

SYNOPSIS OF HONG KONG 2006/07 BUDGET

A. FOREWORD

The Financial Secretary, the Hon. Henry Tang, delivers his third Budget of the Hong Kong SAR for the fiscal year 2006/07 (i.e. from 1st April 2006 to 31st March 2007) this morning. “Recovery, Enhancement, Commitment and Sharing” are the four themes of this Budget.

Due to the rapid growth of the economy and the Government’s effort to rein its expenditure, the Government will restore its fiscal balance, three years ahead of schedule, in both the operating and consolidated accounts for the first time in past eight years. Mr. Tang estimates that the Government will record HK\$5.8 billion operating surplus and HK\$4.1 billion consolidated surplus in this fiscal year (i.e. from 1st April 2005 to 31st March 2006).

Although the financial condition of the Government has been improved, the problem of narrow tax base is yet to be resolved. Having observed the principle of affordability and preserving our tax base, Mr. Tang proposes to lower the marginal salaries tax rates and extend the time limit of claiming home loan interest deduction by three years to a total of ten years. The tax rates of profits tax, charge rate of rates and other taxes will remain unchanged. The Government will launch the public consultation for implementation of Goods and Services Tax (“GST”) in the middle of 2006. The consultation period will last about 9 months and it is estimated that it will take about three years from making a decision to introduce GST to its actual implementation.

Mr. Tang states that, while formulating our economic development and fiscal policies, we should be alert to future challenges and address them with the best interests of our community at heart. The short-term challenges to be faced by Hong Kong include the avian influenza epidemic and volatility in the global financial markets; while in the long term, the challenges include environment pollution, ageing population, mismatch of labor skill, economic restructuring, constant upgrade of quality of our human resources, increase in our productivity and competitiveness etc.

In view of the above, the fiscal targets of the Government over the next few years are to keep the accounts in balance and the share of public expenditure in GDP at 20% or below. Mr. Tang estimates that total government expenditure for coming fiscal year will be HK\$245.6 billion. Expenditure on education, social welfare, health and security will account for over 60% of this. The Government promises that they will make available all necessary resources to cope with the possible outbreak of infectious disease.

The Government estimates that by 31st March 2007, the fiscal reserves should stand at HK\$306.4 billion (approximately equivalent to 16 months of government expenditure). The consolidated account and operating accounts should record a surplus of HK\$5.6 billion and HK\$0.6 billion respectively, which is not too optimistic. Mr. Tang states that Hong Kong is still facing with many challenges in the future. Under the principal of “Prudent Management of Public Finances”, the Government should not rush into deciding on substantial tax reductions. Moreover, despite the economy has been recovered, it is still very fragile. Therefore, he will not, for the sake of winning short-term applause, turn surplus to deficit. He opines that the proposed tax concession measures can mitigate taxpayers’ burden, especially for the middle-class family.

We are pleased to summarize Mr. Tang’s proposed revenue-raising measures for the year 2006/07 in this special newsletter. Some of his proposals may be revised by the Legislative Council before enactment and may even be dropped. We hope that this newsletter will give you some insights to plan for the future. Nevertheless, it should not be taken as professional advice and you are always welcome to contact us for further information and explanation.

PKF
22nd February 2006

B. PROPOSED CHANGES IN GOVERNMENT REVENUE AND CHARGES

1. TAXATION

Salaries Tax

- Propose to lower the marginal rates of the second, the third and the top tax bands by 1%, that is, from the existing levels of 8%, 14% and 20% to 7%, 13% and 19%.

Profits Tax

- Propose no change in tax rate.

Property Tax and Stamp Duty

- Propose no change in tax rates.

Green Tax

- Propose to impose “green” taxes in accordance with the polluter pays principle; and to implement product responsibility schemes to promote recovery and recycling of tyres and to reduce the use of plastic bags.

Goods and Services Tax (GST)

- Launch the public consultation, which will last about 9 months, in the middle of this year. The Government estimates that it will take about 3 years from making a decision to introduce GST to its actual implementation.

2. TAX CONCESSIONS

Home Loan Interest Deduction

- Extend the time limit of applying for home loan interest deduction by 3 years to a total of 10 years but the maximum annual deduction of HK\$100,000 remains unchanged.

Rates

- Propose no change on the charging rate (i.e. 5% of the estimated annual rental value of a property at a designated valuation reference date, assuming that the property was then vacant and to let).

First Registration Tax of Electric Vehicles

- Extend the tax exemption period for a further 3 years.

C. MAJOR TAX RATES FOR THE YEARS 2005/06 AND 2006/07

1. Salaries Tax

Personal tax allowances and deductions:

	2005/06	2006/07
	HK\$	HK\$
Basic allowances:		
Single person's allowance	100,000	100,000
Married person's allowance	200,000	200,000
Additional allowances:		
Child (each)	40,000	40,000
Dependent parent / grandparent:		
a. Aged 55 to 59		
- Basic	15,000	15,000
- Additional ¹	15,000	15,000
b. Aged 60 or above		
- Basic	30,000	30,000
- Additional ¹	30,000	30,000
Dependent brother / sister ²	30,000	30,000
Single parent	100,000	100,000
Disabled dependent	60,000	60,000
Additional deductions:		
Self-education expenses ³	40,000	40,000
Home loan interest	100,000	100,000
Elderly residential care expenses	60,000	60,000
Contributions to retirement schemes	12,000	12,000
Notes:		
1. For dependent living with taxpayer for a continuous period of not less than 6 months.		
2. For whom no child allowance is being claimed.		
3. The maximum amount that can be claimed as deductible expense for training courses attended at approved institutions.		

Standard salaries tax rates:

	<u>2005/06</u>	<u>2006/07</u>
Standard tax rates	16%	16%

Progressive salaries tax rates:

<u>Net Chargeable Income</u>		<u>2005/06</u>	<u>2006/07</u>
First	HK\$30,000	2%	2%
Next	HK\$30,000	8%	7%
Next	HK\$30,000	14%	13%
Remainder		20%	19%

2. Profits Tax

<u>Business Category</u>	<u>2005/06</u>	<u>2006/07</u>
Unincorporated Business	16%	16%
Corporation	17.5%	17.5%

3. Property Tax

<u>Taxpayer</u>	<u>2005/06</u>	<u>2006/07</u>
Property Owner	16%	16%

4. Stamp Duty**Shares transactions:**

<u>Particular</u>	<u>2005/06</u>	<u>2006/07</u>
Including shares, marketable securities, warrants and options registered in HK	0.200%	0.200%

Property transactions:

Sales Consideration	2005/06 & 2006/07
Up to HK\$1,000,000	HK\$100
HK\$1,000,001 to HK\$1,080,000	HK\$100 + 10% of excess over HK\$1M
HK\$1,800,001 to HK\$2,000,000	0.75%
HK\$2,000,001 to HK\$2,176,470	HK\$15,000 + 10% of excess over HK\$2M
HK\$2,176,471 to HK\$3,000,000	1.5%
HK\$3,000,001 to HK\$3,290,320	HK\$45,000 + 10% of excess over HK\$3M
HK\$3,290,321 to HK\$4,000,000	2.25%
HK\$4,000,001 to HK\$4,428,570	HK\$90,000 + 10% of excess over HK\$4M
HK\$4,428,571 to HK\$6,000,000	3.00%
HK\$6,000,001 to HK\$6,720,000	HK\$180,000 + 10% of excess over HK\$6M
HK\$6,720,001 or above	3.75%

Leases:

Leasing period	2005/06	2006/07
Not defined or is uncertain	0.25%	0.25%
Specified in the lease as not exceeding 1 year	0.25%	0.25%
Exceeding 1 year but not exceeding 3 years	0.50%	0.50%
Exceeding 3 years	1.00%	1.00%

5. Estate Duty

Principal Value of the Estate		2005/06 *	2006/07
Over HK\$	Not Over HK\$		
-	7,500,000	-	-
7,500,000	9,000,000	5%	-
9,000,000	10,500,000	10%	-
10,500,000	-	15%	-

Note: The Government abolished the Estate Duty with effect from 11-02-2006 pursuant to the Revenue (Abolition of Estate Duty) Ordinance 2005. For persons who died on or after 15-07-2005 and before 11-02-2006 with the principal value exceeding HK\$7.5 million, the estate duty chargeable will be a nominal amount of HK\$100 only.