FEATURED PERSPECTIVES

Asian Tax Review

Hong Kong — A Touch of Grey

by Laurence E. Lipsher

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This is my tribute tax essay, in which I pay homage to my all-time favorite band, the Grateful Dead (with whom I first boogied in Palo Alto, Calif., at a party in 1967), and to the first — and only — Dead single that made it to number one on the charts. This section is also about me and my in-need-of-a-cut mane, which is starting to turn more white than grey. Oh, and it also deals with Hong Kong and the ''grey list.''

A remarkable piece of spin appeared in the January 7 *South China Morning Post*, which reported the January 6 passage of a bill by Legco, the Legislative Council of Hong Kong, giving Hong Kong's tax authorities more power to gather information on suspected tax evaders and send the data to tax authorities abroad — with strings attached.

I quote the following from the article:

> The City's tax rules fell under the international spotlight during the Group of 20 meeting in London in April last year, which endorsed an internationally agreed tax standard drawn upon by the Organization for Economic Cooperation and Development (OECD). Hong Kong narrowly avoided appearing on an OECD blacklist at the summit. Hong Kong and Macao were mentioned in a footnote as territories that had committed to implement the internationally agreed tax standard.

So what's the spin? Well, my friends, if Hong Kong has narrowly avoided the blacklist but is footnoted and is still not on the OECD white list because it does not have at least 12 tax information exchange agreements and has only five TIEAs included within the double tax avoidance agreements (DTAAs) it has signed with Belgium, Thailand, the P.R.C., Luxembourg, and Vietnam, then what you have is part blacklist, which it is off, and part white list, which it is not yet on. White mixed with black makes grey, any way you look at it. And that's what most of the world is calling it — except Hong Kong.

TIEAs, bureaucracy-to-bureaucracy exchanges bypassing the time-consuming processes involved in DTAAs, are accepted by Hong Kong only as part of DTAAs. Further evidence of Hong Kong's ability to maintain its taxpayer-friendly status is the Russian aluminum giant Rusal's initial public offering on the Hong Kong Stock Exchange and the recent announcement that British Virgin Island entities can now list on that exchange.

Don't get me wrong — I like the concept of tax havens. Both Hong Kong and Singapore still remain tax havens, even though they don't want to be called such.

Continuing my tribute to the Grateful Dead and the color of my hair, I will now touch on the Mandatory Provident Fund (MPF), Hong Kong's equivalent of a social security tax, meant to help taxpayers in their grey-headed years. A December 15, 2009, commentary in the *South China Morning Post* questioned whether,

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after its nine years of existence, the MPF has proven to be a success as a retirement fund tax. My answer is a resounding no.

The MPF covers 98.7 percent of the Hong Kong workforce, but only 14 percent of its contributors make voluntary contributions; the rest, myself included, simply meet the minimum requirements. Why?

- The maximum mandatory contribution has remained HKD 24,000 per year. This is approximately US $3,000 per year, half of which must come from the employee, with the other half being paid by the employer.
- The choices available to us, the contributors and ultimate recipients, are far too limited and completely unappealing.
- The employer chooses the investment to which the employee may contribute. This is being changed, but because of the recession, other items are of higher priority for the government at the moment.
- Perhaps most importantly, there is no tax incentive to encourage anyone to make a voluntary contribution.

I have made more money at the race track than through my MPF — and I don't consider myself a gambler. Now, if there were a tax incentive available, perhaps I would reconsider further funding my Hong Kong retirement account.

But to quote the Dead:

Whistle through your teeth and spit, cuz

It's all right

Oh well, a touch of grey

Kinda suits [me] anyway

And that was all I had to say, and

It's all right

I will get by

I will get by

I will get by

I will survive.

Author Larry Lipsher shows off his "touch of grey" and his Grateful Dead attire in front of the statue of Chinese revolutionary Liang Qi Cao at Zhongshan University in Guangzhou, P.R.C.

Budgetary Tax Proposals

The Hong Kong 2010-2011 budget presentation is scheduled for February 24.

In the January 19 edition of Hong Kong's *Standard*, the Hong Kong Institute of Certified Public Accountants (HKICPA) Taxation Committee called for reducing the corporate tax by half a percentage point to 16 percent and gradually moving toward a 15 percent corporate tax rate to stay ahead of its perceived rival, Singapore, in the race to be the lowest-tax jurisdiction in Asia.

HKICPA Taxation Committee Vice Chair Florence Chan said the half percentage point corporate tax rate reduction would only amount to a HKD 2.2 billion decrease in revenue. Presumably, that would be more than made up through stamp tax revenue coming from the housing market, with mainland investors now investing in middle-income housing in addition to luxury housing.

The HKICPA also called for salary tax allowances for dependents to be increased by 20 percent to ease the inflationary burden on middle-income taxpayers. Chan estimated that this year's budget deficit will be less than HKD 20 billion, half of official estimates, because of land sales and stamp tax revenue.

I would guess that this year's deficit will be even less because of the mainland funds pouring into the Hong Kong Special Administrative Region. I would not be surprised if there's a budget surplus at the end of the fiscal year.

A Touch of India

Not to be outdone by other jurisdictions that are outraged by tax avoidance and tax evasion, the Indian government dropped a bombshell when it announced on December 7, 2009, that it will revise its tax treaties with 25 countries, including Switzerland and Mauritius, and seek amendments to treaties with 51 other jurisdictions in an effort to follow the money trail.

In the *Standard* article and in a December 12 *IFC Review* article, India denied that it was on a fishing expedition. In my opinion, all this is much ado about nothing. Nothing will be accomplished in Switzerland, where a high court this past week held that what the U.S. in particular, and presumably India as well, considers tax fraud and evasion doesn't qualify as such

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under Swiss law. In Mauritius, far too many high-ranking government officials and lawmakers run their Indian business through Mauritius corporations, and they simply won't allow the system to be changed — they like not having to pay tax.

A Touch of Taiwan

There will be no immediate action taken to curb the surge of foreign direct investment coming into Taiwan, the Hong Kong edition of the *China Daily* reported January 14.

A Brazilian-type tax on overseas capital has been suggested in the Taiwanese press to regulate — and stabilize — Taiwan's currency as money pours in primarily from China. Brazil imposed a 2 percent tax on overseas investors of real denominated fixed income securities, real estate, and stocks this past October, after its own currency increased in value by 35 percent. Taiwan's currency is the strongest it has been against the U.S. dollar in 16 months. Money is coming into Taiwan faster than ever before, with exports increasing 46.9 percent for December 2009.

While an investment tax to be levied on foreign investments has been proposed, the Taiwanese government is not yet willing to reduce the flow of foreign direct investments by imposing a tax.

The China Post on January 22 reported that at a January 21 forum held by the Taiwan Academy of Banking and Finance, Yen Ching-chang, the former finance minister, raised doubts about the government's capability to tax hot money because it is hard to keep track of it. He argued that it is not feasible to tax foreign capital, but that instead, the government should monitor local companies' corporate governance to ensure their financial stability. I question what corporate governance and the financial soundness of Taiwanese corporations have to do with the problems of money flow into Taiwan.

Thus far in 2010, US $2.4 billion of foreign funds has come into Taiwan's stock market. Perng Fai-nan, governor of Taiwan's central bank, along with proponents of the tax on foreign direct investment, say the tax will help make up for the shortfall in tax revenue that will be more noticeable after the signing of the cross-strait economic cooperation framework agreement, which is essentially a free trade agreement between Taiwan and China.

It will be a juggling act to encourage the flow of money into Taiwan, maintain a stable currency, and place a tax on it; however, the government has not yet learned how to juggle.

The *China Daily* also reported that the Legislative Yuan, Taiwan's legislative branch, has passed an ''anti-luxury tax'' targeting debtors who live in luxury despite their declared inability to pay their debts and taxes.

This development arose because Jack Sun, the former chair of the Pacific Electric Wire and Cable Co., had an outstanding NT $300 million debt of unpaid taxes but was seen shopping for luxury goods and living in a home worth far more than his stated income indicated he could afford. Taiwan's Ministry of Justice can now impose penalties and fines for unpaid tax debts and can preclude those debtors from purchasing, using, or renting products over a yet-to-be determined value; from riding in luxury or high-cost automobiles; from taking first-class cars on Taiwan's train system (assuming those debtors ride the rails); and from making investments.

I question how the government will be able to enforce this. I can think of several ways to work around it, and I'm sure the debtors have as well. But has the government been able to figure that out?

A Touch of America — in the P.R.C.

What happens when a municipality in China can no longer obtain revenue from selling property?

That is a serious problem affecting Shenzhen and other cities throughout the People's Republic of China. Income from property sales funded the Shenzhen government, but for all intents and purposes, there's no more land left for sale; the property well has run dry. That means one thing — an American-style property tax is right around the corner.

Actually, a property tax has been in effect in sections of Beijing and Lioning Province for the past six years. Thirty-two cities, counties, and districts assess it, and China plans to expand it nationwide, the *Global Times* reported January 6.

But still to be determined is how to estimate property values and create a property database that could be shared by both developers and tax authorities. Fraud prevention is also a major issue that must be addressed.

Alibaba.com, a global trading and news Web site, said expansion of the property tax to other municipalities won't happen in 2010 because of the difficulty in creating a fraud-free system.

Yet the fact is that the property tax will come to China within a couple of years because there is no more land to sell. The Shanghai municipal government is demanding that developers that have purchased land for development either develop it now or relinquish it to the government to resell. The pressure for expanded municipal services will bring about new tax policy, regardless of whether the developers like it.

Taxation in China is administered by both the national and local offices of the State Administration of Taxation. Each office either collects taxes for its own use or collects under a sharing principle, dividing revenue between the central and local governments.

It has been some time since I have written about the basic types of taxation in the P.R.C. There have been substantive changes over the past couple of years — especially last year — such that it's time to focus on this area in coming articles. ◆

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