2015/16 Budget Analysis

Comprehensive budget with diverse initiatives but housing measures are fewer than expected

The Financial Secretary for the Hong Kong Special Administrative Region (HKSAR), Mr. John Tsang Chun-wah, delivered the 2015/16 Budget on 25 February 2015.

Against the backdrop of the social conflict in second half of 2014 and the threats of volatile macro-economy, the Financial Secretary announced a range of measures to support the affected sectors, diversify economic development and care for the disadvantaged with a view to rebuilding confidence, as well as reinforcing long-term economic growth.

The better-than-expected surplus of HKD63.8 billion for FY2014/15 is mainly resulted from the increase in stamp duty and profits tax revenue. In view of the huge surplus, more "sweeteners" and tax measures are offered to businesses and individuals as compared to last few years' budgets.

This analysis highlights the key proposals in the 2015/16 Budget for both businesses and individuals, and includes an appendix summarizing the proposed tax changes.

Businesses

The 2015/16 Budget continues to provide tax rebate on profits tax of 75% (up to HKD20,000). We welcome this one-off relief measure which will benefit businesses in general. The Budget also provides measures for various industries to develop Hong Kong's economy in the long-run.

Relieve the burden of affected sectors

In view of the economic damages resulted from the pro-longed political bickering, short-term measures will be provided to support the affected industries (e.g. tourism, catering and transportation) by way of waiving licence fees and other fees. We appreciate the government showing care and support to these businesses.

Diversify economic development

Industry-focused economic development continues to play an important role in the 2015/16 Budget. Instead of focusing in the pillar industries, the Budget also puts emphasis on providing support to small and medium-sized enterprises, start-ups,
social enterprises and cultural and creative industries e.g. fashion, film etc. We applaud the government's vision to encourage and develop diversified businesses so as to release the aspirations of different class of people in the community. We recommend that tax incentives could be introduced to support these businesses in the future.

**Strengthen pillar industries**

Some of the tax-related measures in strengthening the pillar industries are highlighted below:

**Asset management**

The proposal to extend the profits tax exemption for offshore funds to private equity funds was first mentioned in the 2013/14 Budget. Since then, the government has conducted industry-wide consultations on the proposed new law. On 5 January 2015, a legislative proposal on the new law was presented to the Legislative Council Panel on Financial Affairs. In the 2015/16 Budget, the Financial Secretary mentions that a Bill on the new law will be presented to the legislature for deliberations and approval shortly. Meanwhile, the Financial Services Development Council has collected the comments on the legal framework for open-ended fund companies and the government will proceed to formulate the relevant legislative proposals. We are pleased to see progress on these two initiatives and recommend the government and the Legislative Council expedite the implementation of these measures with a view to increasing the competitiveness of Hong Kong's asset management businesses.

**Corporate treasury centre**

In the 2015/16 Budget, the Financial Secretary commits to take steps to provide a more commercial friendly environment for corporate treasury centres in Hong Kong. It aims to attract multinational and Mainland enterprises to manage their global or regional treasury activities in Hong Kong through its stable and sophisticated financial platform. In particular, it is announced that the tax deduction criteria for interest expense will be relaxed for corporate treasury centres and the profits tax for specified treasury activities will be reduced by 50%. The relevant bill will be introduced in the 2015/16 legislative session. Deloitte applauds the initiatives and recommends that the government expedite this process. In particular, the introduction of 50% reduction of profits tax for specified treasury activities may help to avoid the tax dispute on the source of interest income derived from treasury activities. Nonetheless, the definition of specified treasury activities and details of the relevant tax incentives are subject to further clarifications by the government.

**Intellectual Property (IP) hub**

The government continues to promote Hong Kong as a premier intellectual property hub in the region. Currently, tax deduction is allowed for capital expenditure on the purchase of patent, know-how, copyrights, designs and trademarks. The 2015/16 Budget proposes to extend tax deduction for capital expenditure incurred on the purchase of more types of IP rights. Deloitte appreciates this initiative and we also encourage the government to explore options to (i) advance the deduction of capital expenditure for the purchase of copyrights, designs and trademarks; (ii) relax the deduction criteria for research and development (R&D) expenses; and (iii) provide super deductions for certain expenditure (e.g. R&D expenses) for companies with trademarks registered in Hong Kong.

**Individuals**

**Housing problem**

The housing problem and the overheated property market continue to be challenges for Hong Kong. A series of stamp duty measures (including Buyer’s Stamp Duty (BSD), Double ad valorem Stamp Duty (DSD) and Special Stamp Duty (SSD)) were introduced in an effort to curb property market speculation over the last few years. However, housing prices did not drop but continued to surge since April last year. As a result, there was an unexpected increase in DSD revenue, which was not the government's intention.

In view of the surging housing prices and the expected rise of interest rate in the United States, the government exerts more effort in increasing the housing supply instead. Deloitte is delighted that the government will inject HKD 27.5 billion fiscal reserves into the Housing Reserve. The adoption of a supply-led strategy is hoped to rectify the imbalance between supply and demand in the long run. While the Financial Secretary emphasizes that the government will closely monitor market conditions and will not hesitate to introduce special measures whenever necessary, no immediate measures are introduced to ease the public’s financial burden on housing. We suggest the government provide short-term tax reliefs e.g. deduction of stamp duty for property used as a principal residence and refund of stamp duty where the property has been occupied for at least three years.
Working class

The Financial Secretary introduced a number of one-off relief measures to ease the financial pressure on the working class:

- Salaries tax and tax under personal assessment rebate of 75% (up to HKD 20,000) for final 2014/15 tax payable
- An increase in child allowance from HKD 70,000 to HKD 100,000
- A rate waiver for the first two quarters, subject to a cap of HKD 2,500 per quarter, for each rateable property

The government anticipates that the working population will decline from the year 2018. To maintain the economic growth, various measures are proposed to encourage more people (e.g. women, older persons, people with family commitments etc.) to join or re-join the workforce. Deloitte welcomes the government's vision in exploring the effective use of manpower. We suggest the introduction of an allowance for working couples (e.g. an allowance for a family where both spouses are employed) in order to encourage married women to re-join the work force.

Youth

The Financial Secretary proposes various measures to assist young people in terms of education and career development e.g. training, internship and exchange opportunities etc. Deloitte welcomes these measures as they demonstrate the government's commitment to develop our young people so as to establish the foundation of our future workforce.

Elderly

To relieve the significant demand on public elderly healthcare services and to reinforce the retirement protection, the government would set aside HKD 50 billion to support the healthcare reform and another HKD 50 billion on retirement protection for the elderly.

The Budget also contains short-term measures in providing an extra allowance to Comprehensive Social Security Assistance recipients, Old Age Allowance, Old Age Living Allowance and Disability Allowance recipients that equals to two month of the standard rate payments and allowances. We appreciate the government's care to the elderly.

Issuing iBonds

Similar to prior years, in view of the uncertainty of global financial market and to promote the retail bond market, the government will continue to issue inflation-linked retail bonds (iBonds) in the coming year to Hong Kong residents.

Tax policy

Automatic Exchange of Information (AEoI)

The Hong Kong government has committed to the global effort, in particular, the initiative of the Organisation for Economic Co-operation and Development in combating cross-border tax evasion arrangements. Under the AEoI regime, financial institutions will be required to regularly report to the Inland Revenue Department on specified financial account information which will be exchanged with other jurisdictions. The relevant amendment bill for the AEoI regime will be introduced in 2016 so that the tax information can be exchanged in 2018.

Broadening tax base

The Financial Secretary explains in the 2015/16 Budget the need to broaden tax base in the long-run. In 2006, the government conducted an extensive consultation on the introduction of Goods and Services Tax (GST) which was not launched in the end. The Financial Secretary mentioned that the government may revisit this topic in future to broaden the tax base in the long run.

Other suggestions

Given the current substantial fiscal reserves of the government, Deloitte recommends that the government consider lowering the corporate tax rate by the following alternative methods to enhance Hong Kong’s competitiveness over neighbouring countries and regions in order to attract further foreign investment:

1. Lowering the flat corporate tax rate from 16.5% to 15.5%;
2. Introducing a two-tiered taxation system – for example, taxing the first HKD 2 million of assessable profits at 12% and the remaining at the current profits tax rate of 16.5%; or
3. Introducing a corporate allowance – for example, the first HKD 200,000 of assessable profits is exempt from tax and the remaining at the current profits tax rate of 16.5%.
Currently, certain tax incentives are available to specific business activities e.g. re-insurance, captive insurance, offshore funds etc. While we welcome the government’s proposed tax concession for corporate treasury activities as mentioned above, we suggest more similar tax concessions can be provided to the encouraged business activities e.g. regional headquarters, global trading etc.

Conclusion

The 2015/16 Budget is a comprehensive one with diverse initiatives addressing the needs of different people in the community. While the Budget focuses on long-term economic development policy, it takes a thoughtful approach by controlling unnecessary expenditure with a view to saving for the future and catering for the anticipated structural deficit in ten years. There are initiatives for wide range of industries and several important measures are proposed to prepare for the future job market, elderly and healthcare issues. However, we hope the government would consider more immediate measures to ease people’s financial burden on housing.

Overall, Deloitte supports the government’s vision to preserve surplus funds for medium to long-term policies. We look forward to seeing the government implementing the proposed measures to achieve sustainable economic growth.
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