secretariat
12 January 2021