

9th November, 1939.

PRESENT:—

HIS EXCELLENCY THE GOVERNOR (SIR G. A. S. NORTHCOTE, K.C.M.G.).

THE HONOURABLE THE OFFICER COMMANDING THE TROOPS, (BRIGADIER A. B. THOMSON, M.B.E.).

THE COLONIAL SECRETARY (HON. MR. N. L. SMITH, C.M.G.).

THE ATTORNEY GENERAL (HON. MR. C. G. ALABASTER, O.B.E., K.C.).

THE SECRETARY FOR CHINESE AFFAIRS (HON. MR. R. A. C. NORTH).

THE FINANCIAL SECRETARY (HON. MR. S. CAINE).

HON. COMMANDER G. F. HOLE, R.N. (Retired), (Harbour Master).

HON. MR. T. H. KING (Commissioner of Police).

HON. DR. P. S. SELWYN-CLARKE, M.C., (Director of Medical Services).

HON. MR. A. B. PURVES (Director of Public Works).

HON. SIR HENRY POLLOCK, KT., K.C., LL.D.

HON. MR. S. H. DODWELL.

HON. MR. CHAU TSUN-NIN, C.B.E.

HON. MR. LO MAN-KAM.

HON. MR. LEO D'ALMADA E CASTRO, JNR.

HON. MR. A. L. SHIELDS.

HON. MR. T. E. PEARCE.

HON. MR. LI TSE-FONG.

MR. A. G. CLARKE (Deputy Clerk of Councils).

MINUTES.

The Minutes of the previous meeting of the Council were confirmed.

NEW MEMBER.

The Honourable the Officer Commanding the Troops (Brigadier A. B. Thomson, M.B.E.) took the Oath of Allegiance and assumed his seat as a Member of the Council.

PAPERS.

THE COLONIAL SECRETARY, by command of H.E. The Governor, laid upon the table the following papers:—

Resolution made and passed by the Legislative Council under section 3 of the Public Officers (Changes of Style) Ordinance, 1937, Ordinance No. 25 of 1937, dated 26th October, 1939.

Order made by the Controller of Food under the Defence Regulations, 1939, with the consent of the Governor, fixing the standard prices of certain articles of food, dated 27th October, 1939.

Amendment made by the Court of the University under section 13 (2) of the University Ordinance, 1911, Ordinance No. 10 of 1911, to Statute 11 of the Statutes of the University, dated 26th October, 1939, and approved by the Governor in Council on 26th October, 1939.

Amendments made by the Governor in Council under section 3 of the Hydrocarbon Oils Ordinance, 1939, Ordinance No. 11 of 1939, to the Regulations contained in the First Schedule to the said Ordinance, dated 27th October, 1939.

Trading with the Enemy (Specified Persons) Order, 1939, made by the Governor, with the prior approval of the Secretary of State, under section 3 (2) of the Trading with the Enemy Ordinance, 1914, Ordinance No. 25 of 1914, as amended by regulation 2 of the Trading with the Enemy Ordinance, 1914, Amendment Regulations, 1939, dated 3rd November, 1939.

Defence (Salvage) Regulations made by the Governor under the Emergency Powers (Defence) Act, 1939, as extended to the Colony by the Emergency Powers (Colonial Defence) Order in Council, 1939, dated 27th October, 1939.

Order made by the Controller of Food under the Defence Regulations, 1939, with the consent of the Governor, fixing the standard prices of certain articles of food, dated 3rd November, 1939.

Proclamation No. 16.—Additional members of the Hong Kong Naval Volunteer Force called out for actual service.

Administration Reports, 1938:—

Part I.—General Administration:—

Report to the Director of Colonial Audit on the Audit of the Accounts of Hong Kong, 1938, with copy of forwarding despatch to Secretary of State for the Colonies.

Part II.—Law and Order:—

Report of the Commissioner of Police.

QUESTIONS.

HON. MR. M. K. LO asked:—

Having regard to the following facts—

(1) That the Prevention of Eviction (No. 2) Amendment Ordinance, 1939, was passed “without opposition only on receiving an assurance from the Government that all representations as to amendment of this special restrictive and temporary legislation would be referred to a qualified committee of two official and five unofficial members of the Legislative Council for consideration and report,”

(2) That the report of the Committee referred to above was laid on the table at the meeting of this Council held on the 1st September, 1939,

(3) That the bill of an Ordinance to consolidate and amend the Prevention of Eviction Ordinances, 1938 and 1939, as drafted by the said Committee, was read a first time in this Council on the 1st September, 1939, and

(4) That the Honourable the Attorney General, in moving the said first reading stated in effect the second reading of the said bill would be taken at the then next meeting of this Council—

Will Government explain the reason for delay in implementing the report of the said Committee and state what it intends to do as regards the said Bill?

THE COLONIAL SECRETARY replied:—

Subsequently to the first reading of the Bill the Government came to the conclusion that some of its provisions, especially those

which withdrew the protection of the 1938 Ordinance from certain classes of mortgaged premises, were contrary to the interests of the persons whom that Ordinance was chiefly designed to protect. Whilst recognizing that the Ordinance pressed hardly on mortgagees the Government considered that it was not in the general interest to amend the Ordinance to their particular advantage. The decision which the Government came to does not involve the total abandonment of the Bill, which contained other provisions of a useful and helpful nature; but careful consideration of the effect of these provisions has had to be postponed while other legislative problems arising from the outbreak of war were being dealt with.

FINANCE COMMITTEE'S REPORT.

THE COLONIAL SECRETARY, by command of H.E. The Governor, laid upon the table the Report of the Finance Committee (No. 8), dated 26th October, 1939, and moved that it be adopted.

THE FINANCIAL SECRETARY seconded, and this was agreed to.

DEBATE ON ESTIMATES AND INCOME TAX.

THE COLONIAL SECRETARY moved the following resolution:—

That the Estimates of Expenditure for the year 1940-41 as now presented be approved.

He said: Sir,—I rise to propose the motion standing in my name.

On 12th October, 1939, by a Resolution of this Council the draft estimates of expenditure for 1940-41 were referred to a Select Committee consisting of myself, the Financial Secretary and all unofficial members of this Council.

In proposing that motion the Honourable Financial Secretary announced that it was the intention of Government to ask the Committee, in accordance with the policy which Your Excellency had stated when opening the debate on that day, to present its report in the form of two budgets, namely an ordinary budget and a war budget.

At that time it was fully expected, as Your Excellency said, that proposals for the imposition of Income Tax, the only Revenue head in the war budget, would be sufficiently advanced by now to allow of action to be taken on the lines indicated, but that expectation has not been realised and the Budget which I present to-day as the report of the Select Committee is substantially the one which was considered on 12th October. I am to make it clear that this departure from the original programme is wholly on account of the shortness of time before the opening of the new financial year and must not be taken as an indication that Government has abandoned the scheme.

It is, however, necessary to provide at once for extra expenditure on, for instance, the Volunteers, Maintenance of Internees, the Censorship Department, and so on, which would have been included in the special war budget. It is very difficult to estimate these expenses precisely and a single sum of \$1,000,000 has therefore been included to cover them, under a new Head called Special War Expenditure. This will in due course be transferred for accounting purposes to the war budget if that plan is ultimately carried out.

Certain other additions have been made to the original draft estimates of expenditure: the sum for the Auxiliary Fire Service has been increased to \$9,500 and it has been decided to proceed with the building of the New Fire Station in Hennessy Road at a cost of \$110,000. On the other hand the additional duties recently imposed on liquor and petrol have necessitated a revision of the estimate of revenue: revenue from Duties will, it is now estimated, amount to \$13,526,000 instead of \$12,526,000.

The estimated deficit of \$326,708 shown in the draft estimates as presented on 12th October will be increased to \$440,708.

The following are the items which have been added:—

Head 6 E, Special War Expenditure	\$1,000,000
Head 10, Fire Brigade.	
Sub-head 2, Auxiliary Fire Service	8,500
(Increased from \$1,000 to \$9,500)	
Head 11 B, Air Services.	
Additional Guard for Airport Ground Staff	465
Head 29, Treasury, etc.	
Additional Messenger for Assessor's Office	255
Head 30, Public Works Extraordinary.	
Sub-head 10, New Fire Station in Hennessy Road	105,000
(Increased from \$5,000 to \$110,000)	
	\$1,114,220

The following item has been reduced:—

Head 19, Police Force.	
Sub-head 41, Filing Cabinets	\$220
(Reduced from \$1,510 to \$1,290).	

A few misprints, notably an obvious one in Head 18, Pensions, have been corrected.

I beg to move.

THE FINANCIAL SECRETARY seconded.

HON. SIR HENRY POLLOCK.—Your Excellency,—I have no comments to make on the Budget for 1940-41.

In regard to the proposed War Gift to the Imperial Government, as a resident of the Colony for 51 years, during 29 years of which time I have served as a Member of this Council, I make no apology for treating the making of this gift from the point of view of the welfare of this Colony rather than from the point of view of contributing what must, whatever actual annual sum in dollars is remitted to the Imperial Government, be a mere mite in the War Expenditure of Great Britain.

In taking this view I am supported by the Right Honourable the Secretary of State for the Colonies who clearly, and wisely, told us that "there should be as little disturbance as possible with the Colony's current activities and development schemes, so long as revenue to finance them would be forthcoming."

It is our duty, therefore, in this Council, in considering the amount of dollars to be remitted to the Imperial Government as a gift, to look ahead beyond the immediate present, and to conserve our resources for "current activities and development schemes."

I am convinced that it would be imprudent finance to make an annual contribution to the Imperial Government of a larger sum than \$3,000,000, in addition to the \$6,000,000, per annum which we have to pay for our ordinary Military Contribution and to the sum of nearly 2¼ million dollars in respect of Defence and Special War Expenditure for 1940-41.

My reasons for holding this opinion are:—

(1) That nobody can foretell how long the present war will last, and, therefore, that we are not justified in mortgaging our financial future for an indefinite period of time by sending out of the Colony annually as a special War Gift more than three million dollars.

(2) That the total amount required to be voted eventually to complete the following items in Public Works Extraordinary for 1940-41, namely, items 11, 14, 15, 19, 21, 22 and 23, is over three million three hundred thousand dollars, whereas the amounts now being voted for commencing those works total no more than two hundred and fifteen thousand dollars. The big difference between the above amounts will have to be made up by the tax payer in future Budgets unless we are to leave those Works in a state of suspended animation for the wholly unknown and uncertain duration of the war.

(3) In his speech in this Council on the Budget, on the 12th October, the Honourable the Financial Secretary said:—

“In preparing the final draft a number of items of new expenditure which it had originally been desired to include were deleted in order to avoid budgeting for any substantial deficit in the uncertain circumstances which lie before us.”

That statement of the Financial Secretary I regard as an important admission that certain desirable items of expenditure were excluded from the Budget because of the “uncertain circumstances which lie before us,” and nobody who is acquainted with the circumstances of Hong Kong will dispute that there are many other public works which we would like to have carried out if finances permitted. This seems to me a very strong argument not only against our sending home as a War Gift a sum of more than three million dollars but also a very strong argument against the imposition of a tax like income tax, which will seriously upset Chinese capitalists and industrialists in this Colony.

A few days ago I visited the Kwong Wah Hospital and found that it was badly overcrowded, with, in some cases, two patients occupying the same bed. Also I found over 200 patients quartered in four matchsheds in the grounds, who are exposed to serious danger in case of fire.

In these circumstances it is obvious that more hospital accommodation for several hundred patients ought to be built as soon as possible, involving a probable expenditure of about two million dollars.

I am confident that Your Excellency, who has Public Health matters in this Colony so much at heart, will agree that this is a responsibility which rests upon the Government and that these new hospital buildings ought to be erected as soon as practicable.

My Honourable friend, Mr. M. K. Lo, will presently refer in his speech to other long-overdue Public Health needs, such as a hospital for children and a sanatorium for tuberculous cases. These are obviously projects involving the expenditure of considerable sums of money.

I now pass on to the main theme of my speech, which is that, for the purpose of making a gift to the Imperial Government, other taxes which would not involve the risk of injuring the trade and prosperity of this Colony ought to be substituted for income tax.

In the opinion of responsible business men of this Colony the imposition of income tax would be a disastrous form of taxation to adopt, for it is the unanimous opinion of the Committee of the Hong Kong General Chamber of Commerce, and of the Committee and Members of the Chinese Chamber of Commerce, that they are not in favour of the institution of income tax in this Colony.

My Unofficial colleagues on this Council are unanimously opposed to income tax.

I confess that I find it very difficult to understand what justification the Government has for proceeding with the consideration of an income tax bill in view of the fact that those British and Chinese Experts have unanimously expressed themselves as being opposed to Income Tax.

Anybody who understands the mentality of the Chinese must realise that such a measure as income tax would be likely to cause the flight of capital from this Colony and to prevent new remittances from being made to Hong Kong and also that it would probably deter new factories and enterprises from starting here.

In connection with this latter point I may mention that I have been informed recently that certain Chinese, who had intended to start steelworks in this Colony, have, since income tax was mooted, abandoned the idea.

Other objections to income tax are that it would involve the trouble and expense of having numerous Chinese account books translated into English, and that its collection would involve the employment, at considerable public cost, of a large staff of new Government officials, and that the Chinese have strong objections to their private, family, and business affairs being pried into.

In the Taxation Committee's Report mention is made of the probable cost to Government of administration of income tax, but no consideration seems to have been given to the additional cost of book-keeping, records, legal advice, chartered accountant's fees, etc., that will have to be borne by any business in order to comply with the requirements of the Tax.

We have been told that income tax is enforced in Ceylon, but, with all due deference, that fact is wholly irrelevant, as conditions there are so entirely different from those existing in this Colony.

I fear that Your Excellency, in your desire for this Colony to make a contribution towards the War Gift to the Imperial Government, has not quite appreciated those serious objections to income tax which I have indicated and which will no doubt be stressed by other Unofficial Members. It is hoped, however, that Your Excellency who, in the course of your two years' administration of this Colony, has earned the thoroughly well-deserved reputation of being able to consider every side of a question, will, with the same impartiality, consider the arguments which are now being urged against the imposition of income tax, together with the suggestion that alternative taxes be imposed.

Your Excellency has recently appointed a Committee to go into details of the Income Tax Bill proposed by Government, and I understand that, in that letter of appointment, it was stated that Government was "willing to give full consideration to alternative methods of raising revenue." I have been informed, however, by the Government, that that remark does not mean that the members of that particular Committee are to be at liberty to suggest any alternative methods of taxation. Accordingly I venture to suggest that Your Excellency should now appoint a Committee for the purpose of considering alternative methods to income tax for raising revenue for the War Gift to the Imperial Government. On that Committee I should be glad, if considered eligible, to serve.

That Committee would no doubt be able to recommend many suitable alternatives to income tax. In the meanwhile I suggest some possible alternative methods of taxation, which have the merit of being easily collected, at small expense, and also of being widely spread, such as:—

- A percentage on every electric light and power bill.
- A percentage on every gas bill.
- A percentage on every telephone bill.
- The raising of the annual licence fee charged for wireless sets.
- A tax on cinema and theatre tickets.
- The institution of a special War surtax on the assessed rateable value of property.
- The collection of a percentage on dividends from investments in Public Limited Companies in Hong Kong.

On behalf of all the Unofficial Members of this Council I desire to state that Income Tax is, in our opinion, detrimental to the future of this Colony, and to request Your Excellency to appoint a Committee to consider and report on alternatives to Income Tax, for the purpose of raising revenue for the War Gift to the Imperial Government.

It is my earnest hope that a just and wise solution of this taxation problem may be found and that what ought to be a free-will offering from this Colony will go Home with the cordial and united assent of every Member of this Council. (Applause).

HON. MR. CHAU TSUN-NIN.—Sir, As the draft estimates of expenditure for 1940-41 have been carefully considered by the Select Committee, I personally have no observations to make on the ordinary budget.

As regards the war budget, it is first of all my duty to the Chinese community to dispel any impression which may have got abroad that the motive behind any opposition that has been publicly or privately expressed to the institution of a tax on income reflects any reluctance to raise a special capital contribution to the War Funds of the Imperial Government. The suggestion that the comments or

even criticism, however strong, might be construed as revealing any general attitude of antagonism by the Chinese, fortunately comes from a source which we have all learnt to regard as committed, as a matter of policy, to systematic distortion.

As representing the Chinese community, and by that I mean not only those whose loyalty arises from their British birth but all who have enjoyed for either longer or shorter periods the privileges of citizenship in this Colony, I have to refute in the most unequivocal terms that such opposition, as has already been voiced against the introduction in income tax, is associated with any unwillingness to share in full measure whatever sacrifices which are being claimed from all citizens of the British Empire. I go further and say that far from the adoption of any hesitant attitude towards the raising of a special war contribution by this Colony, it is the general desire of the Chinese community to see that in due course such a contribution be made and in a manner which will be worthy of and do credit to the loyalty of all sections of the community of this Colony.

The Chinese community is far from being insensible of the urgent and special financial needs of the Colony, and they realise that these call for consideration of new methods of raising revenue.

The opposition to the introduction of Income Tax which it is my duty to emphasise, is based on the firm conviction that its practical implication is so fraught with difficulties, that it will not only fail in its object but may bring in its train repercussions and complications in spheres which might not normally be associated with the collection of revenue.

Were the difficulties with which we are faced only of a practical nature I would consider any form of opposition which did not attempt to offer any solution as being inadequate, but as I am convinced that this revolutionary method of raising revenue in this Colony is going to place us in a position where not merely the prosperity but the whole financial structure may be imperilled, I must deprecate even prolonged considerations directed towards solving the various practical difficulties, many of which have been already voiced by public bodies and in the Press.

I feel that in considering the question of Income Tax in this Colony, where the Chinese business population predominates, we should exercise a sense, not merely of scientific but more particularly of what I might describe as "psychological" economics. We are faced by the undeniable fact that the introduction of Income Tax in a wholly or predominantly Chinese community has always proved a failure and as, obviously, there is a reason for this which might be easily ascertained or, on the other hand, evade the most vigilant inquiry, it is my view that without an answer to this question, an answer which would enable us to distinguish conditions in this Colony from countries where the experiment has failed, we are not justified in proceeding with the matter.

It is known with what little success the attempt to introduce Income Tax in Malaya has met, but what is still more important is the evidence from China itself where the Income Tax Laws, which had been most carefully worked out, have proved to be an absolute failure almost from the time of their institution.

I do not think it necessary for me to put forward any theories for these failures, but I do repeat that a very clear explanation should be the starting point and not an incidental matter for our own deliberations.

The Taxation Committee appointed by Your Excellency in October, 1938, had already, as I will admit, a background of very abnormal conditions in this Colony, arising out of the Sino-Japanese hostilities which had then been in progress for over a year. That part of their Report which deals with Income Tax cannot, therefore, be said to have ignored entirely the unusual commercial and financial situation which then existed and might continue for an indefinite period. It is, however, worthy of note that in furnishing replies to a number of practical difficulties in the institution of Income Tax relating to questions which the Committee itself had raised, a very strong note of caution was sounded, and I desire to refer particularly to certain preliminary and conditional recommendations.

These include the absolute necessity for a detailed investigation of the whole field with the assistance of an "expert", and to this I would personally add the maintenance of numerous experts, far beyond the preliminary or introductory stages. And further, the Committee recommended that the imposition of this form of Tax should be preceded by the formation of a large and substantial body of favourable opinion in this Colony.

The experts whose reports I should like to hear before this matter proceeds any further, are not those who can assure us how successfully Income Tax works in other communities, but why it has failed amongst Chinese communities. As for those who would be responsible for administration of Income Tax they would all have to be persons with expert training and much experience.

The hope of obtaining such advice and permanent assistance does not, under existing conditions, appear at all bright. The alternative of procuring officials who have to gain their experience at the expense of the smooth working of the system, which should be guaranteed from its initiation, is a sure way of maintaining its unpopularity.

I am convinced that the majority of the Chinese community believe that it will never be possible to approach that stage at which the incidence of the Tax falls fairly and equitably amongst those who should contribute their more or less towards it. In the Chinese business community the conception of profits on investment differs fundamentally from that which is essential for the assessment of the

Tax. I am aware that there is an increasing proportion of Chinese book-keeping which approaches European methods, but the bulk of Chinese business, whether connected with production or industry or with that preponderance which may be described as general trading, adheres to the systems which, although taking care of the specific profits on output or sales, do not take cognizance of general profits on enterprise.

In unincorporated partnership is issued a combined Balance Sheet and Income and Expenditure Account in which what is considered as the capital may be increased or decreased but in which the "profits for distribution" as such are not shown.

To those who claim that the information required for assessments may nevertheless be easily extracted, and to those who maintain that a partial transition from the present methods has been envisaged, I would make the same reply, namely, that all who are qualified to speak in such matters deny that such transformation appears feasible, except perhaps at the expense of much confusion and ultimate defeat.

In spite of marked and, we hope, permanent industrialisation which has been noted in recent years, the foundation of the Colony's business is still the merchant through whom business flows from the outside world to and from the mainland.

I need perhaps not remind Your Excellency that the book-keeping for the average Chinese merchant is divided into two very separate compartments. There is the general recording of transactions with the world at large which is dealt with by the employees of what is known as "the outer counter", but there is an additional set of books which are kept in "the inner counter" by the proprietor or partners of the business maintained under conditions of extreme privacy, to which no employees have access under any circumstances.

We must try to realise that an official invasion of the "inner counter" means to a Chinese business man a great deal more than the disclosure of his business secrets. To understand this we should appreciate that this privacy, which is traditional, has no origin in any attempt to evade taxation or to mislead official inquiry. It is not a question merely of disclosure of business secrets, of sources of supply or of customers, but of the breaking down of a traditional element in business procedure which has been regarded for centuries as a fundamental form of security, and with it would go a degree of confidence which might undermine the whole structure of business life.

It may be said that the assessments would depend only in part on the investigations of books, and that there are considerable sources from which reliable and indisputable information is available. These include income from public investments, public or private companies, from house properties, mortgages, salaries (which are a matter of record by employers), and all income which is remitted from abroad and which passes through recognized channels such as Banks.

Whilst not agreeing that the proportion of these sources is as large as anticipated, the ability to tax that source does not, unless I misunderstand the situation, provide any encouragement. There arise numerous questions of refunds, rebates and allowances which will have to be considered, as in the vast majority of cases such class of income will not represent the sole sources.

In this Colony, except perhaps in the case of foreign employees, instances must be comparatively few where income is derived merely from a single source. We are, therefore, invariably thrown back, for the purpose of assessment not only of income but of allowances, to investigate each individual case.

As an example of one class of difficulty, I am reminded of the very large proportion of the business transacted in this Colony by what is known as the "middle man" or commission agent, the person who buys and sells not for his own account but passes money after making certain recognised deductions. I would be surprised to hear that the total income from this class of business could be ascertained, with an approximation to accuracy, by inspecting all transactions involved and the records kept by the principals in such transaction. In a large number of cases, neither of the principals carries on business in this Colony. Whilst on this question of commission, it must be well known that in each business, and indeed in many private transactions, there are recognised deductions which are not a matter of record but are, nevertheless, an essential.

It would be interesting to know to what extent the preliminary essentials and qualifications made by the Taxation Committee would have been augmented or emphasised had it been asked to report on this particular subject under the conditions imposed on this Colony through being itself involved in a state of war. I venture to surmise that what little encouragement that Report may have given to the Government for the introduction of the measure now, would have been replaced by a solemn warning against it.

Attention has been sufficiently drawn to the transitory and migratory nature of the capital—refugee capital, if I may so describe it—which has found its way to this Colony in the last two years. Investment and enterprise, including the transfer of manufacturing plant to Hong Kong, has been stimulated by a profound sense of security and by satisfactory appraisal of the benefits to be derived. A disturbance of the calculations and estimates which have preceded these wartime investments will undoubtedly involve a consideration of alternatives when it should, of course, be our object to retain the advantages which this Colony so sorely needed.

I endorse the remark made by the Hon. Senior Unofficial Member that the unanimous opinion of the Committee and Members of the Hong Kong Chinese General Chamber of Commerce is adverse to the institution of income tax in this Colony. A copy of the Chamber's letter has been sent to Government through the Hon. Secretary for Chinese Affairs.

I will conclude, as I began, with an assurance that the responsible elements of the Chinese community are prepared to assist in every way they can in finding a solution to the urgent and special financial problems with which the Colony is faced.

Numerous methods of raising revenue alternative to Income Tax have already been suggested, and in their consideration the Chinese business community desires to be not critical but constructive. No scheme will be attacked only on the ground that it inflicts hardship or strain on any portion of the community. But the opposition to the institution of anything in the nature of a tax on income or profits, which I now have formally to record, arises mainly from the firm conviction that the disturbing effect of its introduction and the confusion attendant on its administration will, by doing incalculable harm to business interests, defeat the object which it is obviously the desire of the Government to attain. (Applause).

HON. MR. LO MAN-KAM.—Your Excellency,—My Honourable friend, the Financial Secretary, in his illuminating “Memorandum on the Financial Position 1938, 1939 and the Estimates for 1940-1941”, to which I shall have occasion to refer again, remarks:—

..... “As last year, the revenue for 1940-1941 has been estimated generally on the assumption that the economic activity of the Colony will be maintained at not far short of its present level. This may prove to be over optimistic, especially since the outbreak of the war, but the whole outlook is at present so uncertain that no other firm basis for estimating the revenue presents itself.”

With the inevitable dislocations of trade caused by the war, and by the various measures dictated by Imperial war economy, and with new taxation under the proposed War Budget, I confess to a strong feeling that the Financial Secretary's fear that the assumption on which the revenue position is based may be over optimistic will, unhappily, prove only too true. I wish, therefore, to state that, in assenting, as a member of the Select Committee, to the Budget now before the Council, I have paid due regard to the Financial Secretary's statement in this Council on the 12th October, 1939 that the programme of Public Works Extraordinary and also the many items of special expenditure appearing in the individual Heads of Estimates, although approved by this Council and the Secretary of State, would not be automatically carried out if the revenue position did not justify the expenditure.

The above, Sir, is all that I have to say on the General Budget, except to renew a plea which has already been made by me in the last two successive Budget Debates in this Council. The plea, Sir, is that Government may be kind enough to make a substantial grant for providing charitable and medical relief to the Chinese on account of the Sino-Japanese conflict.

As I have previously pointed out, such relief is in a humanitarian cause which transcends any consideration of mere “profit and loss”.

But, speaking in this Council on the 13th October, 1938, I was able to show, on the high authority of the Financial Secretary, that in respect of 1937 the revenue benefited to the extent of over \$4,400,000 by the Sino-Japanese conflict. Since then very striking figures have been revealed by the Financial Secretary's Memorandum, to which I have already referred.

Taking, first, 1938. When the Estimate for Revenue was first framed, Revenue was put at just over 30¼ million. The actual revenue exceeded this estimate by \$6,480,935.00, and this excess is attributed by the Financial Secretary "to the increase in the activity of the Colony which prevailed, owing largely to the Sino-Japanese hostilities and the large increase in population due to the same cause."

On the other hand, the original expenditure, put at \$33,379,549, exceeded the estimate by \$3,796,349.00. But of this excess the Financial Secretary points out that \$2,203,216.00 was in respect of unallocated stores, loans and Military Contribution, due to changes in the accounting system, leaving an excess of \$1,593,133.00 in respect of all other Heads. But the only items that can fairly be attributable to the Sino-Japanese conflict are Head 22, Medical Department (epidemics and larger population \$229,513.00), Head 29, Charitable Services (relief of refugees \$245,555.00), Head 34, Public Works Extraordinary (construction of refugee camps and acquisition of property \$622,052.00), amounting to \$1,097,120.00.

The nett gain to the Colony is therefore \$5,383,815.00.

Coming, now, to 1939. The original estimated revenue was put at \$36,097,325.00 (including \$839,704.00 transferred from Government House and City Development Fund). Now this estimate was obviously framed on the basis of the continued operation of the same factors which brought about such striking increases to the Colony revenue in 1938. If this argument is sound, as I think it is, then it can be fairly stated that the nett gain to the Colony in 1939 must be approximately the same as in 1938, on the basis of the original estimate, less any increased expenditure which had not been taken into account in the Estimate of 1939 Expenditure. Of the latter, as shown in Table 3 of the Financial Secretary's Memorandum, the only item I can find relates to Head 5, Charitable Services (relief of refugees), in respect of which the excess over original estimate amounts to \$1,241,736.00.

The nett gain to the Colony for 1939, on the basis of the original estimate, is therefore, say, roughly \$5,000,000.00 less \$1,241,736.00, i.e. \$3,758,264.00.

But the revised estimate of revenue of \$40,475,248.00 shows an excess of \$4,377,923.00 over the original estimate, and if the sum transferred from Government House and City Development Fund (\$839,704.00) is deducted from this increase, the increase as shown by the Revised Estimate amounts to \$3,538,219.00.

The total nett increase to the Colony attributable to the Sino-Japanese conflict for 1939 is therefore \$7,296,483.00.

The gain to the Colony in respect of 1937-1939 is ascertainable and, on my calculation, amounts to a total of \$17,080,298.00. The gain for 1940-1941 can only be an estimate, based on the estimated Budget figures.

Coming, then, to the prospective revenue and expenditure of 1940-1941. The estimated revenue, which "has been estimated generally on the assumption that the economic activity of the Colony will be maintained at not far short of its present level", is put at \$50,861,470.00. It is therefore fair to assume that the nett gain to the Colony arising from the Sino-Japanese conflict will not be less than in 1939, namely, \$7,296,483.00, plus a quarter of this amount for the 3 months in 1941 = \$1,824,120.00 making a total of \$9,120,603.00, less any increase in expenditure attributable to the same causes not budgetted for in 1939. Of the latter, as shown in paragraph 11 of the Financial Secretary's Memorandum, the only item I can see which is directly attributable to the Sino-Japanese conflict is under Head 5, Charitable Services, which shows an increase of \$224,749.00, being "increased grants to the Tung Wah Hospital and for relief of refugees". Moreover, I note from Part 2 of the Financial Secretary's Memorandum, Head 5, Sub-Head 23, that the amount of \$250,000.00 provided for relief of refugees at the present rate of outlay, will not suffice for more than six months. If, therefore, we increase this amount to, say, \$625,000.00 to cover the whole period of fifteen months, plus the whole increase of \$224,749.00, totalling \$849,749.00, and subtract this total from the nett increase of \$9,120,603.00, the resulting increase to the Colony revenue for 1940-1941 is \$8,270,854.00.

If my calculation is right the financial gain to the Colony arising from the Sino-Japanese conflict, in respect of the period 1937 to the end of March, 1941, comes to the stupendous figure of \$25,351,152.00.

Honourable members may be interested to know that the total subscriptions received up to October, 1939 by the British Fund for Relief of Distress in China, Hong Kong and South China Branch, amount to \$491,874.70, and that the amount of expenditure already sanctioned comes to \$406,176.11. This Fund, of which Your Excellency is Patron, is non-political, and purely philanthropic. The flow of subscriptions to the Fund seems to be rapidly drying up, whilst calls on its resources are continuous. May I, therefore, venture to express the strong hope that Your Excellency will see fit to making a substantial grant to this Fund as a friendly gesture of the Colony towards the indescribable sufferings of the Chinese?

I now turn to the War Budget.

The Prime Minister, in the House of Commons on October 12th, stated:—

"It is not with any vindictive purpose we embarked on war but simply in defence of freedom. It is not alone the freedom of a small nation that is at stake. There is in jeopardy the peaceful existence of Britain, the Dominions, India and the rest of the British Empire, France, and indeed all freedom loving countries."

This quotation bears eloquent testimony to the force and meaning of Your Excellency's observation in this Council on the same day, that "this is every whit as much our war as it is Britain's". And the complete realization of the implication of this war on the part of the public is reflected in its ready acceptance of and full-hearted co-operation in all the varied measures which Government has found it necessary or desirable to introduce in this Colony, although many, if not all, of them must have a restrictive effect on business. That residents in the Colony—irrespective of their race and nationality—should have to bear some financial sacrifice, in order that a contribution might be forthcoming to the Imperial War Chest, fitting from the point of view of the Colony as a vital part of the British Empire and worthy of a Colony which yields to none in loyalty and devotion to the Crown, is inevitable. Indeed, they should welcome the opportunity of making such a contribution, for it is unthinkable that they would be content to render mere lip service to a cause, the result of which must have such a significance to Civilisation.

I am certain that there is a complete unanimity amongst all sections of the community on this point. A recollection of the part which this Colony took in the 1914-1918 war—including the splendid response of its citizens to appeals for war charities and war loans, and the voluntary presentation to England of two Service aeroplanes by certain Chinese residents—renders it impossible for anyone to entertain any doubt of the Colony's attitude in this matter.

But I feel it my duty to make it quite plain that, in my view, the reason why the people of the Colony desire so keenly to "do their bit" is because they are animated by sentiments which I have just endeavoured to express, and not because they agree with the statement, which has been made in this Council, that the Colony is lightly taxed, nor because they can regard as otherwise than superficial the comparisons, which have also been made in this Council, between the crushing burden laid on the British tax-payer and the light burden imposed on the Hong Kong tax-payer.

Before coming to the Colony's contribution I wish to deal shortly with both of these points. Sir, there are no data which lead me to think that the Colony is lightly taxed in relation either to the social services available, or to the taxable capacity of the Colony.

I propose to touch on the question of local social services later on in my remarks. In the meantime I must concede that this question is complicated by the peculiar position of the Colony, with its large fluctuating and migratory population.

As regards the taxable capacity of the Colony, it seems to me that an important point which requires expert investigation is as to how much of the Colony's wealth is in the hands of the permanent resident, and how much of it is fugitive and can be driven away by burdensome taxation. From the earliest Hansard which, thanks to my Honourable friend, Sir Henry Pollock, happens to be in my possession—that for 1906—I notice that the estimated revenue for 1907 was under 5½ million. By 1915 the revenue was nearly doubled. In 1930 it nearly reached the 28 million mark, and from then to 1936 it fluctuated between 28 to 33 million. The average yearly revenue for the past 10 years works out at 32½ million. I venture to think that no one who has studied the Budget figures of past years can fail to experience a sense of concern and dismay at the colossal rise in the cost of Government, culminating in this year's 40 million dollar Budget, or to ask himself anxiously whether the Colony's expenditure is not reaching, if it has not already over-reached, the Colony's taxable capacity. Those who care to read the 1906 Budget Debate will find it interesting reading. They will find, too, that the slogan "Hong Kong is lightly taxed" was already current in those early days! The estimated revenue for 1907 was \$5,202,135.00, which apparently represented a somewhat serious decline on the previous year's revenue. The following quotation from Sir Matthew Nathan's address gives an interesting historical background of the Colony's revenue position, and constitutes not an unworthy guide to us as to how the Colony's financial difficulties should be met in times of adverse trade or economic uncertainty:—

"Before going into the long array of figures which I have on my notes I think it will meet your wishes if I explain generally how it is proposed to meet that decline. There are three methods open to us. Either to raise further loans, or to increase taxation, or to reduce expenditure. I am strongly averse to raising additional loans at the present time. . . . I am also averse to increasing taxation. It has been pointed out to me that this colony is very lightly taxed, and I by no means promise that I shall not on some future occasion propose additional imposts, but a time like the present one when trade is bad does not seem a suitable one at which to add to the burdens of traders. . . . There remains a reduction of expenditure, and that is the method which it is proposed to adopt. We must cut our coat according to our cloth. It must necessarily be a simple garment but I hope when I come presently to try it on you, you will agree with me that it is a fairly serviceable one in which the Colony need not feel ashamed to appear next season. It is somewhat of a tight fit, but if we adhere to the estimates we have framed we shall remain in the same sound financial position at the end of 1907 as I am happy to say we shall be in at the end of 1906."

As regards comparisons between Great Britain and Hong Kong I submit, Sir, that however flattering it may be to compare the Colony with the Mother Country, the greatest and wealthiest democratic

country in Europe, no useful comparison between the two places from the point of view of fiscal incidence can be fairly made, having regard to the radical differences in government, institutions, economic resources and social conditions.

In England the amount spent since the commencement of this century on Health, Education, Housing and Social Services—Unemployment Benefits, Poor Law Relief, Old Age Pension, Industrial Insurances, etc.—amounts to astronomical figures. From the primary school to the university, thence to the highest post in the State, the path is open to the poorest lad with brains. Here is a pen-picture of post-war England by Professor H. A. L. Fisher, in his "History of Europe" (page 1210):—

"At this time the British people bore without repining a burden of taxation heavier than that of any European country. The annual service of the debt charge alone amounted to more than 300 million sterling. Fifteen years after the end of the war the State levied 4s. 6d. in the pound on the income of the tax payer irrespective of the supertax on incomes exceeding £2,000 a year. Yet it is characteristic of the democratic spirit which prevailed in the country that, despite bad trade and crushing taxation, the level of the social services, higher than that which prevailed in any other country and more expensive, was not seriously lowered. That the health, the education, and the housing of the people should be well cared for was common ground with all parties in the State."

We are naturally proud of the wonderful progress which the Colony has made under British Rule within the short space of a century. And yet what is its position to-day? Substantially a non-producing country, the Colony still depends mainly on its being an entrepot for its continued prosperity. Though there are undoubtedly known rich people, and also people whose riches are unknown because concealed, sheer poverty is general and widespread. On the question of prevalence of poverty I need hardly dwell, for it is a painful fact, well known to all social workers. Only at the beginning of this year the Honourable the Director of Medical Services, in his inaugural address before the newly reconstituted Nutrition Committee, pointed out that on account of malnutrition, which is a concomitant of poverty, more than one child out of every three died last year before attaining the age of one year, as compared with one in twenty in England. We have no hospitals for children. Indeed, our hospital accommodation is utterly inadequate, and the overcrowding in the Chinese hospitals is, though inevitable, a standing disgrace. The problems of compulsory education (and even of Government-provided primary education), and of juvenile delinquency, are still a long way from being solved. With thousands of deaths from tuberculosis we have as yet not been able to find the means to build a properly equipped sanatorium. For lack of funds we have not begun to tackle the problem of Slum-clearing. We have no Old Age Pension, no Poor Law. We have no Air Protec-

tion for the masses. Since Your Excellency's arrival in the Colony you have spared no effort in providing and increasing social amenities for the Colony in every direction possible, and the Colony owes Your Excellency a very heavy debt of gratitude. But the list of omissions is necessarily still formidable.

As the *South China Morning Post*, in its leading article published on the 13th October, 1939, pointed out:—

“The upper ranks of the Government Service are not open to the Hong Kong citizen: he has no vote nor does he enjoy the full privileges of a British subject—his nationality is only stressed for taxation purposes. The Colony is predominantly Chinese. It has therefore a dual allegiance and a dual commitment. These have emphasised themselves in the Far East war that has been raging for two years—a war which has profited some in the Colony, but bled the majority through many economic wounds. No other part of the Empire has suffered this strain.”

In connection with the above I feel it my duty to give expression to the sense of injustice felt by many of the companies incorporated in Hong Kong which carry on business in Shanghai, Hankow and other parts of China. By the Defence (Finance) Regulation 3B, Government has the right to acquire certain foreign currencies from every British subject (as defined) resident in the Colony, and certain duties are imposed upon such a British subject. By this Regulation “British Subject” includes every company incorporated in the British Empire. During the Sino-Japanese conflict companies of the class I have mentioned have sought protection from the British Authorities, but such protection has always been refused on the ground that such companies, though registered in the Colony, are not entitled to protection. In one case to my knowledge a company incorporated in Hong Kong, which is a “British Subject” as defined by the Regulation, has properties in Canton, Swatow and Toishan, which were either burned or looted, or both.

I have discussed these points—the lightness of Hong Kong taxation and the relative burdens between the British and Hong Kong tax payer—not for the purpose of finding excuses for us to try to “get out cheaply”, but of showing that, in my submission, we should approach the question of the Colony's contribution to England as a matter of patriotic duty, freed from any self-reproof that we have been too lightly taxed, and untroubled by any comparisons made between Hong Kong and elsewhere. I therefore approach the question in this spirit.

First, as to the amount of the contribution.

It must be appreciated that a gift to Great Britain of seven or eight million dollars, as suggested by the Hon. Financial Secretary, can be only a gesture of the Colony's patriotism and of her willingness

to "do her bit" as a part of the British Empire. That sum represents only a few hours of the Imperial War Expenditure, and nothing that the Colony can give can be of any material financial assistance to England. This being so, I feel the less reluctant to discuss the quantum of the proposed gift in relation to the Colony's capacity. A gift of \$7,000,000 represents 21.5% on the yearly average revenue for the past ten years of 32½ million. If to this amount we were to add the special Defence expenditure of 2¼ million, and the Military Contribution of 6 million, the total amount would come to \$15,250,000.00, which is 46.9% on the yearly average of 32½ million. I cannot help thinking that the gift is too much for the Colony, having regard both to the Colony's position and to the Imperial needs at the present time. I venture to think that for 1940, and until the Colony's position becomes a little more clarified, the gift to England should not exceed \$3,000,000.

As we are all agreed that the Colony should make the best contribution of which it is capable, the problem confronting this Council resolves itself to one of finding the best means of raising the money.

Since the underlying idea is a free and spontaneous gift by the Colony to England, and not a tribute to be exacted from an unwilling population, the following broad principles should, in my opinion, govern the choice of means:—

- (1) That, if possible, the means chosen should not involve a violent departure from the Colony's fiscal policy, which has been in existence for nearly a century; and
- (2) That the means adopted should command as much popular approval as possible: at least it should not go counter to deep-rooted and fundamental objections of a substantial portion of the community.

Moreover, it seems to me that the amount of the gift should be subordinated to the means available, based on the above principles, rather than that the means should be adopted in violation of those principles for the sake of obtaining an arbitrarily decided amount. Accordingly I am bound to say that I do not agree with the Government view that the imposition of an income tax is by far the most suitable means to give effect to the natural desire of everyone to bear his just burden for the common cause, for it violates both of the principles I have suggested.

There can be no reasonable doubt that views opposed to the introduction of income tax have been consistently held by many people in the Colony for at least a quarter of a century. Moreover, the Chinese opposition to this measure must be well known to Government. When the idea of an income tax was mooted in connection with the 1914-1918 war the then Senior Chinese representative on

this Council, the late Mr. Lau Chu Pak, wrote in to Government a strong memorandum against it. My Senior colleague on this Council, on the 10th November, 1938, in anticipation of the appointment and report of the Taxation Committee, expressed himself strongly against it. As a member of the Taxation Committee which reported to Your Excellency on the 5th April, 1939, I myself sent in to the Committee a memorandum setting out in detail my own objections. Some of the grave doubts which are widely felt as to the possibility of the successful administration of an income tax in the Colony were summarised in the Taxation Committee's report, which include the following:—

"3. The migratory nature of the Colony's population, and the extremely mixed taxable community, with greatly differing standards of living, make Hong Kong unsuited to the tax generally.

4. Many benefits are still to be derived from preserving the Colony as a haven for "refugee" capital. The Colony's prosperity depends to a large extent on the fact that it is the entrepot of China, a free port, without income tax and without excessive taxation. An unwise fiscal imposition may well upset this precarious prosperity."

"9. Economic and industrial development—particularly of small factories as yet in their infancy—would be seriously affected."

The Committee, whilst recommending the introduction of income tax in a certain eventuality "if it be considered that the tax is capable of successful administration in the Colony", felt it necessary to qualify this recommendation in five ways, specified in the report, from which I merely quote two:—

"(a) The possibility of the successful working of the tax should first be the subject of a detailed investigation with the assistance of an expert, preferably familiar with the collection of the tax in an Eastern country.

"(b) We feel that it would be unwise to impose a tax of this nature until a substantial body of opinion in the Colony believes that the tax can be levied fairly and efficiently."

Should some of the misgivings regarding this proposal, which are indicated in the Taxation Committee's report, prove to be true, then the Colony might well suffer a setback from which it might take her a very long time to recover. At all events it is difficult to imagine a set of circumstances more unpropitious than that now obtaining for trying out an extremely controversial fiscal experiment, with its dangerous potentialities. The Chinese in the Colony, who constitute some 97% of the population, have, for over two years, been going through a severe financial strain in order to render badly needed ✓

assistance to their Mother Country in her hour of need. That there is a depressing uncertainty in the Colony's whole outlook is the authoritative view of the Financial Secretary himself. The fortuitous increases in the Colony's revenue serve but to cloak the unsatisfactory position of the Colony's economy. The flight to the Colony of "refugee" capital during the last two years or so is due no doubt to Hong Kong being "a free port, without income tax and without excessive taxation." Its maintenance in the Colony depends on a delicate equilibrium of confidence and of opposing and competitive financial attractions and drawbacks, which may easily be upset. With the dislocation and diminution of trade caused by the war, and by the necessary war measures; with unemployment caused by the closing down of enemy businesses; with a "dead" property market, and a "moribund" share market; with a low dollar and rapidly increasing costs of imported goods and a concomitant increase in the cost of living in general, and in face of reduced earnings—the outlook for the Colony is indeed bleak.

I am satisfied in my own mind that the Colony's contribution can be raised by other means without incurring the risk of "killing the goose that lays the golden egg". I may incidentally point out that other alternatives will obviate the expenditure of an annual sum of \$320,000.00 which would be required as administrative charges for the collection of income tax.

Sir, it is my personal conviction that income tax is not suitable for Hong Kong, and cannot be equitably administered; that administrative charges will be excessively high; that it will cause untold irritation and inconvenience to the public; and that it will do irreparable harm to the Colony. I am therefore opposed to its introduction.

May I, in conclusion, express the strong hope that Government will find it possible to adopt other alternatives, so as to enable the Colony to make, as a humble gesture of its loyalty and devotion to the common cause, a contribution which, though insignificant in terms of sterling and of the Imperial expenditure, should be all the more acceptable to the Mother Country because it has been raised by measures which command general approbation? (Applause).

THE FINANCIAL SECRETARY.—Your Excellency,—The Council has heard three speeches putting very ably certain objections to income tax and it seems desirable that the case which exists on the other side should be stated at this stage rather than at the end of the debate when there will be no opportunity of further rejoinder by any unofficial member. I regret that I shall have to take up a great deal of the Council's time but I do not apologise for it, because the issue is of such importance and complexity that it would be wrong to attempt to deal with it briefly. In fact I propose, with your permission, to refer not only to comments and suggestions which have been made in this Council but to others which have been given publicity elsewhere. If I reply somewhat caustically to some of the suggestions made in the Press I trust that honourable members will realize that I am not

suggesting that those are suggestions to which they would lend any support. Furthermore, any vigour I may use in expressing the case for this measure should be interpreted not as an indication that Government is determined to carry it through against all opposition, but as an attempt to convert opposition which is thought to be misconceived. Finally I want to show that the proposal was not brought forward without a due weighing of its consequences.

I start from the assumption which has been so fully confirmed by my honourable friends among the unofficial members that there is a general willingness and desire to contribute substantially to the revenue of the Government in order to enable the Government to lend assistance suitable to the resources of this Colony towards the prosecution of the war. I do not propose, therefore, to deal with the view expressed in some quarters, the upshot of which is that the Colony is not in a position to pay any extra taxation whatever. I cannot, however, allow to pass quite unanswered the attempt of my Honourable friend Mr. Lo to refute the statement that the Colony is lightly taxed. That statement is not intended to refer to the obvious fact that the taxation per head of population is a fraction of the taxation per head in the United Kingdom. That is inevitable because the standard of living of most of the population is so much lower. What is meant by the lightness of taxation here is a comparison between the taxes paid here and elsewhere by persons in receipt of comparable incomes. On that basis one has only to consider the various taxes one by one; the percentage of rent paid in rates is about one-third of the average in England; tobacco, liquor and petrol duties are lower than in England or in most Colonies; in the United Kingdom there is a general tariff, a standard customs duty of 10% on all ordinary imports, in nearly all other Colonies there is a similar tariff except that the rate is more often 15% and upwards, while here there is no general tariff at all; death duties are at a lower rate here than in the United Kingdom; Hong Kong has at present no Income Tax, whereas Income Tax in the United Kingdom rises from the standard rate of 7/6 to no less than 17/- in the £ on high incomes, and income taxes at various rates have existed for many years in a number of Colonies. It has been my business for years to study Colonial finances and without burdening the Council with more figures I can confidently assert that I know of no Colony where the general level of taxation in relation to income is lower and no more than one or two where it is as low.

It is also suggested that the level of taxation here is not low if judged in relation to social services. That argument refutes itself because if more taxes are paid naturally Government will be able to provide more social services. I have stressed that point on every occasion when discussing the financial position of the Colony. If Hon. Members want social services they must be prepared to pay for them.

In any case my Honourable friend has not pressed his view to the point of denying that the Colony ought to raise the revenue for war

purposes. I cannot emphasise too often the apparently general agreement on that issue because it relieves me of the necessity to answer such objections to Income Tax as that it will injure business by increasing charges and costs. That must be true of the raising of the same amount of revenue by any other means and if we are weighing income tax against other alternatives, objections of that nature must weigh down each scale equally. In fact, it is the general opinion of economists and is amply borne out by experience elsewhere, that income tax constitutes less of an addition to the true costs of a business than any other form of taxation.

One other suggestion which has not been put in its extreme form in this Council is that we are absolved from lending any more assistance to the Imperial Government because we make a regular Defence Contribution in peace time. In effect, Hong Kong is to be in the Empire on a basis of limited liability. What do honourable members imagine would be the effect if the taxpayer at home had said "we have paid to keep up an Army and Navy in peace time and we shan't pay any more now"? The present war would have been lost by now and if that policy had been pursued in the past there would have been no British Empire and no Hong Kong.

Turning more directly to income tax, a suggestion which has been given a good deal of prominence is that because the Colony is alleged to have been suffering during the last two years from trade depression consequent on the Sino-Japanese hostilities the imposition of income tax would be an intolerable burden. I find that argument almost impossible to understand. I am not going to discuss in detail whether there has been any such trade depression. The increase in the Colony's revenue by approximately 25% since 1937, and the increased dividends paid by practically all the local companies point in an entirely opposite direction. So does the analysis made by my Honourable friend Mr. Lo in his speech this afternoon, although I should like to make clear at once that I do not by any means accept all his conclusions. But if it were true that nobody has been making any profits for the last two years I cannot see where the burden of an income tax comes in. The great beauty of an income tax is that if you have no income you pay no tax, and if it were really true that the business man and the property owner had been making no profits the only people who would remain liable to income tax would be Government officials, for whom I am surprised to find such active public sympathy.

More seriously, the question whether profits are now as large as they were some time ago affects not the equity of the tax but its probable yield. If the gloomier views which have been put forward are justified Government may be disappointed in the yield, but those people who have not been making profits will not be called upon to pay any income tax. I would interpose at this stage that I can think of no other tax which could equally well be guaranteed to avoid hitting the unfortunate business man who has made no profit.

Another general complaint has been about the alleged unequal incidence of income tax. In this category are included a large number of complaints and objections on matters of comparatively minor detail, such as that the exemption limit is too low or that the personal allowances should be increased, or that other allowances should be given for various kinds of expenses or liabilities. Obviously no objection of principle can exist to making adjustments in those allowances if so advised by the very representative Committee which Your Excellency has set up to examine these and other details. If I may carry the war into the enemy's camp again, another beauty of Income Tax is precisely that such adjustments can be made in a way which is impossible with any other tax.

Questions have also been asked as to whether such and such perquisites of Government officials and others are to be taxed, for example, free houses. Provisions laying down the treatment of such perquisites are contained in the draft bill now being examined by the Committee, and if they are thought to be inequitable they can be changed. Other inquirers have asked whether the income tax assessment would include the squeeze upon which so many of us, official and unofficial, are popularly supposed to live. It is the dream of every zealous income tax official that he will some day find a conscientious burglar who will make a full return of the profits of his profession. I have no doubt that he would similarly welcome a full disclosure from the recipients of squeeze, but I fear that he will have to wait until those members of the public who claim to possess full information on the subject are kind enough to communicate it to the authorities. The other problems of assessment of income and allowances are primarily matters of the drafting of legislation and will no doubt receive the due attention of the Committee.

The third general class of comment relates to evasion. That people will try to evade taxation of any kind is certain, but there are means open to Government for detecting many kinds of attempts at evasion, and this matter also is largely one for discussion by the Committee which is examining the draft legislation. In the course of the long period during which income tax has been in operation in the United Kingdom, a very great variety of methods of evasion have been tried and a great many ways of detecting them have been developed. I do not suppose that the would-be evaders are going to publish their methods, but at any rate the methods announced by those persons who claim to be *au fait* with the intentions of the evaders are not different from the ordinary stock-in-trade of the tax dodger all over the world. I have never denied personally that this question of prevention of evasion is by far the greatest problem in the administration of income tax, whether here or anywhere else, but I see no reason why it should be less capable of solution here than in other countries. We are being constantly told that income tax has failed in this country or that. All I can say is that in those British countries where it exists to-day, that is not the official view; and there has been a

steady increase in the number of countries in which income tax exists and in the reliance which is placed upon it in those countries as one of the most important sources of revenue.

One further point on this matter of evasion. A good deal has been made of the point that at the present moment it is unsuitable to introduce Income Tax. Looking from the point of view of administration I am quite sure that war-time conditions and the war control of activities, business and otherwise, give the administration a great many more opportunities to detect evasion than they would have in ordinary times.

There is only one other thing which strikes me in this talk of evasion—it is notorious that other taxes are evaded to a greater or less extent: e.g. import duties on tobacco and liquor are certainly not 100% effective, and from time to time Government is obliged to institute prosecutions for failure to pay, say the stamp duties or wireless licences. It does not occur to anybody, however, to suggest that these taxes should be abolished because they are not quite 100% effective, and if the suggestion is made in the case of income tax I cannot but suspect that it covers some other motive.

A good deal has been made of the alleged enormous expenditure on the collection of income tax. The closest estimate of cost we can now make is something between 3 and 4 lakhs per annum, practically all of which, of course, will be for the staff required. This is in the first place a very small percentage of the expected yield. It will moreover in present circumstances be only to a small extent expenditure on new staff since we expect to draw the majority of the staff required from other branches of the Government service whose activities will have to be reduced to some extent and whose leave is, under present arrangements, being drastically curtailed, so increasing the number of available officers.

It is objected that the tax will cause a great deal of extra private expenditure particularly in the keeping of accounts and preparation of returns. The ordinary man will not need any expert assistance in the preparation of his returns unless he is seeking to avoid taxation. The officials of any income tax department run on the principles of the British income tax administration will be perfectly willing to give quite honestly any advice which may be required by the individual as regards the allowances to which he is entitled. As to business firms the extra expenses would be small except in the case of firms which do not now keep any accounts at all. For those firms I can only suggest that the necessity of compiling accounts for income tax purposes should be a blessing in disguise and not a matter to be regretted. I might here refute the general apprehension that the keeping of accounts in English and the rendering of returns in English will be obligatory; no such intention has ever existed.

The honourable the senior Chinese member has made comments on question of administration which form the main basis of his object in principle and which I therefore want to comment upon in some detail. First, with all respect, I do not believe in this mystery of Chinese accounting; nothing I have heard of it suggests that it is very different from the system adopted by small businesses in Europe as distinct from the complicated accountancy of big European firms; and the adjustment of such accounts for income tax is common routine. Secondly, I cannot follow him in his belief that humanity is divided into Chinese and the rest. The argument that income tax has never been successfully applied to Chinese is appealing, but what are the facts? As to China itself, it is surely obvious that the administration, for reasons I need not elaborate, is too weak to enforce any such tax; but there are other laws which are not enforced in China which we still make a fair show of enforcing here. As to Singapore, I have it on very good authority that the enforcement of income tax was never really seriously pursued. Lastly Mr. Chau has not mentioned one place where a large community of Chinese does, I am reliably informed, pay income tax and where the authorities have developed what they regard as a satisfactory system of examining Chinese accounts, that is the Netherlands East Indies.

There are a good many more detailed points I would like to take up with Mr. Chau if time permitted, I will only say that I am very hopeful that means could be devised of collecting the tax efficiently without prying into all the family secrets which he suggests the Chinese community would so much resent.

The last main group of objections to income tax are of a kind which Government ought to weigh very seriously, if they are in fact true: i.e. that the imposition of an income tax will drive business and capital away from the Colony. I may say that before the proposal was brought forward in this Council at all Government consulted certain leading business men and was assured that an income tax at the comparatively low rate proposed would not have any such effect. I still believe that that advice was entirely sound. Again I would like to remind honourable members that this is a tax on income and not a tax on invested capital as such or on the conduct of business as such. The imposition of income tax will impose no hindrance to the setting up of a business here, and if that business is not successful it will pay no tax. If it is successful I do not think that the man who started it will go away because he finds that he has to pay a proportion of his profits to Government. Again, that is not true of any alternative tax. Increased rates, a sales tax, higher charges for electricity and telephones would all be burdens on a new business from its very commencement and whether or not it was profitable. I am in fact amazed that it should be suggested almost in the same breath that Income Tax will drive away new factories and that some factories should be charged more for their electric power.

Hong Kong has had and still has certain advantages to offer to business and manufacture, i.e. security, almost unique harbour

facilities, an administration which we can claim to reach a high standard of honesty and impartiality, and freedom from irksome restrictions. These advantages will remain and when some of the wilder talk about the imposition of an income tax has died down I do not believe that the enterprising business man will refrain from coming here to make a profit merely because that profit will not be quite so large as it might have been. It is, however, alleged that the existence or prospect of an income tax will drive capital away from the Colony and is in fact doing so. There are few things about which more nonsense is talked than about capital being removed from a country. The bulk of the capital invested in Hong Kong is invested in property, and in plant and equipment of all kinds, for example, the cables of the telephone and electricity companies, which cannot very well be removed from the Colony. All that can happen to such property is that the owner of it can sell it to somebody else. The income from it, however, will remain liable to Hong Kong income tax if it is imposed, and it is a matter of indifference to Government whether that tax is paid by the existing owner or by somebody else who buys his property from him.

I do not deny that there are other kinds of capital which can be removed. The principal type of such capital is actual cash balances which may be placed on deposit with banks or other financial institutions and which undoubtedly have come to Hong Kong as a temporary safe resting place. It is obvious that a non-resident who holds such deposits in Hong Kong might be tempted to transfer them elsewhere if he had to pay income tax on the interest received from them, and the transfer of such deposits might do the Colony harm. For that reason the Bill which is now being examined by the Income Tax Committee provides that bank interest payable to non-residents shall be exempt from income tax.

It is alleged not merely that the existence of income tax will drive capital away in the future but that the prospect of it is already doing so. I do not know where that information is obtained. Movements of capital are notoriously difficult to detect and I can only go by such indications as are available. In the first place if a lot of people were selling Hong Kong dollars one would naturally expect the exchange rate to go down, within the limits permitted by our stabilization arrangements; in fact, however, anybody who has dealings in the exchange market will know that the effective market rate has been for many weeks at just about the highest point at which the banks can fix it under those arrangements. That does not indicate any flight from the Hong Kong dollar. Secondly, the returns which Government is now receiving of exchange transactions, details of which it is impossible to publish, do not indicate any such substantial flight. Thirdly, if a nervous shareholder were trying to avoid payment of income tax on Hong Kong investments he might be expected to sell his shares in Hong Kong companies. In the last four weeks the prices of the principal Hong Kong shares have moved hardly at all; but what movements have occurred show an average increase of about

1½%. These are the only indications from which I personally can form any judgment as to whether capital is leaving the Colony and they suggest that it is not. No doubt I shall again be told that a great deal is going on which Government does not know about and I can only repeat that it is impossible for the Government to know things if the people who claim to have the information do not take the trouble to communicate it.

It is, I believe, asserted in some quarters that our entrepot trade makes income tax unsuitable. I say asserted because I have never heard any attempt to prove or even explain the statement. I have heard the echoes of a good many discussions about introducing income tax in various countries and it is curious how unanimous the opponents always are that their particular country is so peculiar that what works elsewhere will not work there; but the common plea is rather the opposite of this particular theory. It is usually argued that income tax is not suited to agricultural countries but only to trading communities. Government is certainly not lacking in solicitude for the re-export trade, as our reluctance to impose the full system of exchange and import control demonstrates; and it is Government's view that the nature of our trade does make very undesirable many kinds of taxation and many restrictions, but I cannot see how that trade is damaged by a tax which imposes no hindrance whatever to the free inflow and outflow of goods but merely asks the trader to account in due course for the profits of those transactions.

For these reasons I am very strongly of opinion that the economic consequences of imposing an income tax have been enormously exaggerated. I am more inclined to believe that because exactly the same prognostications of disaster have been made repeatedly in other countries, without ever having been realised so far as can be shown by actual facts. Even with regard to the more fluid kinds of capital for which we have actually suggested special treatment it is extremely instructive to note that the high rates of income tax prevailing in the United Kingdom have never prevented enormous influxes of money to London when the nervous capitalist in Europe has thought that for the moment London would be a safer place to keep his money in than in any other financial centre. I believe that the capitalist is more interested in the security of his capital than in small variations in the net returns upon it and if the security of Hong Kong can be maintained, which after all is the fundamental reason for our selfish interest in the present war, I do not believe that capital will cease to come here.

Before leaving this aspect of the matter, however, I do want to emphasise that the Government is very ready to consider any modifications in the detail of an Income Tax which will minimise such economic dangers as exist. The Committee on the Bill has in fact already agreed upon one important recommendation with that end and I myself have in mind to propose others, e.g., some special concession to newly established factories. It is therefore possible to hope that whatever foundation those apprehensions had in fact will be further reduced when the draft bill emerges from the Committee.

This whole question of the economic effect, moreover, requires examination by comparison with the effect of the possible alternatives to an income tax, which is the last matter I want to discuss. The Government is very willing to consider such alternatives and certainly did not make the present proposal without having already considered a great many. I observe, however, that neither of my Chinese friends has made any specific suggestions for alternatives. I suspect that the honourable Mr. Lo, at any rate, remembers our discussions in the Taxation Committee, on which he rendered such valuable assistance, and fully realises the objections to other methods of taxation which led that Committee to advise unanimously that an income tax was in principle the best method.

Of the suggestions which have been put forward some are extremely wild, such as the proposal to repudiate Government's pension liabilities to the extent of 50%; others would be trivial in yield and expensive to collect, e.g. duties on cosmetics, a system of Government lotteries, etc. Still others while not hard to collect could not yield any very large sums. Among those I would include the suggestions of the honourable and learned the Senior unofficial member for surcharges on electricity, gas and telephone accounts. Of suggestions which are capable of yielding a ready substantial revenue I start with the introduction of a general customs tariff. The cost of a customs department would certainly not fall short of that of an income tax department, and I am sure that I should have the support of all the big business houses in saying that the introduction of such a tariff and the multiple restrictions its collection would entail would do more damage to Hong Kong trade, above all to its entrepot trade, than any income tax. It is a very important additional defect of a general customs tariff that it necessarily taxes people according to what they spend, not according to what they receive; and it therefore bears more heavily on the poor man whereas I think we should all agree that any new tax to be imposed should bear more heavily on the wealthier members of the community. That point had been very strongly urged by the Secretary of State. Precisely the same objection applies to the suggestion of a sales tax, which in addition I should expect to be peculiarly susceptible of evasion and particularly expensive to collect since it would involve detailed scrutiny of the accounts of all businesses including those innumerable small shops whose profits would be too low to bring them within the purview of an Income Tax department.

Proposals which have more to commend them in the way of simplicity are for further increases in the duty on liquor, petrol and tobacco. As regards liquor and petrol the main objection to any such increase is that there is a point at which increased duty leads to diminished consumption, and it is probable that we could not get a very much larger gross revenue from these duties than we expect to get as they now stand. The same applies in principle to tobacco, and there is the additional objection that that duty is in the main

paid by the poorer class of the community. In any case it is quite certain that any additional revenue that can be got from these duties would be very much smaller than the amount expected from income tax.

The honourable and learned member Sir Henry Pollock has suggested *inter alia* a tax on dividends of Hong Kong companies. I would submit three criticisms. First, is it equitable to tax the limited liability company and not the partnership, to tax capital invested in local companies and not capital invested in companies registered elsewhere? Second, what is to prevent such companies transferring their registration to Shanghai and paying their dividends there even if the profits are earned in Hong Kong? Third, and most important, it is one of the valid objections to income tax as a war tax that a part of the yield will be paid on income liable to United Kingdom income tax and will be recovered by the payers from the United Kingdom Exchequer; nearly all that income consists of dividends on Hong Kong shares, so that a very high proportion of our receipts from such a levy, probably 50%, would be drawn from the pockets of His Majesty's Government.

Finally, the simplest, and to many people the most attractive, method is to put it on the rates. That is certainly administratively practicable and the primary objection to it is on grounds of equity. It is suggested by many people that the addition to the rates would be borne by the property owner. I confess that it seems to me unfair that he should be expected to pay the whole sum required, while recipients of large incomes from other sources are to be allowed to escape scot-free, and at the same time it seems to be far more likely to prevent further investment of capital in the Colony, if it really is the case that the property owner would pay. In fact, however, I believe that a large part of such an increase in rates would be passed on to the occupier, i.e. once more in the main to the poorest class of the community. Moreover any increase in the cost of living accommodation will merely help to perpetuate the dreadful conditions of overcrowding which we all deplore.

The general objection to all these alternatives is that none of them approaches an income tax in the extent to which it can be adjusted to the capacity to pay of the individual, and, therefore in fairness of the distribution of the necessary burden of taxation. In that connection I suggest that there is something unfair in the criticisms of imperfection which are levelled against the suggested income tax. Because income tax professedly attempts to adjust the burden fairly in a way that no other tax pretends to do it is hotly criticised because it does not reach 100% fairness. I have already suggested that nobody thinks of demanding the abolition of other taxes because they are not free from evasion, and nobody thinks of abolishing the rates because the assessments do not correspond exactly with the periodical fluctuations in the actual rents of properties; but for income tax other standards are applied and it is practically

suggested that unless we can guarantee 100% efficiency it will be grossly inequitable even to attempt that fair distribution of the burden which is rightly claimed for it. If we are to choose between one kind of tax and another I would ask that we should not make the choice on grounds merely of convenience of administration. It is of very real importance that any tax of the magnitude we are discussing should be levied not merely conveniently but equitably, and should be placed on the shoulders best able to bear it. I believe that no member of this Council will venture to deny that income tax is best fitted to secure an equitable distribution of the burden, and I think it would be discreditable to us all if we were to falter in the attempt to secure that ideal of justice and equity because of minor difficulties and expenses of administration. I would like to close by pointing that sentiment with a personal example. It so happens that none of the alternatives which have been suggested here or elsewhere would call for any appreciable sacrifice on my own part; only an income tax will really hit me. The same must be true of many others in the higher income groups. Certainly I could not feel content if alternative taxation were adopted which merely diverted my share of the burden to others less able to bear it. (Applause).

HON. MR. S. H. DODWELL.—Your Excellency,—Though the Budget before us to-day is a heavy one considering the world situation, the explanations given to the Select Committee have satisfied me that it would be false economy not to proceed with the Public Works Extraordinary programme, unless our revenue shows signs of a serious decline. Should this occur, the contingency is satisfactorily covered by the assurance we have received that certain of these works will not be commenced without further reference to the Finance Committee.

At the same time, it is impossible not to be alarmed at the ever-increasing cost of Government, which in my view must continue to increase unless there is a radical change in the principles laid down for conducting the Colonial service. A system which renders it almost impossible to dismiss an unsatisfactory servant, and which adheres tenaciously to the practice of promotion by seniority, is bad enough, but when to this is added the inequality of the terms of service in the different Colonies, which renders most difficult the very desirable transfer of staff from one Colony to another, the Government in my judgment is saddled with three disabilities which would speedily ruin any ordinary business concern.

As Your Excellency is possibly aware, I have protested before now in this Council against the Government's policy of purchasing practically all their supplies through the Crown Agents for the Colonies, and very little through the local merchants who carry on the Colony's trade. The Government's reply is that the purchase of all Colonial supplies through one central organization is an economic and business-like procedure, and one which is adopted by all business concerns with branches abroad. In many respects I agree that this answer is unanswerable, and I am quite prepared to withdraw my opposition to

the policy, if only the Government would be businesslike in all directions. Some radical change in regard to the three disabilities I have mentioned seems essential, and would so increase the efficiency of the whole service that substantial reductions in staff and overhead would result.

With regard to this much vexed question of Income Tax, I have listened with great interest to my Unofficial colleagues' remarks, and to the very able reply of the Honourable Financial Secretary who, in spite of the disabilities surrounding the transfer of staff that I have just alluded to, has in some miraculous way arrived here, and if I may say so, is most efficiently carrying out the duties of a new broom. He is now quite rightly bent upon sweeping up part of our hard-earned incomes in order to devote them to the prosecution of the greatest of all causes, but he proposes to use a type of broom that some of us don't consider suited to the interests of the Colony.

As one of the business men originally consulted with regard to the imposition of Income Tax, I would say at once that my opposition to it did not arise until I later discovered the serious objections on the part of the Chinese community, who represent such a large proportion of our population. I was also a little misled by the fact that my Honourable friend, Mr. M. K. Lo, signed the Tax Commission's report, which, in spite of its qualifying remarks about Income Tax, I should hardly have expected him to do in face of the very decided views he now expresses.

I am at one with the Financial Secretary in repudiating the idea that the Colony's trade has suffered during the last two years. It has been quite abnormally prosperous, but is now showing very distinct signs of dwindling. During the last war, Hongkong's trade benefited rather than the reverse, but to-day there is so much Government control of imports and exports and exchange, not as much here as in other parts of the world, and so much uncertainty about the effects of the Sino-Japanese conflict, that it is impossible to form a reliable opinion about the future. In these circumstances I feel that it is an unpropitious moment to embark upon a doubtful experiment.

The Financial Secretary has alluded to the success which has attended the imposition of Income Tax in other places, and particularly mentioned the Dutch East Indies, where the Chinese are apparently paying up without demur. His reference to burglars reminds me of the well-known incident that occurred not so many years ago, of the wealthy Chinese merchant in Java who for years had been getting away with a return of 10,000 guilders a year, when his income was probably in the region of a million. The tax collection department at last in desperation raided his office and seized all his books. He promptly engaged an adept burglar, who stole the books from the collector's office and burnt them. He then sued the Government for the loss of the books and obtained damages. That, however, may be an isolated case, and in the event of Income Tax being introduced, I hope my honourable friend will not have to resort to such drastic measures.

I would like now to contradict the impression which seems to be circulating in the Colony that the Committee of the Chamber of Commerce, of which I am one, was neither in favour of making any contribution to the Imperial War Chest, nor of paying Income Tax themselves. Nothing could be further from the truth. The Committee was unanimously in favour of a substantial contribution, their share of which they have no desire nor intention to evade. Only two considerations weigh with the Committee: firstly, will the introduction of Income Tax drive Chinese industrial enterprise and capital away from the Colony and prevent fresh capital and industries coming to it, and secondly, will not the organization for collecting it prove too costly?

The Committee's answer to both these questions was in the affirmative. We attached little importance to the danger of industrial enterprise being driven away from the Colony, for the single reason that most of it derives considerable benefit from Imperial Preference, but we came to the unanimous conclusion that the risk of a flight of capital was a very real one which should not be taken if our war contribution could be collected in some other way. In our position as a storage, distributing, and financing centre, with no mineral or agricultural wealth to speak of, we are on an entirely different footing to Ceylon and other Crown Colonies which have introduced Income Tax. Our trade is very largely dependent upon cheap money. In my own experience it has suffered very seriously on many occasions before from flights of capital, when interest rates have risen to 7% and 8% and seriously affected all industry and trade. In the light of the strenuous opposition of our Chinese colleagues who fear that it will have this effect, I personally feel that it might be a dangerous experiment.

This may seem strange advice from one whose Company is registered at Home, pays Home Income Tax and Excess Profits Tax, and on this account was at a serious disadvantage during the last war. Nevertheless, it is my considered opinion unless we can get over the Chinese objections. I recognize that none of us should rightly pass final judgment upon the subject until the Bill is before us and we know its terms. The Committee now sitting may succeed in devising some method of making it less objectionable to our friends. Under their terms of reference it is difficult to see how this can be achieved, but if it can, then the main objection I have to Income Tax will disappear.

There is another point which needs serious consideration before setting up an expensive collection department, which, if it is to do its work thoroughly I fear will almost certainly cost more than the four lakhs mentioned by the Hon. Financial Secretary. I doubt if the Government really appreciates how large a proportion of the tax, if applied throughout the Colony, would have to be refunded by the Home Government. I estimate that six large British concerns, apart from the purely local limited companies, would contribute a very

substantial proportion of the tax collected from European British companies, and the great majority of their shareholders are in the United Kingdom.

Finally, Sir, I realise only too well that opposition to Income Tax at the present moment sounds extremely unpatriotic, no doubt particularly so to my Honourable friend the Acting General Officer Commanding, and the Services generally, who pay their 7/6d.

So far as the European Britons in the Colony are concerned, I am confident that they are fully prepared to accept their responsibility in this matter and that all would gladly make their contribution through the medium of an Income Tax, provided that reasonable allowances are made, and that the tax is for the duration of the war. From what my Chinese colleagues have said, it is clearly not the payment of the contribution to which they object, but to the method of its collection. Conceivably, of course, the danger of a flight of capital may prove an exaggerated bogey. We undoubtedly have a magnificent harbour and many attractions and facilities to counteract the imposition of the tax, but from my thirty years' experience of how little it takes to upset the delicate economic equilibrium of this Colony, I am convinced that there is a grave element of risk, and that in view of the difficulties of trading we are likely to have to contend with, it is one we should not take unless the Committee now in session can make the Bill palatable to the Chinese community. (Applause).

HON. MR. LEO D'ALMADA E CASTRO, JNR.—Your Excellency, —In view of present circumstances I do not propose to criticise the Colony's ordinary budget insofar as its public works expenditure is concerned, because at a time like this, when, as I believe, economy should be the watchword, whatever disappointment one may feel over the programme of public works must be borne in silence. But for the same reason I would be failing in my duty were I to pass over the figures connected with administration costs.

More than one Unofficial member has in past years called these figures astronomical, and the epithet is more apt to-day than ever. One realises that with a growing Colony must of necessity come a certain increase in the personnel of administration and consequently in its cost. The objection lies not to this but rather to the fact that in recruiting its officers, Government does not give the Hong Kong man the chance he deserves. I had occasion last year to complain that local men were not employed in the service as much as they should be. If reform in that direction was desirable then, its need to-day is more evident than ever, on the score both of fairness to the community and of keeping down expense. Government might well consider also the payment on a dollar basis of those of its junior officers who are engaged locally and who, while on probation, are paid in dollars. In their case there is no justification for an automatic transfer to sterling when they have proved satisfactory. Conditions

are such all over the world to-day, and the amenities of life in Hong Kong are so much greater than they were say thirty years ago, that such a policy would not result, as might be feared, in discouraging the right type of young man from joining. I am confident that on this much more economical basis, which would mean a saving both in actual pay and in passages, there would still be eager seekers after posts from the ranks of those who have spent their youth here and are the product of our local schools.

So much for our ordinary Budget. On the subject of the War Budget I am, like the rest of my unofficial colleagues, strongly opposed to the proposed taxation of incomes for reasons which I shall give later. Before doing so, however, let me make it clear that, as in the case of my colleagues, my objections do not arise from self-interest. Nor are they voiced on behalf of the Portuguese community. From the personal standpoint, indeed, few measures could be more welcome—it is obvious that the legal profession stands to gain considerably from its introduction, lawyers probably coming next after chartered accountants as persons whose assistance must of necessity be invoked by the taxpayer, whether he be willing or loth to pay. Were I actuated by selfishness, therefore, I would urge its immediate adoption. As for my community, so far as I can judge from a preliminary examination of the draft bill, the scale upon which it is proposed to base the tax, together with the numerous allowances, ensures that few will be hard hit, apart altogether from the fact that we desire, as does everyone who has enjoyed the protection of the English flag and the privileges of living within the Empire, to help as much as we can in this War.

The novel arrangement of the interposition of the Honourable the Financial Secretary's speech between those of Unofficials and with it his invitation for a rejoinder call for a reply to his arguments by those following him. Some of his remarks make it clear that he is enamoured of the measure. He talks about the beauties of the tax. We on our part regard it as his ugly duckling and, if I may be permitted to mix my similes, metaphors and proverbs rather thoroughly, we think it is not only an ugly duckling but a vicious one which may well attack and injure the Hon. Mr. M. K. Lo's goose that lays the golden eggs. The points made by the Financial Secretary are numerous, and to deal with each of them would necessitate more time than the circumstances allow of. But it must not be supposed that, because I do not reply to them, I accept his arguments. I think it would be better to confine myself to my main objections to the tax.

I object to this proposed tax, Sir, for three reasons. The first is the attendant danger, already mentioned, of the flight of capital from this Colony. While not convinced that this is the inevitable result of income tax, I am nevertheless certain that it is a danger well within the bounds of possibility, and once this is admitted, and it cannot be denied, then there can be no question but that a measure involving this risk is one that should be resorted to only when all other means of raising money have been tried and found wanting.

That this is far from the case is obvious from the numerous alternatives suggested to Government by representative and responsible bodies in this Colony, by the press, and by individuals sufficiently alarmed at the prospect to have filled the correspondence columns of more than one local paper during the last few weeks. It must be remembered, as has been mentioned more than once since this tax was first mooted, that it is not being imposed on a colony enjoying a period of normal commercial prosperity. The "prosperity", if so it may be called, of the last two years or so, has been artificially brought about, and no one would care to predict its continuance for any length of time. Our outlook is, at best, uncertain, and the most confirmed optimist cannot pretend that the present state of Far Eastern affairs does not give rise to serious misgivings in our part. Government in these circumstances must do nothing from which may arise a risk to the Colony's future.

I have two other, and these perhaps secondary, objections to income tax. One of them is the strong probability that in a mixed population such as ours, it will be found impossible to administer it equitably, so that while some will bear the full burden of it, others, and they are the vast majority, are so placed as to be in a position easily to escape it. And there is no reason to suppose that they will not avail themselves of this escape. My third objection is the necessity for the creation of a new administrative department, not only because of the cost but because of its inevitable liability to bribery and corruption. I have in the past criticised the Police and Revenue Departments in regard to this. Prosecutions of members of the departments show that I am justified in my criticisms. An Income Tax Department, once created, will quickly earn for itself an unenviable reputation for the same failing.

These in brief, Sir, are my objections to this proposed tax, and I have voiced them with the less hesitation because in doing so I am echoing the opinions of business men, men with years of experience in the commerce of this Colony, men who have come into more frequent and closer contact with the Chinese business community than any member of Government has come or can hope to come. Above all, Sir, I am convinced that in voting against this measure I am doing right by our Colony because the Chinese members of this Council, who represent a community without which we could not hope to exist, have expressed themselves strongly against it. When a measure of this kind, and of such vital importance to Hong Kong, meets with opposition from so large and important a section of its population, when that opposition is based, as in this case, not on any unwillingness to contribute towards the cost of the war, but on reasons sincerely advanced, when there are available alternative methods of taxation, less expensive and probably more speedy of yield, then, Sir, prudence surely counsels its abandonment.

We are told, Sir, and we like to believe, that this is a war to make the world safe for democracy. If Government, by use of its official majority were to impose upon this Colony a form of taxation

against which the representatives of the people, if I may so call the unofficials, have expressed themselves so strongly and so unequivocally, it would be a sad commentary indeed on rule by the people. (Applause).

H.E. THE GOVERNOR.—Before calling upon other Unofficial Members to speak, I would like to make it quite clear that there is no question of calling upon the official majority to support a measure which would extract from this Colony a gift to the Imperial Government.

HON. MR. A. L. SHIELDS.—Your Excellency,—I have no comments to make on any of the items in the Estimates now before us but would express some concern that the estimated Revenue to meet the Expenditure is based on returns for the current year and in anticipation of these figures being maintained.

While I am in no way despondent about the ultimate future of the Colony I must voice the views held by the General Committee of the Chamber of Commerce that future Revenue may be seriously affected by the continuance of the closure of Chinese ports, the advent of the War which with possible trade restrictions for the conservation of currency, Government interference with the free movement of trade by the use of import and export permits, the stoppage of trade with Germany and the reduction of Steamship space available at much higher freight rates.

The burden of expenditure for cost of Government still grows like the "green Bay tree." Pensions and Emoluments are increasing, we have to provide for large sums for social services, Defence etc. and necessary Public Works have to be postponed in spite of our inflated revenue due to unusual conditions which even the most optimistic can hardly expect to continue without a serious dip in the curve.

The Unofficial Members of this Council welcome the assurances given by Government that a number of the schemes for which preliminary grants have been made will be reduced or deferred if Revenue shows signs of decreasing.

It is true there is always the taxpayer to fall back upon and you, Sir, stated in your speech on the 12th of October that this Colony is lightly taxed. Any taxation which can be avoided is an unnecessary burden on the Community. The taxpayers capacity to pay is not unlimited and in a serious depression such as we have seen periodically, heavy taxation will tend to make the taxpayer fold his tent and imitate the proverbial Arab. It will certainly keep out new capital and new industry, and a vicious circle on the downward track may well cause future Governments much heart burning and anxiety.

When China reopens to normal trade much of the money now here may seek investment and business opportunity elsewhere. The improving facilities in neighbouring ports and the possible provision in

these ports of duty free zones will be in direct competition with Hong Kong.

It may be said that Hong Kong will always be attractive on account of the security offered but I believe the old order in China is over. The new China will be run by Officials whose increasing patriotism will oblige them to do the best they can for their own people. With merchants who are second to none in business acumen and financiers and bankers who are becoming more experienced in the handling of their country's affairs, outside traders will have to look to their laurels.

Hong Kong's phenomenal growth was due to the influx of Chinese attracted by the cheap facilities of our free port, low taxation and security.

Let us beware lest we find ourselves with little to offer but security. Let us look over our stock in trade and see what else we have to offer; the answer is Service but it must be at a competitive price. Low taxation with its corollary, low cost of living should be the aim of this and future Governments.

I make these general remarks, Sir, as some of my Unofficial Colleagues are dealing with specific items in the Budget.

I have nothing further to say on the War Budget as it has already been fully covered by the Hon. Mr. Dodwell and my other Unofficial colleagues, except to remark that the interjection of the Financial Secretary's speech in the middle of the Debate is rather upsetting, and I hope time will be given to make a rejoinder. It is impossible to do so now, but I hope there will be a chance later on to deal with the Financial Secretary's Statement. (Applause).

ADJOURNMENT.

H.E. THE GOVERNOR.—The time is now five o'clock and obviously we cannot get through all the business before us to-day. As I have already explained to the Council, I have, unfortunately, an engagement which I should be very sorry not to attend. It is to review the Police Reserves. I will, therefore, adjourn the meeting until Monday next.

Before I do so, I should like to answer the point raised by Mr. Shields as to a rejoinder to what the Financial Secretary has said. Of course I cannot break the rules of debate which are laid down here and which do not allow a member to speak twice on a subject, but there are still unofficial members who have not spoken and who will have the opportunity of making the rejoinder. The practice of allowing members to know something about the Government's case before they make up their minds about it is not one that should be condemned. This is the only Legislative Council in the Empire, so far as I know, in which it would be apart from ordinary procedure for an official

member to intervene in the debate in order to answer criticism of the Government's proposals. Thus it may eventuate that members finish speaking before they have a true conception of Government's case.

I think it is only fair to unofficial members that at a certain stage of the proceedings, after some kind of case has been made against a Government motion, a Government official should stand up and state the other side. It does give unofficial members an opportunity for the rejoinder which Mr. Shields rightly desires to be given.

I should like to see this procedure adopted by this Council as is done in other Legislative Councils in the Empire (of which I can say I have a good knowledge) so that a debate should be fairly free and—to put it rather tritely—members should know what they are talking about. I wish to emphasise that I do not say this with any intention of being rude; my point is that it is desirable that the Government case should be clearly put before members so that they know what they are opposing—if they are opposing. I shall, therefore, continue on every occasion, where I consider it helpful to the Council, to call at some stage, upon a Government official to reply to the criticisms that have been raised. I trust all members will agree that this is the right way to treat a debate.

Council stands adjourned until Monday next at 2.30 p.m.
