



**THE 2011-12 BUDGET**

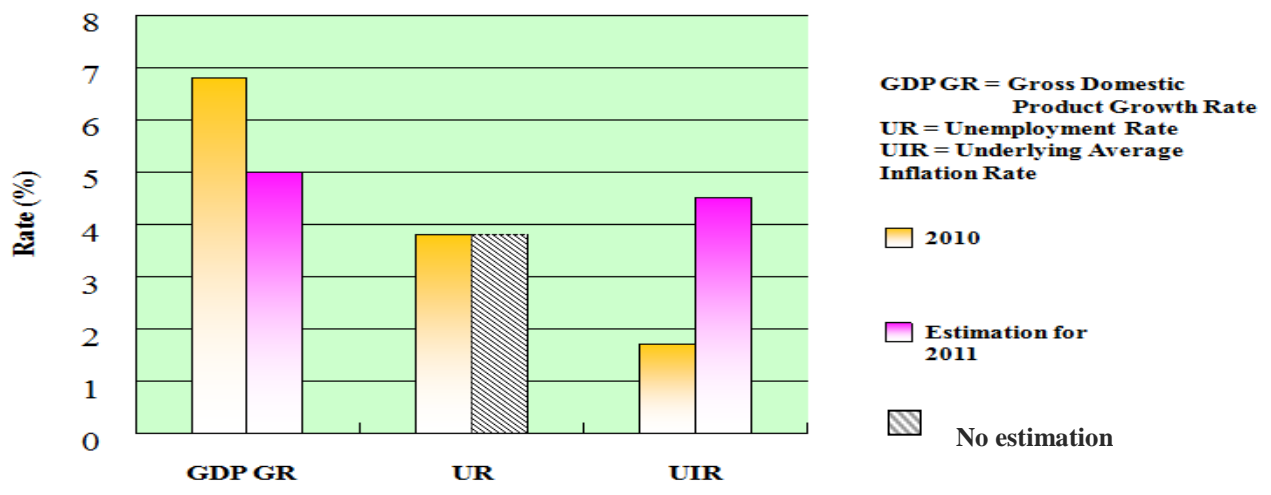
*The Financial Secretary, Mr. John Tsang, delivered the 2011-12 Budget Speech at the Legislative Council on 23 February 2011.*

*In this Tax Flash, we set out a summary of the following items:-*

- *Economic Performance and Outlook*
- *Financial Highlight*
- *Relief and Measures*
- *Policies to Risk of Asset-Price Bubble*
- *Strategy of Fighting Inflation*
- *iBond*
- *Enhancing Business Environment*
- *Our Commentary*

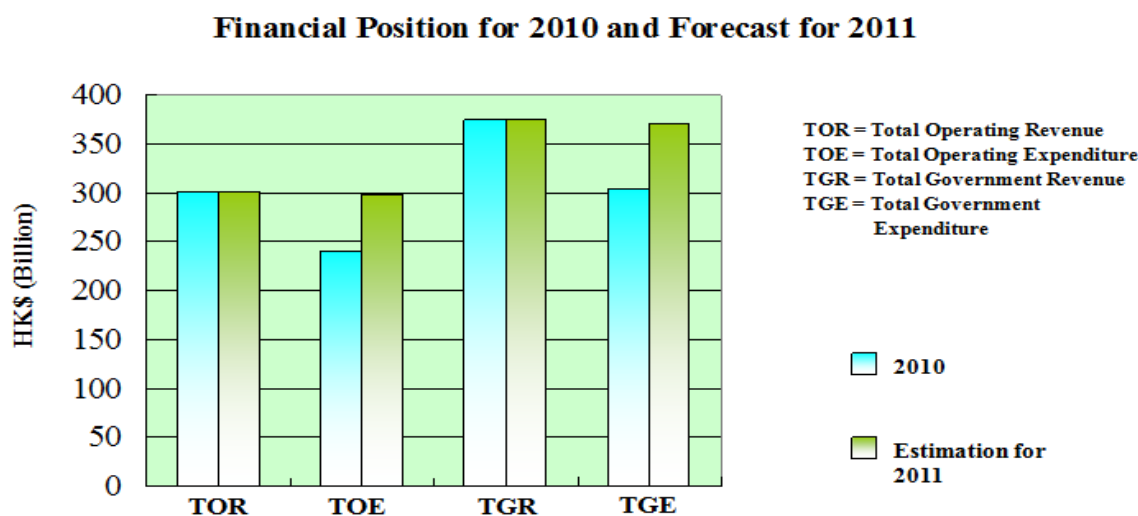
**1. Economic Performance and Outlook**

**Economic Performance for 2010 and Outlook for 2011**



- ♦ GDP grew by 6.8% in 2010. GDP growth rate of 4-5% is forecasted in 2011.
- ♦ Unemployment rate dropped to 3.8% recently. As the unemployment rate has already fallen back to a relatively low level, there will be limited room for further significant decline. The implementation of statutory minimum wage may affect the unemployment rate in 2011.
- ♦ The underlying inflation rate was 1.7% after netting out the effects of the Government's one-off relief measures in 2010. 4.5% is forecasted for 2011.

## 2. Financial Highlight



- ♦ For the current financial position, a surplus of HK\$60.7 billion in the Operating Account and a surplus of HK\$71.3 billion in the Consolidated Account are forecasted for 2010/11. By March 2011, the Hong Kong's fiscal reserves will have increased to HK\$591.6 billion. This is likely to be a conservative figure.
- ♦ A surplus of HK\$3.6 billion in the Operating Account; a surplus of HK\$0.27 billion in the Capital Account.; and a surplus of HK\$3.9 billion in the Consolidated Account are forecasted for 2011/12.

## 3. Relief and Measures

### ➤ *Salaries tax and allowances*

- ♦ Dependent parent / grandparent allowances

	<b>Allowance (not living together with the taxpayer)</b>	<b>Allowances (living together with taxpayer)</b>
<b>Aged 55 – 59</b>	HK\$18,000 (increase from the current amount of HK\$15,000)	HK\$36,000 (increase from the current amount of HK\$30,000)
<b>Aged 60 or above</b>	HK\$36,000 (increase from the current amount of HK\$30,000)	HK\$72,000 (increase from the current amount of HK\$60,000)

- ♦ Child allowances

Raising both the child allowance and the additional one-off child allowance in the year of birth by 20% from HK\$50,000 to HK\$60,000 for each child.

- ◆ Elderly residential care expenses  
The deduction ceiling for elderly residential care expenses will be raised from the current HK\$60,000 to HK\$72,000.
- *Mandatory Provident Fund (“MPF”)*  
Making a one-off injection of HK\$6,000 into the MPF accounts of all MPF scheme members and members of occupational retirement schemes covered by the Employment Ordinance of Hong Kong as of 23 February 2011.
- *Residential electricity subsidy*  
Granting each residential electricity account a one-off subsidy of HK\$1,800.
- *Rate*  
Waiving rates for 2010-11, subject to a ceiling of HK\$1,500 per quarter for each rateable property.
- *Rent for public housing tenants*  
Paying two months' rent for public housing tenants. For non-elderly tenants of the Hong Kong Housing Society's Group B estates, the Government will pay two-thirds of their rent for two months.
- *Miscellaneous*
  - ◆ Providing a one month extra allowance to Comprehensive Social Security Assistance, Old Age Allowance and Disability Allowance recipients.
  - ◆ Increasing the rate of each tax band for the First Registration Tax for private cars by about 15%.
  - ◆ Increasing the duty on cigarettes by HK\$0.5 per stick or 41.5%. Duties on other tobacco products will also be increased by the same %. This will increase the price of a 20 cigarettes pack to approximately HK\$49.
  - ◆ Supporting students from low-income families, more students will be granted full assistance. Each post-secondary student receiving full assistance will be entitled to an additional grant of HK\$1,000 every year.
  - ◆ Injecting HK\$250 million into the HKSAR Government Scholarship Fund to extend the benefits to students of publicly-funded sub-degree programmes.
  - ◆ Allocating HK\$100 million to launch a five-year pilot scheme to subsidise on a matching basis, local tertiary students participating in short-term internship or learning programmes in the Mainland, including visits, exchanges or voluntary services. Participants will be able to learn about the prevailing social, economic and cultural landscapes of our country through these programmes. Each student may receive a subsidy of up to HK\$3,000 per person.

#### **4. Policies to Risk of Asset-Price Bubble**

##### **➤ Residential Flats**

To ensure a healthy and stable development of the property market, the Government will implement measures in the following areas:

##### *1. Land sales arrangements*

The government would introduce government-initiated land sale arrangements, which include:

- ♦ specifying in the Application List four residential sites for government-initiated sale by open auction or tender this year; and
- ♦ putting up for sale by tender five residential sites in addition to those sites on the Application List; and restricting in the sale conditions their use for construction of about 3,000 small and medium-sized flats in total.

In response to the Government request, the West Rail Property Development Limited has redesigned six property developments above MTR stations along the West Rail in respect of which master layout plans and building plans have been approved. This will increase the supply of small and medium-sized flats.

##### *2. Supply of public housing*

Relevant government departments will identify public rental housing (PRH) sites to maintain the average waiting time for general PRH applicants at around three years. In the five-year period starting from 2010-11, the forecast construction of new PRH flats is about 75,000 flats. The new PRH flat construction forecast for 2011-12 and 2012-13 will be some 11,200 flats and 16,700 flats respectively.

##### *3. My home purchase plan*

The Government and the Hong Kong Housing Society (HKHS) will launch the My Home Purchase Plan for eligible applicants. The Government has already earmarked sites in Tsing Yi, Diamond Hill, Sha Tin, Tai Po, Tuen Mun and other areas for a total of some 5,000 flats to be built under the Plan.

##### *4. Increasing land supply*

The Government will continue to increase land supply. Two possible ways are reclamation on an appropriate scale outside Victoria Harbour and rock cavern development.

## ➤ **Commercial Buildings**

To enhance Hong Kong competitiveness, a steady and adequate supply of Grade A offices, and development of new high-grade office clusters should be maintained. The Government will increase the office supply in Wong Chuk Hang and West Kowloon in the next five years and will revitalize industrial buildings in Kwun Tong and Kowloon Bay.

## **5. Inflation**

Fighting inflation is a major task in 2011. The Government has proposed the following strategies:-

- ◆ The Government will strive to ease the domestically generated price pressure by forestalling property market exuberance, preventing excessive credit growth and pursuing a prudent fiscal policy.
- ◆ The Government will continue to diversify the sources of our food imports to countries surging food prices.
- ◆ The Government will keep enhancing our productivity to alleviate the inflationary pressure.
- ◆ The Government will continue to invest heavily in infrastructure, thus increasing the capacity and efficiency of our overall economy. These efforts will not only promote economic development and provide job opportunities, but also reduce the risk of hyperinflation in the medium to long term.

## **6. iBond**

The Government Bond Programme was introduced in 2009 in order to promote the development of the local bond market. The Programme comprises two parts, one on issuing bonds to institutional investors and the other to retail investors.

In order to enhance retail investors' understanding of the bond market and increase their interests in bond investment, HK\$5 billion to HK\$10 billion worth of Hong Kong-dollar inflation-linked retail bonds, or "iBond" with a maturity of three years to Hong Kong residents will be issued. Interest will be paid to bond holders once every six months at a rate linked to the inflation of the previous half-year period. This will help to reduce the impact of inflation on Hong Kong people.

## **7. Enhancing Business Environment**

In order to enhance Hong Kong business environment, the Government are committed to maintaining our competitive edge through continuous investment in new infrastructure. They will also strive to create a more favourable business environment through improving working procedures and reducing compliance costs.

➤ *Headquarters economy*

- ◆ Stepping up promotion efforts and taking the initiative in approaching overseas enterprises in order to encourage overseas enterprises to set up business in Hong Kong.
- ◆ Providing aftercare services and support to foreign companies already established in Hong Kong.

➤ *Support for Small and Medium Enterprises (SMEs)*

- ◆ Increasing total guarantee commitment under the SME Loan Guarantee Scheme substantially from HK\$20 billion to HK\$30 billion.

➤ *Development into a global financial centre*

- ◆ Fostering further development of offshore RMB business, consolidating our position as a platform to raise international capital and enhance the competitiveness of our asset management industry.
- ◆ Maintaining close contact with relevant Mainland authorities as well as the financial regulators and market participants of both sides to further develop Hong Kong's RMB bond market.
- ◆ Encouraging overseas enterprises to issue RMB bonds in Hong Kong, soliciting more Mainland enterprises to issue bonds in Hong Kong and expanding channels for enterprises to invest in the Mainland the RMB capital raised in Hong Kong.
- ◆ Improving our listing platform to attract more enterprises from different places to list in Hong Kong.
- ◆ Maintaining a high standard of regulations. The Stock Exchange of Hong Kong will continue to streamline the listing process for overseas companies to shorten the timetable and lower the costs.
- ◆ Studying ways to further facilitate secondary listing of overseas companies in Hong Kong, and accept companies incorporated in other jurisdictions (such as India and South Africa) to apply for listing in Hong Kong.
- ◆ Seeking to enter into agreements on the avoidance of double taxation with more trading and investment partners so as to foster the growth of asset management business continuously.
- ◆ Developing an Islamic financial platform in Hong Kong to diversify our financial markets continuously.

## **Our Commentary**

We are pleased to see that the Financial Secretary announced a number of stimulus measures which focuses on improving people's livelihood, stabilizing the property market, combating inflation, investing in infrastructure, etc.

The Financial Secretary touched on the area of how Hong Kong's competitiveness can be enhanced. He mentioned about the proposed increase of office supply in Wong Chuk Hang and West Kowloon. On the other hand, the Government will step up promotion efforts and taking the initiative in approaching overseas enterprises to encourage them to set up in Hong Kong their Asia Pacific headquarters.

While these relief measures may address the expectations of the needy to a certain extent, the expectations of the middle class and business sector are not as well matched. More specific and long-term initiatives on how to enhance Hong Kong's business environment and development should be covered in the Budget.

As tax practitioners, we are quite disappointed with the Budget which failed to address, despite repeated calls from various business associations and professional bodies, the following:

- i) The granting of depreciation allowances for plant and machinery of Hong Kong taxpayers used in the PRC under an import processing arrangement.
- ii) The granting of tax deduction on capital expenditure on registered trademark, copyrights and registered designs.
- ii) The offering of tax incentives for setting up headquarters or fund management company in Hong Kong.
- iii) The granting of more generous deduction regime (super deductions) on research and development expenditure.
- iv) Increase the tax band of the salaries tax.

As tax consideration plays an important role in business decision-making, the above suggestions would help to increase Hong Kong's competitiveness and create more opportunities for business development and personal enjoyment in Hong Kong.

The Financial Secretary commented that "economy has fully recovered". We understand that the Government should manage the public finance prudently. However, in view of the significant increase in government revenues with fiscal reserves over HK\$590 billion, the Financial Secretary should introduce more measures to relieve the burden on the middle class and business sector so that the entire community can share the prosperity of Hong Kong economy. We hope the above tax measures will be addressed by the Financial Secretary in next Budget.

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